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Treasury Laws Amendment (Making Multinationals Pay Their Fair Share – Integrity and Transparency) Bill 2023

The Property Council of Australia welcomes the opportunity to provide a submission to the Senate Economics Legislation Committee about the *Treasury Laws Amendment (Making Multinationals Pay Their Fair Share – Integrity and Transparency) Bill 2023* (**Bill**).

The Property Council of Australia champions our largest industry, employing over 1.4 million Australians, contributing 18 per cent of our national tax take and shaping the future of our communities and cities. Property Council members invest in, design, build and manage places that matter to Australians: our homes, retirement villages, shopping centres, office buildings, industrial areas, education, research and health precincts, tourism and hospitality venues and more.

Executive Summary

The Property Council's position on the Bill is summarised as follows:

1. The Bill negates the positive impact of the Federal Government's recent announcement to reduce the withholding tax rate on Build to Rent (BTR) assets, which we welcomed. **It will put at risk investment a minimum of 20,000 Build to Rent (BTR) apartments currently under construction or in the planning phase, while jeopardising the feasibility of the 150,000 BTR apartments in the pipeline over the next decade.**

2. **The Bill's provisions extend beyond its expressed objectives with unintended consequences.** If the Bill is passed without targeted and specific amendments, it will materially reduce the allocation of global capital into the Australian property sector.

3. We understand the Government's publicly stated intention that the Bill give effect to integrity measures to prevent base erosion and reduce deductibility but the Bill overreaches by expanding the Commonwealth's revenue base at the cost of new housing projects. **The Budget forecasts that the Bill will raise $720 over the next two years. Recent Property Council modelling shows that over the same forecast period more than $400 million (over 55 per cent) will flow from REITS and Wholesale Property funds alone.**

4. One of over a hundred examples, is a pipeline in excess of a thousand apartments, worth more than two billion dollars. That development, otherwise commencing in 2023 or 2024 will no longer be able to go ahead because the investment assumptions are no longer viable.

5. **Amendments to the Bill can easily be made, so that it appropriately addresses integrity risks, facilitates standard commercial lending arrangements in the property sector and**

avoids contributing the Australia's housing affordability crisis. This can occur through the targeted and specific amendments recommended in the Appendix to this submission.

Bill's expansion beyond its expressed objectives

The Bill will have a disproportionately negative impact on the property sector. Without amendments, the Bill will result in Australia having one of the most restrictive interest limitation regimes in the world for investments in real estate assets.

- The Property Council and its members support the stated objectives of the Bill. Although those objectives, expressed in the Government's policy announcement and Second Reading Speech, were limited to integrity measures to prevent base erosion, the drafting of the Bill goes beyond this.

- The institutional property sector (Real Estate Investment Trusts, or REITs) does not pose a genuine risk or concern of profit shifting but, instead, will be caught by the provisions of the Bill because of the legitimate way in which they do business and use debt to finance projects.

- **Through consultation on the Bill, we have subsequently been advised that a further intention (although never publicly acknowledged) is to expand the Commonwealth's revenue base, not merely limit base erosion.**

- Given Australia competes globally for capital, this will serve to reduce capital allocation into Australia, leading to a decline in development activity and impacting employment.

- This will result in increased costs (e.g. rental expenses) for tenants across several sectors like student accommodation, commercial office, retail, industrial and logistics. Crucially, it will serve to restrict housing supply as our nation faces a shortage of homes and a housing affordability crisis.

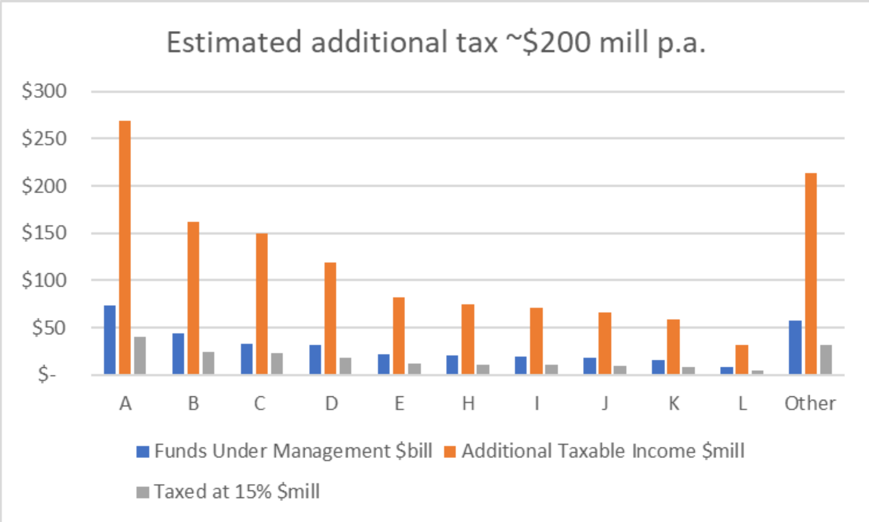
The Budget forecasts that the measures to which the Bill will give effect will raise around $360 million per year.

