

NSW BUILD-TO-RENT – TREASURER'S GUIDELINES AND PLANNING LAW DETAILS RELEASED

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OVERVIEW

In late July 2020 the New South Wales Government announced it would provide duty and land tax incentives for qualifying "build-to-rent projects". Qualifying projects must meet conditions set out in the Treasurer's Guidelines. Those Guidelines were first published on 12 February 2021.

The incentives include:

- a 50% reduction in the taxable value of the land (reducing the land tax otherwise payable at general rates)
- an exemption from "surcharge land tax" (the foreign investor land tax surcharge on residential property)
- an exemption from "surcharge purchaser duty" (the foreign investor duty surcharge on residential property).

The concessions are offered for a maximum period of 20 years, expiring in 2040. The Chief Commissioner of State Revenue can later claw back the concessions if key conditions are not satisfied for a period of 15 years – see below for further details.

LAND TAX REDUCTION – ELIGIBILITY REQUIREMENTS

The value of the land on which a build-to-rent property has been constructed will be discounted by 50% if:

- a building is situated on the land;
- construction commenced on or after 1 July 2020; and
- the Chief Commissioner is satisfied the building will be used and occupied as a "build-to-rent property" in accordance with the Treasurer's Guidelines.

It will be necessary for the land owner to apply to the Chief Commissioner for the reduction. If the relevant land will only be used and occupied partly for a build-to-rent property, the concession may be available on a pro rata basis – see further below for details.

THE TREASURER'S GUIDELINES

The Treasurer's Guidelines set out when a property is being used and occupied for a "build-to-rent property". The following is a summary of the Guidelines.

1. *There must be a "building" on the property*

- This can include a group of building or parts of buildings on the same parcel of land.

Note that the build-to-rent property cannot be subdivided for a period of 15 years.

2. *Planning Requirements*

- All relevant development consent requirements must be complied with as well as any relevant affordable housing policies under the *Environmental Planning and Assessment Act 1979 (NSW)* (Act).
- The new *State Environmental Planning Policy Amendment (Build-to-rent Housing) 2021* was made and came into force under the Act on 12 February 2021. This operates to:
 1. Make certain build-to-rent housing 'State significant development' for which the consent authority is a delegate of the Minister for Planning and Public Spaces. This includes build-to-rent housing outside of the City of Sydney where:
 - a) the capital investment value is more than AU\$100 million for projects in the Greater Sydney Region or more than AU\$50 million for all other projects;
 - b) the tenanted component is at least 60% of the capital investment value; and
 - c) the development is not prohibited under any other environmental planning.
 2. Amend *State Environmental Planning Policy (Affordable Rental Housing) 2009* to include a number of specific provisions for build-to-rent housing. These include:
 - a) Making build-to-rent property development permitted with development consent on any land on which residential flat buildings are permissible as well as on land zoned B3 Commercial Core, zone B4 Mixed Use and zone B8 Metropolitan Centre;
 - b) Restricting the application of the build-to-rent provisions to properties containing at least 50 dwellings for residential lease on the same lot of land;
 - c) Restricting the subdivision of build-to-rent properties for a period of 15 years from the date an occupation certificate is issued (other than in zone B3 where the subdivision prohibition continues in perpetuity);
 - d) Specifying a number of non-discretionary building standards for build-to-rent housing, including for building height, floor space ratio and parking;
 - e) Allowing for the flexible application of the design criteria in the Apartment Design Guide under *State Environmental Planning Policy No 65—Design Quality of Residential Apartment Development*, such as requiring the consent authority to give consideration to the amenities proposed to be provided to tenants though common spaces and shared facilities; and
 - f) Requiring that the ground floor of build-to-rent developments located in business zones contain active uses that encourage interaction between the inside of the building and adjoining external public areas (and not residential accommodation or car parking).

3. Building Requirements

- The buildings on a parcel of land must contain at least 50 self-contained dwellings used specifically for the purpose of build-to-rent.
- The property must comply with affordable housing policies that may be imposed under the *Environmental Planning and Assessment Act 1979*, including any state environmental planning policies made from time-to-time to promote the development of affordable or social housing.
- The build-to-rent dwellings must be available to the general public without restriction (other than those required for public health and safety, or to promote announced Government policy, or to ensure designated affordable and social housing is used for that purpose).

