Residential Property Developer Tax (RPDT)

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To: RPDTconsultation@HMTreasury.gov.uk

Introduction and background

The British Property Federation (BPF) represents the real estate sector – an industry which contributed more than £100bn to the economy in 2019 and directly employed more than 1 million people[1]. We promote the interests of those with a stake in the UK built environment, and our membership comprises a broad range of owners, managers and developers of real estate as well as those who support them. Their investments help drive the UK's economic success; provide essential infrastructure and create great places where people can live, work and relax.

Over the last decade the residential rental market has evolved considerably in the UK, prompted by investment from large institutional investors that are seeking long term stable investment returns. Purpose Built Student Accommodation (PBSA) and Build-to-Rent (BTR) assets are the most established rental asset classes, with investors now also showing increasing interest in a rental model which could be appropriate for the retirement living communities.

The BTR market is still relatively new in the UK, and still represents a small proportion of both new housing supply and of the total residential rental sector. Approximately 5,000[2] new BTR homes were developed last year, which accounts for around 2-2.5% of total new housing supply in the UK. However, it is growing strongly and has the potential to contribute more, with BTR representing 20%[3] of London's new housing supply last year.

We are deeply concerned that this tax could stymie the potential of this sector to continue to grow and contribute to our housing supply.

As the tax has been designed with traditional volume build-to-sell (BTS) trading business models in mind, as proposed it will have a penal impact on the rental sector – particularly in light of the proposals to impose a dry tax charge where a building isn't even sold. These proposals will disproportionately impact on the viability of new high quality, professionally managed rental homes in the UK. Everyone would like to see more homes built, but this tax really works against that.

Furthermore, it would be counterproductive to several the government's wider objectives around sustainability levelling up through residential led investment regenerating of our towns and cities. In particular, we would highlight the following benefits of BTR and PBSA that would be undermined by this tax:

Counter-cyclical housing delivery
The BTR business model is counter-cyclical – because investors are seeking returns over very long time horizons, investment and development will happen (and will often be more common) during a recession. To that end, this sector can play an increasing role in helping meet the government's

[1] https://bpf.org.uk/about-real-estate/
[2] https://bpf.org.uk/media/4118/btr-q1-2021-bpf-2.pdf
[3] https://bpf.org.uk/media/4118/btr-q1-2021-bpf-2.pdf.

housing targets in the UK, and will complement the more traditional build-to-sell (BTS) model, where construction typically reduces during a recession and government support is more prevalent.

Sustainability and quality

As long term owners and investors, the quality and longevity of the homes being built today are of paramount importance in this sector. Investors are not only mindful of the sustainability standards of today – but also seek to future proof their assets for the future. As long term owners and operators of these assets, the quality of the design and build is absolutely paramount to their business models – by investing up front in high quality buildings, they can reduce the potential maintenance and retrofitting costs in the future – which will improve returns in the long run. This does mean that upfront costs are high, and margins are tight in this sector – making viability more marginal than for other residential developers, like traditional housebuilders.

As part of the drive for quality and efficiency, the sector is playing a leading roles in supporting the innovation of new construction methods – notably, Modern Methods of Construction, which involves significant amount of manufacturing offsite, enabling greater quality control over the final build quality, and faster delivery times.

Levelling up - regenerating our towns and cities

BTR and PBSA assets are drawn to town and city centre locations – with good access to jobs and universities and transport links. Quite often, BTR investment will be the catalyst for the regeneration of our inner-city brownfield sites – areas which are often difficult to generate viable investment propositions because they are inherently more complex and riskier to build out. Encouraging this investment will support the government's levelling up agenda by stimulating investment in our towns and cities – as well as wider benefits of limiting urban sprawl. Over 50% of BTR investment in now in the regions and this is increasing.

The UK residential investment sector competes globally for institutional and international capital and this tax will reduce investor appetite for the sector and reduce the viability of new development. This tax has not been designed with rental asset classes in mind, which is why the proposals are particularly complex and penal when applied to the rental sector. This cannot be justified given the limited tax revenues that will be generated by the rental sector from this tax.

In light of the considerable benefits that BTR brings to the UK's housing supply and wider government priorities, investment asset classes such as BTR and PBSA should not be within scope of this tax.