The Property Council's modelling, which is based on extensive consultation and de-identified case studies (commercial-in-confidence), suggests that REITs and Wholesale Property Funds will contribute $200 million per annum (approximately), owing to the fact that many will no longer meet the Third-Party Debt Test or the Group Ratio Test.

Over 50 per cent of forecast revenue will come from a broader property industry that contributes 13 per cent of GDP and which has never been the stated target of these measures like other industries have.

This illustrates that the Bill will either disproportionately impact REITs (in contrast to what was intended) or that revenue forecasts are significantly less than what is likely to be collected.

Table 1 below has been compiled based on direct feedback from Property Council members (each of whom have been de-identified and labelled as "A" through "L"), based on analysis of their likely taxation obligations now and should the Bill pass the Parliament and the legislation commence.



The property industry is a capital-intensive sector, requiring significant investment to deliver projects. The use of genuine Third-Party Debt deductions allows investment returns to remain competitive within the global market.

Australian deals compete with other jurisdictions that offer "carve-outs" and exemptions for the property sector.

Borrowing from external lenders, in particular foreign capital, is often the only option for developers in the current macroeconomic climate while superannuation funds remain unengaged with the sector and REITs are capital constrained.

The Bill will negatively impact genuine third-party foreign debt which is the only way at present Australia finances the BTR sector.

Commencement Date

The Bill proposes significant changes, and the commencement date of 1 July 2023 is inadequate, given that the legislation remains in Bill form, differs significantly from the Government's October 2022 policy announcement and remains subject to this Committee's review. Owing to the breadth of amendments required, the commencement date must be delayed by 12 months, to 1 July 2024.

If the commencement date is not delayed, then the Bill should only apply for income years commencing after 1 January 2024 to avoid retrospective application.

The Bill will hurt housing supply and affordability

Australia is facing a severe housing supply deficit, which is the primary factor hurting housing affordability.

Australia needs better planning, more land supply, proper housing targets and a national strategy on build-to-rent and purpose-built student accommodation to ensure our housing supply keeps pace, let alone improves.

The National Housing Finance and Investment Corporation's *State of the Nation's Housing Report 2022-23* outlines a shortfall in new Australia homes of over 79,300 to 2033. Just as the Property Council supports any measure to boost housing supply, we are concerned by any measure that will restrict it.

We welcomed the Government's recent announcement to reduce the withholding tax rate on BTR projects from 30 per cent to 15 per cent. According to research from EY, this measure could encourage the delivery of an additional 150,000 new apartments over 10 years. The Bill will negate those benefits.

Following the Government's announcement, certain new BTR projects have been announced which are proposed to be delivered through JV developer arrangements, funded by genuine third-party global capital.

However, the introduction of the Bill has resulted in significant uncertainty and threatens many of these projects.

The advice we have received from several members is that the Bill could reduce the typical Internal Rate of Return on a BTR project from 13 per cent to 9 per cent. Further advice suggests that this will serve to render the delivery of BTR projects unviable. Assuming this is the case, the Bill puts at risk approximately 20,000 BTR projects across Australia, including 3,500 in NSW, 4,200 in Queensland, 15,000 in Vitoria and 500 in Western Australia.

Of course, these figures do not take into account the impact of the Bill on typical Build to Sell projects and the impact on housing supply is likely to be far greater.

Specific and targeted amendments

Through eight separate consultation sessions between the Property Council and Treasury, we have raised our concerns in relation to the Bill. We propose several amendments which will serve to maintain the integrity of the legislation and achieve its expressed objectives, while mitigating the unintended consequences that it will otherwise have on housing supply.

It is clear that a one-size-fits-all approach is not appropriate for both consolidated groups and trust structures. In fact, we note that the complexity of the issues is the main reason why both the US and UK provide carve-outs for the property sector from their equivalent regimes, given that the feasibility of housing as key social infrastructure is at stake.

Set out in the **Appendix** is a summary of each of the relevant issues with the Bill, and the solution to fix each of them. This list seeks to address integrity risks identified by Treasury and is a list of the basic changes that need to be made to ensure that the legislation does not have significant adverse impacts on taxpayers. Versions of this list have been provided to Treasury throughout the consultation process and, in many instances, Treasury has indicated that the impact of the legislation was unintended and would be remedied. This remediation has not occurred.