Note that it is permissible for the build-to-rent dwellings to be spread across multiple buildings on the same parcel of land. Further, if an adjacent land parcel is consolidated with a land parcel that already qualifies as a build-to-rent property, it is not necessary for any additional build-to-rent dwellings on the adjacent land parcel to also meet the 50 dwelling threshold to qualify for the concessions.

4. Ownership Structure

- The dwellings and common land comprising the build-to-rent property must be held within a unified ownership structure, which can include a group of entities holding joint ownership. However, it is not permissible for the structure to provide a de facto subdivision or divided ownership of the build-to-rent property.

5. Management Structure

- The build-to-rent property must be managed by a single management entity, with on-site access to management for tenants.
- The management function can be outsourced to a third party – it does not need to be undertaken by the landowner.

It is important to note there is an exemption from the above management requirements for specific build-to-rent dwellings that are made available for use as affordable or social housing for a continuous period of 15 years.

6. Lease Conditions

- Each tenancy with a build-to-rent dwelling must be subject to a Residential Tenancy Agreement under the *Residential Tenancies Act 2010*. The landlord must comply with all requirements of that Act.
- Tenants must be offered a range of lease terms, including a genuine option to enter a lease for a fixed term of at least three years. However, a landlord will not be in breach of this requirement if a tenant who is made the offer of a fixed three year term opts for a shorter period instead.

7. Other Factors

As a "catch-all", the Chief Commissioner may have regard to any other factors that he or she considers relevant in determining whether a property is being used for build-to-rent. It is expected that Revenue NSW will release public guidance on how it will administer these concessions.

PROPORTIONATE REDUCTIONS IN LAND VALUE

If the whole of a parcel of land is used for build-to-rent purposes, the land tax concession should not be reduced. This is notwithstanding the parcel may not be wholly used for build-to-rent dwellings. The Treasurer's Guidelines include examples of where this may be the case, including where part of the property is reasonably used for on-site management accommodation and facilities necessary to operate the build-to-rent business.

However, if a part of a parcel of land is not used for build-to-rent purposes, the value of land tax concession will be reduced. This will be relevant if part of the parcel will be used for retail or other purposes. The reduction may be calculated on a basis the Chief Commissioner considers appropriate. The Guidelines suggest that floor space and area may provide a reasonable basis of apportionment.

SURCHARGE LAND TAX EXEMPTION – ELIGIBILITY REQUIREMENTS

The eligibility requirements for the land tax reduction outlined above act as a "gateway" for the surcharge land tax exemption. The owner must first be entitled to a land value reduction under those provisions before the surcharge land tax exemption can apply.

The exemption applies to land owned as at midnight on 31 December in a year (the "taxing date"), starting with land owned as at midnight on 31 December 2020.

The additional eligibility requirements for the surcharge land tax exemption are that:

- the owner of the land must be an "Australian corporation"; and
- there must be a building that is a build-to-rent property on the land; and
- that building must have been constructed by the owner or a related body corporate.

Note that the building can be constructed either before or after the taxing date (meaning a refund may become retrospectively available).

The exemption will apply for a maximum period of 20 years. It will not apply to land owned as at midnight on 31 December 2040.

SURCHARGE LAND TAX – EXEMPT PERSON

The Chief Commissioner may approve a "foreign person" as an "exempt person" for particular land if the Chief Commissioner is satisfied that person is likely to be entitled to a surcharge land tax refund. This allows the exempt person to claim the exemption without having to first pay the surcharge land tax and then seek a refund.

The approval may be subject to conditions.

SURCHARGE PURCHASER DUTY – ELIGIBILITY REQUIREMENTS

Once again, the eligibility requirements for the land tax reduction outlined above act as a gateway to the surcharge purchaser duty exemption. The transferee must be eligible for a land value reduction under those provisions before a surcharge purchaser duty exemption can apply.

The additional eligibility requirements are that:

- the owner of the land must be an "Australian corporation"

- the transfer must have been entered into on or after 1 July 2020 (but a transfer made after that date, in conformity with an agreement for sale or transfer entered prior to that date, will qualify).

SURCHARGE PURCHASER DUTY – REFUNDS

If surcharge purchaser duty has already been paid, and the eligibility requirements are satisfied, the owner will be entitled to a refund.