We look forward to engaging further on the development of this tax. Please do not hesitate to get in touch if you require further information.

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Residential Property Developer Tax (RPDT)

Structure of this response:

Part 1: Executive summary and key recommendations

Part 2: Response to consultation questions

Appendix 1: BTR vs BTS funding models – and explanation of 'forward funding'

Appendix 2: Room types and building configuration in the PBSA sector

Summary of acronyms used:

BTR – Build to rent

BTS – Build to sell (traditional volume housebuilder models)

PBSA – Purpose Built Student Accommodation

Part 1: Executive summary and key recommendations

1. As noted in introduction, we have grave concerns about the consultation proposals, and in particular, the potential to stifle investment and development of professional investment in rental homes – we provide a summary of our high level concerns and recommendations below.

2. ***BTR and PBSA investors and developers already cover costs of repairs*** - BTR investors own their investments for the long term. They lease their buildings on short term tenancies and will be responsible for any structural repair works, or any works needed to meet the latest health and safety requirements. There is no mechanism to pass these costs onto tenants – and there is no ambiguity around which party is responsible for these costs, as there is for owners of long leases. Therefore, the BTR and PBSA sector will effectively incur a double charge for repair works, once when the building is constructed (with this tax), and a second charge when repair works are needed on their buildings in the future. Furthermore, BTR and PBSA owners have not benefited from the cladding remediation fund and have funded any cladding remediation works directly. BTR and PBSA developers will often have long-term relationships with investors and have also ringfenced funding to make contributions to remedial works.

3. ***Current proposals would be disproportionately penal on investment business models*** – the proposals are penal for BTR and PBSA investors as compared with BTS business models. The most egregious elements of the tax for a rental business model are as follows:

    a. **Notional profits** - taxing 'notional profits' will lead to a dry tax charge for BTR and PBSA investors – because they typically make their returns on rental income received over several years or even decades, rather than on the immediate sale of the property. A dry tax charge will be tantamount to a levy, at a time when there are no true economic profits – hence it will have a disproportionate impact on the viability of BTR investment. Taxing notional profits will also be incredibly subjective, which will add complexity.
    b. **Gateway 2** - BTR assets tend to be higher rise than those delivered by traditional volume housebuilders, therefore, it seems very likely that the forthcoming Gateway 2 levy will only exacerbate this distortion further.
    c. **Losses and interest costs** - the proposals to restrict interest costs and losses are penal and again are likely to have a bigger impact on BTR businesses than their BTS counterparts. The tax treatment of interest costs on a development can vary depending on a number of factors – most notably, whether a business capitalises the interest costs into the cost of their assets (or trading stock), or whether they incur those costs as they arise and effectively generate losses. While the tax and accounting treatment will vary for different businesses, this is likely to have a more penal impact on investment assets.
    d. **Annual threshold** - BTR developments are often of significant scale and built out far more quickly than a traditional BTS development (as recognised by the Letwin Review). BTS developers will typically need to build out much more evenly, to ensure that they do not saturate the property sales market, which could have a negative impact on the price of their product. The opposite is true for BTR and PBSA – as a long term investment asset, the quicker a development can be completed and ready for people to live in, the more quickly rental returns can start being generated for investors. This means that a BTR development will be completed much more quickly than a comparably sized BTS development – as such, the £25m annual allowance will be of less help to BTR businesses, while a BTS business would have the option to amend the pace of their sales in a given period in order to fall under the threshold and reduce the likelihood of RPDT arising on their projects.

4. ***The BTR market has not benefitted equally from wider government support*** – one of the reasons set out in the consultation for extending the scope of this tax to all residential asset classes is that the government's wider policies and support have benefitted the whole residential market, and therefore it is right for the whole market to contribute. We do not think it is accurate to say that wider government measures have supported the whole sector equally – indeed some of the more significant measures to support the residential property sector have overwhelmingly supported the BTS market (notably the SDLT holidays, help to buy, and mortgage guarantee schemes). If anything, these measures have put BTR investors in an even less competitive position when bidding for land. Furthermore, there are a number of measures which have actively penalised BTR investors more than traditional BTS models – notably the SDLT 3% surcharge on additional dwellings.