<u>Third Party Debt Test (TPDT)</u>

The Government committed in the October Budget 2022-23 to "retain an arm's length debt test as a substitute test which will apply only to an entity's external (third party) debt". Most of the Property Council's members are discovering that the TPDT, as drafted, results in a denial of debt deductions on third party debt. At the most general level, the relevant requirements to satisfy the TPDT are inconsistent with standard third-party lending practices and security arrangements. This will have not only a detrimental impact on the real estate sector, but also lending volumes of Australian banks and non-bank lenders.

The critical issues with respect to the TPDT are set out in detail in the Appendix.

While we understand the purpose of elements of the TPDT is to achieve certain integrity objectives, the breadth of the drafting constitutes significant overreach. Rather, particular integrity measures should be seriously considered and targeted measures be drafted appropriately.

Debt Creation

The Bill contains unanticipated measures on which the Government did not consult, being the so-called "debt creation" rules, with which there are numerous problems.

First, they apply to deny debt deductions from 1 July 2023, but there is no requirement that the relevant transaction needs to have been implemented on or after 1 July 2023. Accordingly, the debt creation rules are, in effect, retrospective.

Second, they are intended to address what the Explanatory Memorandum describes as "debt creation schemes that lack genuine commercial justification". However, the breadth of the rules will apply to a very large number of ordinary commercial (and third party) transactions, and there is no requirement in the legislation that the scheme lacks a commercial purpose or is motivated by obtaining debt deductions. Most tax integrity measures of this nature would (and, as a matter of good tax policy design, should) include a purpose test.

Third, although the rules are purportedly to target cases of "debt creation", the rules do not require there to be any increase in debt levels before they can apply. This is in contrast to Australia's former debt creation rules, which contained an exclusion for schemes where there was no net debt creation.

There are also several legislative drafting issues that we recommend be addressed, which are set out in the Appendix.

The debt creation rules should be removed from the Bill, and further consultation should be undertaken. At a minimum, the debt creation rules should be deferred until income years commencing on or after 1 July 2024 and should only apply to future arrangements.

The Fixed Ratio Test (FRT)

The Property Council asks for a few simple amendments so that the FRT works appropriately, summarised as follows:

- excluding prior year capital and revenue losses in the calculation of tax EBITDA;
- including a separate provision setting out the calculation of tax EBITDA for Attribution Managed Investment Trusts (AMITs); and
- allowing excess thin capitalisation capacity of a downstream associate entity to flow to an upstream associate entity, to ensure that structures where external debt is sourced at an upstream level (e.g., debt related to a portfolio of assets) are not adversely impacted. Integrity concerns in respect of double gearing structures can be appropriately addressed, consistent with the current associate entity rules.

The Group Ratio Test (GRT)

The GRT allows an entity in a group to claim debt-related deductions up to the level of the worldwide group’s net interest expense as a share of earnings. In other jurisdictions, it is often the equivalent of this test that is used by highly leveraged groups where the debt that is provided is third party debt.

However, as drafted, the GRT is not appropriate, because:

- the GRT applies a ratio to tax EBITDA. As tax EBITDA is required to be calculated disregarding income derived through downstream associate entities, any debt sitting at a holding level in a non-consolidated structure will likely have nominal or nil tax EBITDA. Other jurisdictions' versions of the GRT do not operate in this manner.

- many entities fall outside the definition of a "GR group", which is a requisite gateway to access the test. For example, many large inbound investors, such as foreign superannuation funds, are classified as "investment entities" for accounting purposes, and so do not prepare consolidated financial statements. One of the requirements associated with a GR group is that they prepare consolidated financial statements. Although the OECD recommended an alternative test for investment entities, the legislation as introduced departs from the OECD's recommendations, and in so doing penalises investment entities.

Conclusion

The Property Council will work with Treasury, Government, and the Senate Economics Legislation Committee to ensure that the legislation appropriately addresses integrity risks while also facilitating standard commercial lending arrangements in the property sector.

A failure to do so will have serious negative consequences on economic activity, housing supply and housing affordability in the short, medium and long term.

Please see below for attached **Appendix** of *Issues register with Tabled Legislation* for reference.

If you have any questions about our submission, please contact Antony Knep, Executive Director – Capital Markets, on 0424 547 664 or at aknep@propertycouncil.com.au.