This refund must be applied for:

- within 12 months of the Australian corporation first becoming entitled to a land tax reduction; and
- no later than 10 years after completion of the transfer to the Australian corporation.

The refund may be for the full surcharge purchaser duty amount paid or a lower amount as set out in an order made by the Treasurer.

SURCHARGE PURCHASER DUTY – EXEMPT TRANSFEREE

The Chief Commissioner may approve a person as an "exempt transferee" for a particular transfer (or class of transfers) if the Chief Commissioner is satisfied that person is likely to be entitled to a full surcharge purchaser duty refund. An exempt transferee does not need to pay the surcharge purchaser duty and then seek a refund.

The approval may be subject to conditions.

THE CLAW BACKS

As noted at the outset, all of the above exemptions and concessions may potentially be cancelled and clawed back if, within a period of 15 years after the land tax reduction first becomes available, the land is subdivided or the ownership of the land is otherwise divided.

Further, there may be claw backs if approvals were provided on a conditional basis, or undertakings were provided, and those conditions have not been satisfied or the undertakings were breached.

In addition to any tax or duty that may be payable as a result of a claw back, penalties and interest may apply.

WHAT ABOUT LAND ACQUIRED AND OWNED BY FOREIGN TRUSTS?

As explained above, the surcharge land tax and surcharge purchaser duty exemptions require the land to be acquired and owned by an "Australian corporation".

We expect that this requirement can be satisfied where the Australian corporation acquires and holds the land as trustee, but this will need to be confirmed with Revenue NSW.

A similar issue may also arise where the land is held by an Australian corporation as bare trustee (nominee / custodian) for a foreign person. This is a common structure for REITs.

In relation to the surcharge land tax exemption, we note there is the additional requirement that the building be constructed by the Australian company or a related body corporate. This may suggest that the exemption won't be

available where land is held by a bare trustee that does not itself (or via a related company) undertake the construction.

To provide certainty, it will be important for Revenue NSW to publicly set out its views on these issues.

WILL LANDHOLDER DUTY AND SURCHARGE DUTY APPLY?

Surcharge duty may also be payable in addition to landholder duty if a "relevant acquisition" is made in a private landholder that has a residential land holding in New South Wales.

The surcharge purchaser duty exemption is limited to transfers of residential-related property. It does not appear to extend to surcharge duty on a relevant acquisition in a private landholder.

This may be relevant if the investors in an Australian company that owns a qualifying build-to-rent property exit the project by selling their interests in the company. The incoming investors may potentially be liable for both landholder duty and surcharge duty.

K&L GATES' COMMENTS

The release of the Treasurer's Guidelines is welcome. It provides a degree of certainty to those developers and institutional investors who are considering undertaking a new build-to-rent project in New South Wales.

However, the Guidelines do significantly narrow the categories of build-to-rent projects that will qualify for the concessions. Specifically, the requirement for tenants to be offered a Residential Tenancy Agreement likely means that the concessions will not be available for "commercial residential premises" (such as serviced apartments, boarding houses and co-living developments) where residents are more likely to have a licence to occupy their accommodation in form of a rooming agreement.

Similarly, the fact that the dwellings must be offered to the general public (except in limited circumstances, such as for affordable and social housing) likely means that a qualifying build-to-rent project cannot be exclusively targeted at specific classes of residents (such as retirees or students).

While these incentives will assist qualifying projects, institutional investors will also need to take into account other tax obstacles for build-to-rent projects, including GST. For foreign investors, the lack of Managed Investment Trust concessions for residential rent may also be a factor.

Given the strict requirements, qualifying projects will need to be approached holistically having regard to the ownership structure, management structure, lease tenure and resident profile, financing requirements, planning requirements and construction issues. For foreign investors, there will be additional considerations in respect of FIRB and cross-border tax.

It is worth noting that the New South Wales Government is separately considering abolishing stamp duty and land tax in favour of a new annual property tax. However, those reforms (if implemented) are unlikely to apply to high value residential development sites for a number of years (to protect Government revenues during the transition period). Accordingly, the build-to-rent incentives set out above are likely to be the only state tax concessions that are available in New South Wales for build-to-rent projects over the next few years (and possibly longer).

FOOTNOTES

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