# Federal Budget Changes Will Impact Property Buyers, Investors

2017-18 federal budget confirmed some policy changes that would impact property buyers, landlords, developers, and investors.

Listed below are some of the key changes you need to be aware of:

## CGT changes for foreign investors

The Government announced that foreign and temporary tax residents will not be able to access the CGT main residence exemption from 7:30 pm (AEST) on 9 May 2017 (existing properties held prior to this date will still be eligible for the exemption until 30 June 2019). From 1 July 2017, in relation to the Foreign resident capital gains withholding (FRCGW) rules: the rate of withholding will be increased from 10 per cent to 12.5 per cent; and the CGT withholding threshold will be reduced from $2 million to $750,000.

## Travel claims

"Removing travel to an investment property as a claimable expense will impact those investors with properties in regional areas or in locations that are distant from where the investor lives," said Tim Lawless, director of research at CoreLogic RP Data. While regional areas could be disadvantaged by this new policy, the impact on investment demand is likely to be minimal. Lawless said the new ruling is likely a response to the perception that some investors are claiming travel expenses that may "be more related to personal usage rather than legitimate expenses related to their investment."

## Depreciation deductions

This change can affect the investor's ability to depreciate things such as appliances and utilities if these items were purchased by the previous owner. "There could be the potential that this policy encourages investors to renovate established homes rather than purchase recently built product where they won't be able to realise the depreciation benefits of recently installed appliances," Lawless said. In the past, successive investors were able to claim depreciation on plant and equipment items well in excess of their initial value. "There is an argument that the rules could have been fairer towards investors buying near-new property with near-new equipment and who will now not be able to claim depreciation on these items.

## The $5,000 vacancy levy

This levy is aimed at ensuring foreign investors are actually contributing to housing supply and aren't simply offshoring their capital with no intention of occupying or leasing their property.

"The additional levy isn't likely to act as a major disincentive to foreign investment; however, the policy could be difficult to monitor and enforce," Lawless said.

## Restricting stock that can be sold to foreign buyers

This ruling will significantly impact developers who sell a large proportion of their stock via roadshows throughout the Asia-Pacific and other regions, or who rely on foreign marketing networks to sell their stock.

"Attracting domestic demand to some high-rise unit projects that have been designed specifically for foreign buyers may not have market appeal domestically. New unit approvals have already fallen dramatically, and these changes may compress new approvals further as developers struggle to achieve the required number of presales to commence construction," Lawless said.

*M. Mata, "Federal budget changes will impact property buyers, investors", Your Investment Property, 2017. [Online]. Available: http://www.yourinvestmentpropertymag.com.au/news/federal-budget-changes-will-impact-property-buyers-investors-236279.aspx. [Accessed: 18- May- 2017].*

## *Chinese money ‘a godsend’ to Australia*

China continues to be the largest source of investment in Australia with the latest FIRB figures showing a surge in real estate applications over the 2016 financial year.

The Foreign Investment Review Board’s (FIRB) annual report 2015-2016 shows that foreign investment applications grew by 9 per cent to 41,445 in 2015-16 from 37,953 in 2014-15. Most of the growth was driven by residential real estate transactions.

For the third year in a row, China was the largest source of approved investment ($47.3 billion). Residential real estate applications jumped 19 per cent to $72.4 billion from $60.8 billion. The figures come as measures announced in the federal budget last week looked to curtail foreign investment in a bid to improve housing affordability. The government plans to tax vacant properties, limit the share of foreign investment in new projects and increase foreign investors taxes.

“Chinese investment translates directly into jobs, tax revenue, economic growth and new housing construction. There’s nothing about it that any reasonable person can object to. Frankly, China has been a godsend for Australia these past 10 years,” Mr Pittar said.

However, he noted that over the past year growth in Chinese investment has levelled off, from 90 per cent growth in Chinese buyer inquiries via Juwai.com in 2015 to 28 per cent in 2016. “Growth will probably be lower still this year, unless it receives some sort of push from loosening regulations in China,” Mr Pittar said.

Last year the Reserve Bank of Australia warned that a fall in Chinese demand for Australian property could have serious consequences for local lenders. In its April 2016 Financial Stability Review the RBA predicted that a substantial reduction in Chinese demand would likely weigh most heavily on the apartment markets of inner-city Melbourne and parts of Sydney, “not only because Chinese buyers are particularly prevalent in these segments but also because other factors would reinforce any initial fall in prices”. “These include the large recent expansion in supply in these areas as well as the practice of buying off-the-plan, which increases the risk of price declines should a large volume of apartments return to the market if the original purchases fail to settle.”

While Australian banks have little direct exposure to Chinese property investors, the Reserve Bank fears a reduction in demand could trigger broader risks for local lenders. “Although the direct exposures are small, if a reduction in Chinese demand did weigh on housing prices, this could affect banks’ broader mortgage books to some extent,” the RBA said.

Earlier this year the federal government forced the foreign owners of 15 illegally purchased properties to sell, taking the total number of forced sales to 61 since May 2016. “From the extremely low number of divestments that were forced due to noncompliance, it is safe to conclude that foreign investors are extremely well behaved,” Mr Pittar said. “The rate of noncompliance is so tiny as to be almost invisible. While estimates show that one in 20 wealthy Australians cheat on their taxes, fewer than one in 1,000 foreign investors cheat in the property market.”

*J. Mitchell and J. Mitchell, "Chinese money ‘a godsend’ to Australia", Mortgagebusiness.com.au, 2017. [Online]. Available: https://www.mortgagebusiness.com.au/breaking-news/11091-chinese-money-a-godsend-to-australia. [Accessed: 01- Jun- 2017].*

## *The transitional CGT relief measure and your SMSF*

Transitional CGT relief is temporary relief available to all super funds, not just SMSFs, for certain CGT assets that would otherwise lose the tax exemption through the necessary efforts to comply with the new transfer balance cap and new conditions to be applied to transition to retirement income streams (TRIS).

Upon the introduction of the transfer balance cap, effective July 1, 2017, it is expected that some SMSF trustees will need to scale back existing pensions so that members do not exceed their transfer balance cap, which is $1.6 million for the 2017-18 financial year.

If CGT assets are sold to enable the commutation and withdrawal from existing pensions, then the current law will apply to these disposals and the transitional CGT relief is of no relevance.

Conversely, if a fund member decides to commute a portion of their superannuation interest, that currently is in the pension phase, back into the accumulation phase, then the transitional CGT relief will be more than relevant. This is because investment earnings, including capital gains, are taxable in the accumulation phase.

Additionally, from July 1, income from assets supporting a TRIS will not be eligible for an exemption from income tax on earnings, so the CGT relief provisions will be relevant for superannuation members receiving a TRIS.

Essentially, the transitional CGT relief ensures any capital gains that might arise as a result of superannuation fund members complying with the transfer balance cap or because of the TRIS losing the tax exemption will continue to receive concessional treatment.

*"The transitional CGT relief measure and your SMSF", Breaking tax and super news - Tax & Super Australia, 2017. [Online]. Available: http://taxandsuper-newsroom.com.au/index.php/2017/05/08/transitional-cgt-relief-measure-smsf/. [Accessed: 01- Jun- 2017].*