Kind regards

Mike Zorbas
Chief Executive
Property Council of Australia

Appendix – Issues Register with Tabled Legislation

#	Category	Issue per EM	Status under Bill	Priority	Ref	Proposed solution
1	TPDT - Choice		Where the Commissioner has decided to allow revocation a TPDT choice under 820-46(4) any deemed choice under 820-46(5) automatically ceases to apply (820-47(5). The entity to which the deemed choice previously applied would then be out of time to make the choice (absent the Commissioner's discretion).	Low		Where the entity has itself made a choice under 820-46(4), 820-46(5) should not apply to it such that the choice can be preserved (subject to a separate application to revoke).
2	TPDT – Deemed Choice		Deemed choice applies to an entity that has entered into a *cross staple arrangement with an entity that has made a choice under 820-46(4) or is taken to have made a choice under 820-46(5). Where an entity on the trust side borrows from a bank (as would usually be the case) and therefore makes a choice to apply the TPDT, the deemed choice on the company side would result in denial of interest deductions on any cross stapled loan that does not meet the third party debt conditions. In this regard, many cross stapled loans will not qualify as conduit financing as they may not be sourced from third party debt but rather from cash reserves, capital raisings, proceeds on disposal of assets etc. The integrity concerns in relation to different choices only arises for upstream entities, and should not arise for stapled entities.	Critical	820-48(3)	Remove 820-48(3) or at a minimum include a requirement that the party to the cross staple arrangement must be a member of the borrower's obligor group.

3	TPDT – Deemed Choice		A 20%+ associate entity that is in the obligor group is deemed to make the third party debt test choice where the borrower in the obligor group makes this choice.			Entities that are in the obligor group only because they provide security over shares or units held in obligor group members or loans to such members should not be subject to the deemed choice as the security is not in the nature of additional credit support (but rather is required to assist the bank with enforcement of its security over the underlying assets of the obligor group). Change to: *820 49 Meaning of obligor group etc.* *(1) Subsection (2) applies if:* *(a) an entity (the borrower) has issued a *debt interest to another entity (the creditor); and* *(b) the creditor has recourse for payment of the debt to which the debt interest relates to* ***one or more of*** *the assets of one or more other entities (each of which is an obligor entity).* *(2) Each obligor entity and the borrower is a member of an obligor group in relation to the *debt interest.* ***(3) For the purposes of paragraph (1)(b) disregard assets that are *equity interests and *debt interests in an entity that is a member of the obligor group (disregarding this subsection).***
4	FRT	To avoid penalising groups of trusts that are not eligible to form a tax consolidated group, the fixed ratio earnings limit should include an ownership based proportional share of any excess fixed ratio earning limit over the net debt deductions of associate	This issue is even more important as under the Bill taxable distributions must be ignored in calculating Tax EBITDA.	Critical		Excess thin capitalisation capacity for underlying entities needs to be available. Propose that any of the excess fixed ratio earning limit over net debt deductions is includes in Tax EBITDA: - For investments in trusts, based on the proportional

		entities (i.e. associate entity excess amount). The fixed earnings limit should then be reduced with reference to the tax EBITDA relating to distributions from an associate entity.				share of net income (or determined trust components of an AMIT) - For investments in companies, determined by reference to share of equity calculated on a monthly basis.
5	FRT	Carry forward capital losses are required to be separately added back in calculating tax EBITDA in s820-49 (as such losses do not form part of tax losses for earlier income years, rather form part of the calculation of the net capital gain included in taxable income.	Carry forward revenue losses are also not added back under the Bill. Apart from causing the FRT to deviate from its stated objective of reflecting economic activity for an income year, this change creates complexity and potential circularity in the Tax EBITDA calculation (as the tax loss utilised can be impacted by the denial under the FRT).	High	820-52(1)(a)	Exclude the application of prior year revenue and capital losses in the calculation of taxable income.
6	FRT	Tax EBITDA is based on "taxable income", this concept does not exist for trusts and partnerships, which are required to determine "net income".	The issue has been addressed for Division 6 trusts but not for AMITs that calculate "determined trust components" calculated based on section 275-265 and 276-270. It is clear that an AMIT does not apply Division 6 (section 95AAD). An AMIT will therefore have nil tax EBITDA for the purposes of the fixed ratio test.	Critical	820-52(4)	Include a separate provision setting out the calculation of tax EBITDA for AMITs.
7	FRT		No interest deductions are available under the fixed ratio test for a head trust borrower, where the head trust's only income relates to distributions from sub-trusts – While this is an intended outcome, it is particularly adverse where the third party debt test is unavailable to the head trust borrower. Note that this does not apply to a beneficiary of an AMIT that includes amounts in assessable income under 276-80.	Critical (in conjunction with TPDT issues and debt creation rule)	820-52(6)	This issue needs be addressed in conjunction with the issues relating to the TPDT and debt creation rule.