5. ***Complexity*** – adding rental developers to this tax will significantly increase its complexity, to the disadvantage of rental operators and tax authorities. This makes no sense. For the amounts of tax involved, the introduction of this complex new tax is disproportionate for both businesses and HMRC – especially for investment asset classes, like BTR (Build to Rent) and PBSA (Purpose Built Student Accommodation). In order to ensure that the tax will not have an undue impact on viability assessments and therefore housing supply, the tax must be far simpler to understand and compute.

6. Excluding investment asset classes will go a long way to alleviating the most significant complexities within the proposals, but we would also encourage government to consider alternative options which could impose a more proportionate administrative burden, in light of the tax revenues involved. In particular, an alignment with corporation tax (with perhaps a surcharge on trading profits from some residential developments), would significantly alleviate the administrative burden given businesses already need to compute profits on this basis anyway.

7. ***Trading and investment business models are very different –*** A lot of the complexity arises as a result of trying to bring rental asset classes within scope of this tax. Build-to-rent and build-to-sell business models are very different – both in terms of the way in which returns are generated, and because they make returns over very different time horizons. The IPF briefing paper, "Mind the Viability Gap"[4] provides a useful overview of the differences between BTR and BTS business models, and seeks to quantify the viability challenges for BTR investment.

8. The existing corporation tax regime recognises that 'trading' and investment' businesses' are distinct, and as such, a different approach to taxing these very different business models is appropriate. Moreover, the UK tax regime has evolved considerably over the last few years and as a result, introducing this additional tax on notional profits would risk a double taxation effect when rental investments are ultimately sold by investors.

[4] Mind the Viability Gap: Achieving more large scale Build to Rent housing: https://www.ipf.org.uk/static/uploaded/e06a7d4a-892b-495b-811d78b43305726e.pdf

Summary of key considerations and recommendations

A. Exclude investment asset classes – like BTR and PBSA

9. Extending the scope of this tax to investment asset classes like BTR and PBSA will disproportionately impact on the viability of development of new homes for rent, both of which are increasingly designed specifically for that purpose and are largely unsuitable for general sale on a unit by unit basis, and protected by planning categorisations. Excluding these asset classes will also make the rules far simpler – given it is inherently challenging to impose a tax designed for trading businesses on assets designed for investment businesses. As such, rental asset classes, like BTR and PBSA, should be carved out.

B. Student accommodation - should be carved out

10. The government acknowledges that a carve out for PBSA could be justifiable where the developments have some communal features or characteristics. In additional to the justification for excluding investment asset classes more broadly, as touched on above, we would urge government to carve out the wider Purpose Built Student Accommodation (PBSA) market, because they make an important contribution to housing supply, and play a huge role in the success of our Higher Education sector more broadly. In particular:

    a. If PBSA is supported – we estimate that 77,000 traditional family homes would be freed up for the wider market, making a significant contribution to housing supply.
    b. Appropriate accommodation for students plays a key role in the success of our wider Higher Education sector – a huge export industry which attracts students from around the world.
    c. There is a recognised shortage of adequate student accommodation in London and other UK cities: PBSA investors work closely with UK universities to provide good quality and affordable accommodation in the right locations. RPDT will add to the commercial pressures on PBSA development and potentially restrict growth in the education sector.

11. Given the evolution of the student accommodation sector in recent years, it is important that the rules and definitions reflect modern accommodation for students. In particular, “cluster flats” are increasingly common designs – typically providing a number of en-suite bedrooms which all have access to a communal kitchen and living space. There are also en-suite studios, with communal facilities that are not interconnected. In order to ensure that similar business models are not discriminated against, we would urge government to consider a broad carve out for PBSA. Like BTR, most PBSA will have planning restrictions to ensure that it remains in student use, and so any exemption could be defined in those terms.

C. Retirement communities – housing with care should be carved out

12. We are concerned that there is some ambiguity in the consultation in respect of what is intended to fall within scope with respect to retirement accommodation. We understand from member interaction at stakeholder events that the intention is for a limited carve out, which would not include purpose built housing for older people.

