BTR SERIES PART 4: AFFORDABLE HOUSING AND KEY WORKER HOUSING—WHAT ROLE DO THESE PLAY IN THE BTR SOLUTION?

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Australia is currently experiencing a national housing affordability crisis that continually worsens. One solution to the urgent need for more social and affordable housing lies in the build-to-rent (BTR) model.

DEFINING AFFORABLE HOUSING

In Australia, “affordable housing” does not have a common meaning across jurisdictions or government programs. Affordable housing is typically defined as a rental property that is priced so that low to moderate income households are also able to meet other basic living needs. Whilst some jurisdictions define “affordability” based on a household's ability to pay as determined by the income in that household, other jurisdictions define affordability as rent that is lower than the prevailing market rate.

If Australia is to embrace the BTR sector, with affordable housing as part of the model, affordable housing should be clearly defined in each government program and for each project prior to funding in a manner that is consistent and clearly specifies for whom the affordable housing is being delivered.

DEFINING KEY WORKER HOUSING

“Key worker housing” targets key workers who provide an essential service in industries such as health or education. These workers are typically on moderate incomes and may not be able to afford housing near the location of their employment. Rental subsidies for long-term rental units allow these individuals to reside in locations that would otherwise be unaffordable so that they can service the community.

IS AFFORDABLE HOUSING OF ITSELF A CHARITABLE ACTIVITY?

The application of charity law to housing providers is critical, as a range of tax incentives, including goods and services tax (GST), duty, land tax, and income tax, are dependent on this analysis. The Australian Charities and Not-for-profits Commission has set forth an interpretation statement on the provision of housing by charities. In this statement, the commissioner notes that the fact that a government has created a housing scheme does not necessarily mean that providing housing under the scheme is “charitable” under the *Charities Act 2013* (Cth). Accordingly, affordable housing of itself may not be charitable, as it is generally provided to key workers who do not require housing for the “relief of poverty.” This can be an issue for community housing providers (not-for-profit organisations who manage and maintain affordable rental housing for tenants in local communities across each state) that are considering establishing special purpose vehicles to undertake certain affordable housing projects.

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BENEFITS OF AFFORDABLE HOUSING AND KEY WORKER HOUSING IN THE BTR MODEL

With each day, more population groups are affected by the rising cost of living in Australia. As a result, access to housing that is affordable in the community has been significantly impacted. The clear benefit to integrating affordable housing and key worker housing into the BTR model is that it provides affordable living options for individuals on low to moderate incomes. As noted above, it also allows essential service workers to live close to their employment even where those are in less affordable neighbourhoods that require critical services.

The National Housing Finance and Investment Corporation (NHFIC) plays an instrumental role in the BTR model, as it provides concessional finance options to BTR developers to support affordable housing and key worker housing. There are also government subsidies and financial incentives that can be provided to developers to cover the deviation between market rent and rental rates under an affordable housing regime. If the government incentives have the desired effect, the government will be under significantly less pressure to directly fund and build new dwellings.

Some of the key financial incentives will be tax related. In Part 2 and Part 3 of this series, we discussed some of the issues that arise, including the proposed reduced withholding tax rate for qualifying BTR projects held within managed investment trusts. Further, GST reforms to address upfront GST leakage (irrecoverable GST costs on land and acquisition) would greatly encourage developers to undertake BTR projects.

Social infrastructure is also a key consideration for investors—certain Australian superannuation funds have embarked on BTR projects that include affordable housing or key housing in light of delayed government expenditure and population and migration growth. Certain superannuation funds have mandates for affordable housing and key worker housing. In addition, there is an incentive for Australian super funds to participate in key worker housing, as in certain instances, key worker members of the super fund may be given preferential access to the accommodation.

The use of incentives to encourage the expansion of affordable housing in a multifamily context has been widely implemented globally. In the United States, incentives such as tax credits for low-income housing decrease the amount of funds required to be borrowed by developers and enable developers to provide affordable rents to the community.

It is also worth noting that, in the United States, grants or low-interest loans are provided to developers to encourage the development of low-income housing. For example, close to half of all multifamily mortgage debts in the United States are said to be backed by US federal government agencies such as the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, and the Government National Mortgage Association (colloquially known as "Fannie Mae," "Freddie Mac," and "Ginnie Mae" respectively). We will talk more about this in Part 5 of our series, regarding debt financing for BTR projects.

The United Kingdom also has a variety of incentives, such as the Affordable Homes Guarantee Scheme, that support the delivery of homes to low-income families. Developers in the United Kingdom also receive financial incentives such as grants and tax breaks to encourage the development of properties for social rent.

Notably, section 106 agreements in the United Kingdom allow local governments to negotiate with developers more flexibly outside the regular planning regime - this ultimately encourages the creation of developments that support low-income housing.

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CHALLENGES IN DELIVERING AFFORDABLE HOUSING SOLUTIONS

At this time, there are several hurdles to delivering affordable housing in Australia. The first of which is that BTR projects with affordable housing components may be taxed at the same rate as other asset classes that provide stable returns for investors. Specifically, land tax may apply at the same rate as for commercial or industrial premises (although a few states have now introduced some specific BTR concessions to address this - see Part 3 of this series for more detail on indirect taxes).

Whilst affordable housing may be managed by private companies as well as community housing providers, only registered providers receive support from the federal government. There is also additional cost and complexity tied to affordable housing resulting from a duplication in services (i.e., property management) due to the requirement that affordable housing dwellings must be managed by a community housing provider. Notably, key worker housing does not require oversight from community housing providers, which can streamline costs tied to the project.

Obtaining the required capital to fund affordable housing in a BTR development can also pose a significant challenge. Whilst concessional funding from sources such as NHFIC as noted above are available, corporate investors may set additional milestones, which can be difficult to achieve in light of the subsidised rental rates provided under affordable housing and key worker housing regimes.

REFORM REQUIRED

Ultimately, reform is required at the federal, state and local government levels to incentivise investors to enter the BTR sector. Additional incentives and supporting regulatory policies are necessary for BTR projects to be deployed at scale. As set out in Part 2 and Part 3 of this series, tax will also play an important part in the incentives that are required.

Beyond tax, incentives such as access to government land, density bonuses, and rental top-ups must also be provided to developers so that they can achieve their investor return requirements and feasibility targets.

In addition, state and local government reform is required to modify planning mechanisms and zoning regulations so that BTR projects can be developed at a more profitable level. Currently, the approval process for BTR developments is expensive, as approval times are often extensively delayed. It is critical that state and local governments immediately rectify this issue and streamline the planning approval process for BTR projects.

Ultimately, the Australian Government must not only take steps to ensure an increase in affordable housing and key worker housing, but it must also ensure that the appropriate supply is sustained over decades to protect future generations.

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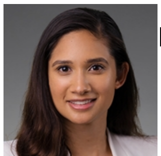

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