7.1	FRT		Tax EBITDA now excludes any income derived from interests in companies, trusts and partnerships. Australian businesses that undertake substantial business activities through joint venture companies, trusts & partnerships (common in the property development and construction industry) will be significantly impacted by this change. It is not uncommon for JV partners to debt fund a portion of their equity interest in the JV, with limited or no debt within the JV. There are numerous commercial reasons why the debt may be sourced by the JV partner and not the JV including: 1. JV partners have different gearing requirements/policies 2. Individual JV partner may have access to cheaper funding as part of broader group facilities 3. Mitigate against risk of default by the other partner if each JV partner is only responsible for their own debt financing Based on current drafting, JV partners will not be able to include any EBITDA from the JV in their thin cap calculations, resulting in denial of interest deductions.	Critical	820-52 (3), (6) & (8)	Fixed ratio earnings limit should include an ownership based proportional share of any excess fixed ratio earning limit over the net debt deductions of associate entities (i.e. associate entity excess amount). This proposal will also solve for issue #12 (i.e. head trust borrower).
8	GRT	GR group net third party interest expense is always financial statement net third party interest expense adjusted to include amounts in the nature of interest or any other amount calculated by reference to the time value of money, so there is no need to have two separately defined terms.	The GR group net third party interest expense definition and financial statement net third party interest expense seem circular.	Low		Suggest a single defined concept being GR group net third party interest expense.
9	GRT	Net interest expense in ss 820-53(4) is not defined	No change (relevant subsection is now 820-54(4)(a))	Low	820-54(4)(a)	

10	GRT	The requirement to determine if any GR group member has negative entity EBITDA and to exclude this from GR group EBITDA is onerous and in any event is difficult to understand from a policy perspective (why should the fact that a particular activity is undertaken in a separate entity make a difference?).	No change	Medium	820-55(3)	Remove 820-55(3)
11	Debt deduction creation		A "legal or equitable obligation" is not a CGT asset. It is not clear how it is possible to debt fund the assumption of an obligation.	Medium	820-423A(2)	Remove "or a legal or equitable obligation".
12	Debt deduction creation		For 820-423A to apply there is no requirement that the debt deduction relates to an arrangement with an associate (i.e. third party debt deductions can be denied). There is also no recognition that there may have been existing third party debt which is being refinanced as part of the transfer of an asset (i.e. there is no additional debt funding overall). There was no consultation in respect of this new integrity rule and it has potentially extreme breadth of application (including principal purpose anti-avoidance rules).	Critical	Subdivision 820-EAA	Remove from the Bill to allow consultation.
13	Debt deduction creation		Where a trust seeks to 'push down' debt to a subsidiary trust to address the complete denial of deductions under the FRT as a result of the requirement to exclude distributions from trusts in tax EBITDA, deductions of the subsidiary trust in relation to the new debt (which would be used to fund a return of capital by the subsidiary trust) would be wholly denied.	Critical	820-423A(5)	Remove from the Bill to allow consultation.

13.1	Debt deduction creation		The debt deduction creation rule operates completely separately to the FRT such that both sets of rules apply to the same deductions, i.e. whether net debt deductions exceed the fixed ratio earnings limit is based on all net debt deductions, including debt deductions that are denied under the debt creation rule. This seems clear from the definition of debt deduction in s820-40(1)(b) by reference to amounts that are deductible but for the operation of Division 820. As the debt creation rule is contained in Division 820, both sets of rules must be applied to the same deductions. For example, if the fixed ratio earnings limit is $1,000 and debt deductions are $2,000, including $500 of debt deductions that are disallowed under the debt deduction creation rule, the FRT would operate to also deny $750 of the remaining $1,500 of debt deduction (i.e. total denial under Division 820 of $1,250, rather than $1,000). Section 820-423C also clarifies that nothing in Subdivision 820-EAA limits other provisions of Division 820 in their application to reduce, or further reduce, debt deductions of an entity.	High	820-40(1)(b) 820-423C	Remove from the Bill to allow consultation. Provide an ordering rule, such that the debt deduction creation rules apply prior to the thin capitalisation rules.
13.2	Debt deduction creation		It is not clear whether Subdivision 820-EEA can apply to arrangements that were entered into prior to the income year commencing on or after 1 July 2023.	Critical	820-423A	Remove from the Bill to allow consultation. Clarify that 820-423A(2) and (5) only apply where each of the relevant conditions (e.g. acquisition or issue of debt interest) is met in an income year commencing on or after 1 July 2023.