13. There is a huge undersupply of appropriate housing for our elderly and as such, this kind of development should be encouraged. In particular, the provision of purpose built housing for older people, with significant support available on site, can allow elderly people to continue

living independently for longer, thereby alleviating significant pressure on our hospitals and national health service.

14. This is another sector that has seen huge evolution is recent years, as such any definitions should reflect common designs and practices - developments with care on site are commonly referred to in the sector as "housing with care", and we would support an exclusion for these types of developments as a minimum.

15. We also recognise the broader issues of undersupply of appropriate housing for our elderly, and as such, there would be merit in considering a broader carve out – in particular, a carve out for developments with a C2 planning use class warrants further consideration.

D. Keep it simple: target trading profits within corporation tax

16. Introducing a surcharge within corporation tax on trading profits related to in scope residential development would be a far simpler approach to raise revenues – for both HMRC and the tax payer. The corporation tax regime already exists, so this would significantly reduce the resource pressure on HMRC to both develop and operate the tax. And this would be far simpler for tax payers, who already need to compute their trading profits for corporation tax purposes.

17. If government are truly worried that business models would temporarily switch to investment asset classes in order to mitigate this tax, there is precedent for appropriate safeguards within existing tax and planning rules. For example, it would be possible to relatively easily apply something similar to the protections in the REIT rules for disposals of assets shortly after construction is completed. Any in scope building which is sold within 3 years of a development could automatically be treated as within scope of RPDT, or simply a higher rate of tax could be applied to those gains/profits.

18. Alternatively the planning rules already allow for local authorities to claw back some of their affordable housing contributions which would otherwise have been due if a developer changes the use of their development (e.g. from BTR to BTS) within say 10-15yrs of completing a development – this mechanism could also provide some helpful precedent for an appropriate safeguard.

19. We would note that a broader carve out for residential rental asset classes, like BTR and PBSA, would still be required under this approach, in order to avoid creating a distortion between different modes in the rental sector – notably those that develop in-house vs those that use a third party developer.

E. Model 2 – the tax should target only residential development profits

20. We would strongly encourage the tax to be targeted at in scope residential development activity only (model 2), and for tax numbers, rather than accounting numbers to be used in profit calculations. If there is a lot of support for model 1 from other stakeholders, this option could be available by election, if a business considers that it would simplify their compliance.

21. Model 1 (the proposal to tax the whole of a company's profits) would introduce significant uncertainty for businesses that carry on a number of different activities and create a significant administrative burden in identifying the activities that are within scope of the RPDT, simply to determine whether or not any significance threshold has been breached.

F. Interest costs and losses should be taken into account when computing "profits"

22. We already have rules within corporation tax which restrict interest costs and losses. Restricting these further will take businesses even further away from being taxed on their true economic profits. This is fundamentally unfair and will cause the tax to be paid by less profitable businesses. Furthermore, it will create huge uncertainty around what level of tax will be due – which will have a big impact on viability of developments. It also adds undue complexity to the regime. Given that the tax regime is new and the rate will be set as a function of the tax base, then its seems to only add complexity to the calculation of the tax.

G. Investment funds and REITs

23. It is common for large and bulky investment in real estate to be carried out collectively, either through a fund or joint venture – in order to share risk and pool resources. In the context of residential property, this is particularly common for investment asset classes like BTR and PBSA, as the long term, stable, investment returns are particularly attractive for funds and institutional investors.

24. It is important to ensure that the practicalities of investment through funds and REITs is considered as part of the development of these rules, and in particular that the compliance and reporting burden for transparent funds is proportionate, and there is sufficient clarity in respect of how the rules should apply to exempt investors, and fund managers.

25. In respect of REITs, these rules will be challenging to apply and will disrupt the fundamental principle of a REIT, which seeks to impose tax on property income returns in the hands of the ultimate investors. Given the notional gains being taxed will not be property income returns, it is not clear to us how a tax of this nature could easily be integrated within the REIT regime, without damaging its fundamental principle or distorting the distributions that REITs are required to pay out to investors. As such, we would suggest that REITs should be carved out of these proposals.

H. S. 106 affordable housing contributions should be within scope

26. We consider that it would be simpler to include affordable housing within scope, particularly affordable housing contributions as part of S.106 obligations. These are predominantly built at cost, or at a loss, and as such, the losses generated from the affordable housing contributions should be factored into the overall "profit" of a residential development – in order to ensure that the profits subject to tax are as close to the true economic profits as possible.

27. However, we have wider concerns that this tax will have implications for the supply of affordable housing contributions, because the viability of other residential developments will be compromised. In particular, given BTR investments typically have very slim margins, if this tax has an impact on viability calculations, this will have negative impact on the amount of affordable housing that can be delivered on BTR developments in scope.

I. Defer the implementation date

28. Housing developments take years to come to fruition – from acquiring the site / design / planning / construction and finally to sale or rental. The viability of the developments that become subject to tax next year will have been done several years ago based on tax rates and

laws that were in place at the time. Moreover, the investment and financing will also have been secured several years ago – meaning that funding this tax now will be incredibly challenging, particularly in the context of a BTR development, where a dry tax charge is being imposed.

29. Furthermore, rushing through complex legislation risks creating poorly drafted legislation, which will be incredibly unhelpful – adding uncertainty to future project viability assessments.

30. As such, we would recommend a deferral of the start date, of at least a year – and ideally a mechanism to grandfather (i.e. exclude) projects which started before legislation was introduced (or at least before this consultation was published). Furthermore, the rules should allow a just and reasonable apportionment of profits in the introductory straddle period – as BTR property 'sales' are not consistently distributed over a period of time, as it would be for the BTS market.

Part 2: response to consultation questions

Chapter 3: Scope

Question 1 : Is this definition a reasonable basis for identifying residential property in scope for the tax? Will companies be able to identify profits in scope using this definition?

31. The build to sell (BTS) residential market is, in almost all material factors, an entirely different and distinct market from purpose built rental assets, like BTR & PBSA , producing different housing stock for different markets and operating under entirely different market conditions. A tax regime that does not distinguish between these markets is likely to create distortions that fundamentally disadvantage one of these markets.

32. Extending the scope of this tax to investment asset classes like BTR and PBSA will add significant complexity in the rules, potentially for very little tax take, given purpose built rental asset classes only account for around 2-2.5% of new residential supply each year. It will also disproportionately impact on the viability of development of new homes for rent, because it will act more like a levy that a tax on true 'profits' - as such, these investment asset classes should be carved out.

What are "development profits"?

33. It is reasonably well understood what is meant by 'residential property' – albeit there is a lack of clarity in respect of the government's intentions for some communal asset classes like student accommodation, and the treatment of retirement homes (which are touched on in separate questions later). However, there is greater uncertainty around what the government might consider to be "development profits" in practice – this will create some uncertainty around which profits should be within scope, and which party in a development project may be within scope.

34. To illustrate this further, the 'development activities in scope' listed on page 10 of the consultation could be carried out by several different entities along a development lifecycle, and even when a development is developed 'in-house', it would not be uncommon for any number of those activities to be contracted out to a third party. This has the potential to generate significant uncertainty, and as such, government must be clear on exactly which element in this supply chain these are seeking to tax.

35. In particular, clarity would be welcome on the following scenarios:

    a. Gains made on land sold with residential planning permission.

    b. In house construction activity.

    c. Forward funded arrangements, where a third party developer carries out a development on behalf of the long term investor (as is common for BTR and PBSA developments).

36. We would also note that we do not think it is helpful that construction has been included on the list of in scope activities, and yet third party construction activity is carved out. This has the potential to distort commercial decisions when deciding between in house vs third party construction companies.

Question2 : Do you agree with the approach to affordable housing? What are the implications for housing associations and to what extent would their taxable activities fall in scope?

37. We consider that it would be simpler to include affordable housing within scope, particularly affordable housing contributions as part of S.106 obligations. These are predominantly built at cost, or at a loss, and as such, the losses generated from the affordable housing contributions should be factored into the overall "profit" of a residential development – in order to ensure that the profits subject to tax are as close to the true economic profits as possible. Furthermore, it could prove challenging to carve out the affordable element of a BTR of PBSA development when valuing a whole PBSA or BTR block.