14	TPDT– Conditions	The borrower must be "an Australian resident". An Australian resident is defined as a "resident of Australia" for the purposes of the *Income Tax Assessment Act 1936*, which is then relevantly defined to mean a person, other than a company, where certain requirements are met or "a company which is incorporated in Australia, or which, not being incorporated in Australia, carries on business in Australia, and has either its central management and control in Australia, or its voting power controlled by shareholders who are residents of Australia." A trust is not a "person" or a company and so cannot be "an Australian resident" and therefore cannot satisfy the TPDT conditions.	No change.	Critical	820-427A(3)(e)	Include an "Australian entity as defined in section 336 of the Income Tax Assessment Act 1936".
15	TPDT– Conditions	It is unclear whether the requirement in ss820-61(2) that the entity uses the proceeds of issuing the debt interest "wholly to fund its [Australian] investments" and "its Australian operations" can be satisfied in respect of the re-financing of funding in respect of such Australian investments or operations. For example re-financing of a loan or directly replacing equity funding with third party loan funding.	Changed to *"uses all, or substantially all, of the proceeds of issuing the debt interest to fund its commercial activities in connection with Australia that do not include:* *(i) any *business carried on by the entity at or through its *overseas permanent establishments; and* *(ii) the holding by the entity of any *associate entity debt, *controlled foreign entity debt or *controlled foreign entity equity."* The exclusion for "associate entity debt" will severally limit or even effectively remove the ability for the ultimate	Critical	820-427A(3)(d)	Remove reference to "*associate entity debt".

			borrower to on-lend borrowed funds to an Australian group entity, and also seems to make the conduit financing rule inaccessible. It is also not clear whether the activities of the entity cannot include a foreign PE or investment in foreign assets, or whether the proceeds of the debt interest cannot be used to fund such activities, although the EM provides that the "conditions aim to ensure the third party debt test only captures genuine third party debt which is used to fund Australian business operations", suggesting the narrower interpretation.			
16	TPDT– Conditions	The requirement that the third party lender only have recourse for payment to the assets of the entity will often mean that the ETPDT will not be available, for example it is common for the third party lender to have recourse to the membership interests in the borrowing entity, assets of subsidiary entities, or for another entity to provide a guarantee (although this could potentially be structured as an asset of the borrower).	Now also generally excludes assets of the borrower that are "rights under or in relation to a guarantee, security or other form of credit support". This is stated to be "to ensure that multinational enterprises do not have an unfettered ability to fund their Australian operations with third party debt." but applies even if rights are provided from an Australian entity in the obligor group. In addition, a strict limitation on recourse to Australian assets may preclude Australian multinational groups applying the TPDT if the entities have granted security over all assets, as there will often be limited foreign assets (e.g., a foreign bank account). Accordingly, some form of permissible foreign assets is necessary, to ensure entities are not adversely	Critical	820-427A(3)(c)	Change as follows: "*(c) the holder of the debt interest has recourse for payment of the debt to which the debt interest relates only to or* ***substantially only to the following*** *assets:* *(i)* ***Australian assets held by the entity and by any member of the obligor group in respect of the debt interest other than*** *rights under or in relation to a guarantee, security or other form of credit support* ***provided by a *foreign entity which is an associate entity; and*** ***(ii) *equity interests or debt interests in one or more members of the obligor group (disregarding subsection 820-49(3)).***" [Refer to the changes above in relation to the definition of obligor group]

			impacted by nominal assets that may arise from time to time.			
17	TPDT– Conditions		Recourse to assets of the borrower that are "rights under or in relation to a guarantee, security or other form of credit support" are permitted if … the right relates wholly to the creation or development of a *CGT asset that is, or is reasonably expected to be, real property situated in Australia (including a lease of land, if the land is situated in Australia)" and "… the right would not reasonably be expected to allow, directly or indirectly, the holder or another entity to have recourse for payment of the debt … against a *foreign entity that is an *associate entity of the holder." While "the extent (if any) to which the right relates incidentally to another matter" is disregarded, it is not clear whether this will capture the creation or development of chattels as part of a large property development (e.g. fit-out assets, signage, telecommunication towers). To facilitate foreign investment in Australian development projects (e.g. build to rent projects), credit support from a foreign investor should be permitted.	High	820-427A(4)	Adopting the extended definition of "investments in land" in s102MB would assist to address this issue. Remove the restriction on credit support etc. from a foreign resident for the creation or development of Australian investments in land.
17.1	TPDT - conditions		Credit support rights are disregarded in relation to development of real property assets. The EM notes that 'the connection between a credit support right and the creation or development of real property must be tested continuously ….. where a credit support right initially related wholly to funding the creation or	Critical	820-427A(4)	Allow the exception provided in subsection 820-427A(4) to apply for up to 2 years post completion of the development.

			development of real property, but subsequently relates to other business activities in later income years in relation to the same real property (such as an investment holding activity where the real property development activity is completed), then the exception provided by subsection 820-427A(4) will not apply.' Practically this will be problematic for BTR developments. Banks are requiring the credit support to continue during the lease up period until the asset reaches stabilisation (c96% leased). The lease up period for BTR (1-2 years depending on size of the development) is typically longer than a commercial asset. This means that BTR funds will not be eligible to apply the TPDT during the lease up phase.			
18	TPDT – Conduit financier		The general exclusion for assets that are "rights under or in relation to a guarantee, security or other form of credit support" also applies in relation to the assets of the obligor group in the context of the conduit financing conditions. Recourse to Australian assets of the obligor group should be permitted, including rights of credits support. As drafted, any assets of an obligor group that is not held by the borrower is arguably credit support to the borrower, which makes the extension of recourse to assets of the obligor group meaningless.	Critical	820-427B(4) 820-427A(3)(c)(ii)	Change as follows: "*the holder of the debt interest has recourse for payment of the debt to which the debt interest relates only to or* ***substantially only to the following*** *assets:* ***(i) Australian assets held by the entity and by any member of the obligor group in respect of the debt interest other than*** *rights under or in relation to a guarantee, security or other form of credit support* ***provided by a *foreign entity which is an associate entity; and*** ***(ii) *equity interests or debt interests in one or more members of the obligor group (disregarding subsection 820-***

						49(3))." [Refer to the changes above in relation to the definition of obligor group]
19	TPDT – Conduit financier	As the ultimate debt interest issued by the conduit financier needs to meet the external third party debt conditions, the conduit financier cannot be an offshore entity with a loan to an Australian subsidiary as the requirement in ss820-61(2)(d) would not be satisfied, even if all the other requirements are met (same terms, recourse etc.). It is unclear why cross border back to back loans should be excluded.	No change, now 820-427C(f) and 820-427A(3)(e).	Medium		
20	TPDT – Conduit financier	Borrowers are defined in ss 820-61(5) as one or more associate entities of each other, there is no requirement that the entity is actually issuing a debt interest to the conduit financier. In this case the ETPDT cannot apply unless the conduit financier on-lends to an entity and <u>all</u> of its associate entities.	No change (although now 820-427C(1)(b)).	Critical	820-427C(1)(b)	"Borrowers" should be defined as associate entities each of which have issued debt interests to the conduit financier.
21	TPDT– Conduit financier		Section 820 427C needs to apply to each debt interest separately, rather than requiring that all debt interests within an associate entity group must satisfy the requirements (which would prohibit, for example, non-interest bearing loans funded through excess cash in the structure). The requirements should be limited to amounts financed out of amounts borrowed externally. As drafted, there is a requirement that all debt between associate entities satisfy the rules (and, if one fail, they all fail). This does not make sense - e.g., unless the amount is sourced out of the external debt, it should not be required to satisfy the relevant requirements.	Critical	820 427C	Amend as set out below: (1) This subsection applies in relation to an income year (the relevant year) if all of the following conditions are met in relation to the income year **in respect of a debt interest:** ... (c) **one or more entities mentioned in paragraph (b) (the borrowers)** issues a debt interest (a relevant debt interest) to: (i) the conduit financer; or (ii) another borrower: **(d) paragraph (e) applies:** (i) **where** subparagraph (c)(i) applies—**to the relevant debt interes**t that was financed by the conduit financer with

						proceeds from the ultimate debt interest; or (ii) **where** subparagraph (c)(ii) applies— **to the relevant debt interest** that was financed by the other borrower with proceeds from another debt interest that is a relevant debt interest (whether because of subparagraph (i) of this paragraph, or because of another operation of this subparagraph **(which may be applied multiple times));**
22	TPDT– Conduit financier	For the purposes of ss 820-61(5), the "same terms" requirement in ss 820-61(5)(e) may not be possible to satisfy if it requires the same security to be provided under the relevant debt interest as is provided to the bank (e.g. first mortgage over an asset). It is also unclear whether only key terms (e.g. term, interest rate, timing of interest payments) need to be the same, or whether <u>all</u> terms must be the same. We would suggest that only the interest payment terms should need to be the same, or substantially the same, to balance any potential substantial re-characterisation integrity concerns with the ability to apply the rules in practice without needing to replicate the full extent of the third party loan agreement, including facility fees, line fees, management fees, debt covenants, security etc.	Changed to "the terms of each relevant debt interest, to the extent that those terms relate to a cost incurred in relation to the relevant debt interest, are the same as the terms of the ultimate debt interest, to the extent that those terms relate to a cost incurred in relation to the ultimate debt interest." It seems that <u>each</u> cost under the on-lending must be the same as a cost incurred in relation to the ultimate debt interest. There will generally be a range of fees, including interest, line fees, commitment fees, administration / management fees etc. which would be on-charged as an 'all-in' cost.	High	820-427C(1)(e)	Amend to refer to "the terms of each relevant debt interest, to the extent that those terms relate to a cost or costs incurred in relation to the relevant debt interest, are the same as the terms of the ultimate debt interest, to the extent that those terms relate to a cost or costs incurred in relation to the ultimate debt interest."
23	TPDT– Conduit financier		Swap costs "directly associated with hedging or managing the interest rate risk in respect of the debt interest" are deductible where attributable to a debt interest that satisfies the TPD conditions	Critical	820-427A(2)(b)	Remove 820-427A(2)(b) or permit a deduction where the amount is paid indirectly to an entity that is not an associate entity.