38. However, we are mindful of implications on business models whose primary focus is on the development of affordable housing – and given the government will not want to jeopardise viability of affordable housing, it may be appropriate to consider a carve out in these cases – e.g. where a business generates say, over 50% of their profits from these activities, or perhaps a carve out linked with registered provider status.

39. We also have wider concerns that this tax will have implications for the supply of affordable housing contributions, because the viability of other residential developments will be compromised. In particular, given BTR investments typically have very slim margins, if this tax has an impact on viability calculations, this will indirectly have negative impact on the amount of affordable housing that can be delivered for BTR developments in scope.

Question 3: Do you agree with this approach to communal housing?

40. We agree with the proposal to exclude certain communal dwellings from the charge. As touched on below, we consider that retirement villages with care and purpose built student accommodation more broadly should be covered by this exclusion.

41. In addition, we consider that the government's rationale for excluding communal dwellings would apply equally to BTR housing – in particular, page 9 of the consultation sets out that an exclusion for communal housing is justified because it has "different characteristics relative to the broader housing market and will not derive benefit from the government's interventions". This rational equally applies to rental asset classes, like BTR and PBSA, which behave very differently to the wider residential market, and have not received the same government support. As such, this rational would further support extending a carve out for these purpose built rental assets.

42. Other asset classes which have elements of investment and communal living characteristics including shared ownership and co-living developments – it would seem appropriate to extend a carve out to these assets as well.

Question 4: Do you agree with this approach to student housing?

43. We would support a broader carve out for purpose built student accommodation.

44. Given the evolution of the student accommodation sector in recent years, it is important that the rules and definitions reflect modern accommodation for students – but also, that the definition does not draw an arbitrary line which could distort the market. In particular, "cluster flats" are increasingly common designs – typically providing a number of en-suite bedrooms which all have access to a communal kitchen and living space. You can also have en-suite

studios, with communal facilities that are not interconnected with the flat. In order to ensure that similar business models are not discriminated against, we would urge government to consider a broad carve out for student accommodation. Like BTR, most student accommodation will have planning prohibitions to ensure that it remains in student use, and so any exemption could be defined in those terms.

45. In addition, the wider PBSA market makes an important contribution to housing supply, and plays a huge role in the success of our Higher Education sector more broadly. In particular:

    - If PBSA is supported – we estimate that 77,000 traditional family homes would be freed up for the wider market, making a significant contribution to housing supply.

    - Appropriate accommodation for students plays a key role in the success of our wider Higher Education sector – a huge export industry which attracts students from around the world.

    - There is a recognised shortage of adequate student accommodation in London and other UK cities: PBSA investors work closely with UK universities to provide good quality and affordable accommodation in the right locations. RPDT will add to the commercial pressures on PBSA development and potentially restrict growth in the education sector.

46. We would draw your attention to Student accommodation; The Facts[5], which should prove useful it determining an appropriate carve out for this sector. It is a paper prepared by sector experts which seeks to set out some common definitions in the student accommodation sector, and provide a broad overview of the market. We have included an extract in Appendix 2.

Question 5: Is there an alternative to the approach described for retirement housing, which considers provision of care and allied services, that should be considered?

47. We are concerned that there is some ambiguity in the consultation in respect of what is intended to fall within scope. We understand from member interaction at stakeholder events that the intention is for a limited carve out, which would not include purpose built housing for older people, particularly models that include the capacity to deliver varying levels of care on site.

48. There is a huge undersupply of all retirement housing in the UK. Given the potential for this sector to play a huge role in releasing traditional family homes back to the market, as well as alleviate growing pressures on the NHS and social care system, we consider that government should be considering a broad definition to carve out housing for older people, particularly where care and service are provided to residents.

49. This is another sector that has seen huge evolution is recent years, as such any definitions should reflect common designs and practices. We published a report[6] last year which quantifies the undersupply of suitable elderly accommodation in the UK, and seeks to define some of the modern offerings in the sector, which we hope will be useful in developing an appropriate carve out.