			unless "referrable to an amount paid, directly or indirectly, to an *associate entity". This will prevent deductibility of swap costs that have been on-charged to a borrower, even if the on-charge is on the same terms. It is not unusually for a FinCo to on-charge swap costs to the entity that holds the relevant income producing assets.			
23.1	TPDT– Conduit financier		Swap costs are only treated as attributable to a debt interest if the swap hedges interest rate risk in relation to that particular debt interest. Where a swap hedges interest rate risk across a number of debt interests that each qualify under the third party debt conditions, the swap payments should be deemed to be attributable to a debt interest and therefore deductible.	Critical	820 427A(2)(a)	Amend 820 427A(2)(a) to allow hedging of interest rate risk in respect of "one or more debt interests"
24	TPDT– Conduit financier	The conduit financier and borrowers must be "Australian residents". An Australian resident is defined as a "resident of Australia" for the purposes of the *Income Tax Assessment Act 1936*, which is then relevantly defined to mean a person, other than a company, where certain requirements are met or "a company which is incorporated in Australia, or which, not being incorporated in Australia, carries on business in Australia, and has either its central management and control in Australia, or its voting power controlled by shareholders who are residents of Australia."	No change	Critical	820-427C(1)(g)	Include an "Australian entity as defined in section 336 of the Income Tax Assessment Act 1936".

		A trust is not a "person" or a company and so cannot be "an Australian resident" and therefore cannot satisfy the conduit financing conditions.				
25	TPDT– Conduit financier		While the rules "disregard the terms (if any) of a relevant debt interest issued to the conduit financer that have the effect of allowing the recovery of reasonable administrative costs of the conduit financer that relate directly to the relevant debt interest", any other costs are not able to be on-charged (for example audit fees, directors fees or other costs in relation to the operation of the conduit financier). Where existing on-lending arrangements include recovery of such costs, these agreements will need to be amended.	High	820-427C(2)(c)	Amend as set out below: (c) disregard the terms (if any) of a relevant debt interest issued to the conduit financer that have the effect of allowing the recovery **by the conduit financer or another borrower** of reasonable administrative costs **or costs** that relate directly to the relevant **debt interest or the ultimate** debt interest; and
26	TPDT– Conduit financier		The rules disregard the terms of a relevant debt interest that allow for the recovery of costs "directly associated with hedging or managing the interest rate risk" of the conduit financer in relation to the ultimate debt interest. Given the requirement in 820-427C(1)(e) is only that the terms of a cost under the relevant debt interest are the same as the terms of the ultimate debt interest it is not clear what 820-427C(2)(d) is intended to achieve, noting also that hedging costs under a relevant debt interest are not deductible if paid to an associate entity.	High	820-427C(2)(d)	
26.1	TPDT – Conduit financier		In applying subsection 820-427A(3) of the TPDT conditions in relation to a relevant debt interest or the ultimate debt interest, 820-427B(4) modifies the reference to	High	820-427B(4)	Clarify that recourse is available to Australian assets of all Australian entities that are members of the obligor group.

			"assets held by the entity" in the recourse condition in subparagraph 820 427A(3)(c)(i) to refer to the following assets: (a) the Australian assets held by the conduit financer; (b) the Australian assets held by "*each entity **not mentioned in subparagraphs 820-427C(1)(c)(i) and (ii)** that:* *(i) is a *member of the *obligor group in relation to the ultimate debt interest; and* *(ii) is an Australian resident."* The entities mentioned in 820-427C(1)(c)(i) and (ii)(c) are "(i) the conduit financer; or (ii) another borrower". Another borrower is a borrower other than the borrower that issues the relevant debt interest. Assets of an entity that borrows from the conduit financier and on-lends to another entity therefore seem to be excluded, even if the interposed borrower is a member of the obligor group.			
27	TPDT–General	The third party earnings limit only refers to debt deductions attributable to a debt interest that satisfies the ETPD conditions, and any debt deductions not attributable to a debt interest (under the expanded definition) will necessarily be denied.	Changed in respect of swap costs other than payments to an associate entity, however other debt deductions that are not related to a debt interest will continue to be denied.	Medium	820-427A(1) 820-427A(2)(a)	