[5] https://www.hepi.ac.uk/wp-content/uploads/2020/08/HEPI-Student-Accommodation-Report-FINAL.pdf

[6] https://bpf.org.uk/media/3305/bpf-housing-and-care-for-older-people-report.pdf

50. Developments with care on site are commonly referred to in the sector as "housing with care", and we would support an exclusion for these types of developments in particular, given the significant role that care and the capacity for delivering care to residents plays in the physical structure and business case for such project.

51. There is another cohort of retirement living schemes in the market known as "housing with support", which offers a lower level of integrated care than "housing with care" schemes, aimed more at people in early retirement who are still able to retain more of their independence.

52. A definition could be based on the modern trends in retirement housing set out above of "housing with care" and "housing with support". Alternatively the planning system could provide a useful basis to define a carve out, as senior living schemes commonly include requirements associated with the provision of onsite care, communal facilities, and a range of integrated support as part of their planning consent – or a wider carve out for C2 use class could also be considered until such a time as a specific planning definition is established for purpose-built homes for older people.

Question 6: Are there additional forms of communal housing that you believe should be excluded from the definition of residential property activity for the purposes of the RPDT?

53. We would encourage a broader definition as possible for both PBSA and retirement living communities to be carved out of RPDT. Both asset classes contribute housing supply for different demographics where we currently have acute shortages of appropriate housing. By providing more appropriate housing for students and our elderly populations, more stock of family homes will be released into the market, therefore contributing to broader housing supply.

54. As touched on above, we also consider that investment asset classes which have been purpose built for rental, like BTR and PBSA, should be carved out following the same policy rationale as for other communal dwellings – in particular, they have "different characteristics relative to the broader housing market and will not derive benefit from the government's interventions" (rational extracted from page 9 of the consultation).

55. New asset classes will continue to evolve and the rules should be adaptable to accommodate new products on the market. For example, other relatively new asset classes which have elements of investment and communal living characteristics including shared ownership and co-living developments – it would seem appropriate to extend a carve out to these assets as well.

Question 7: How should income from the development stage of build-to-rent activities be measured for the purposes of the tax? Do groups already recognise build-to-rent income in their development profits? On what basis?

How is a BTR development valued?

56. By way of background, a BTR development is valued based on the notional rent assumed on completion of a development, which deducts the operational costs (given there is no service charge recovery for a landlord for BTR). This results in a net rent that then gets capitalised to provide a notional (not realised) value at the end of the development period. There are no sales of units (and therefore no interim profit). Therefore it takes many years (typically 20 years +) for a landlord to pay back its original construction costs as it only has a rental income. Adding a further tax burden into the valuation would make the already marginal returns unattractive and

discourage development – which would potentially discourage the investment from taking place, or have a detrimental impact on affordable housing contributions.

57. Significant complexity and uncertainty arises as a result of the proposed taxation of notional gains on the completion of an investment asset (like BTR). There is no sale of the units of this building to a home owner, so determining a fair and equivalent "profit" on development, which compares to a build to sell model, will be very challenging. In particular, valuation gains and losses can be influenced by a number of factors – for example:

    a. Inflation on land values over period of ownership

    b. Planning permission uplifts

    c. Uplifts in value following the development

    d. Uplifts as a result of wider regeneration of the area including infrastructure investment

    e. Level of occupation – a vacant BTR block will be worth less than a fully let block

    f. Track record of the manager (this will often factor into a lender's valuation) – and links to their ability to maintain low levels of vacancy across the development.

58. Splitting out these factors will be difficult and subjective – and will likely require third party valuations. Such subjectivity will require significant resource from both the tax payer and HMRC – and will likely result in high levels of disputes.

59. Additional complexity arises in BTR and PBSA development models where a funding model known as "forward funding" is very common (more detail on this in appendix 1). In this case, a number of the development activities within scope of the tax are carried out by different parties, so some clarity will be needed to understand which party should be liable for the tax.

60. Splitting out which part of the valuation relates purely to development activity will be difficult and highly subjective – and for the most part, will generate very low levels of taxation, particularly for rental asset classes.

61. The complexity and uncertainty will also impact on viability assessments, which will generally have to consider a 'worst case scenario', thereby having a disproportionate impact on production of homes from the rental sector in the medium to long-term, alongside affordable housing components required to be delivered as part of the planning process.

62. The complexity of extending this tax to an investment businesses, and the penal nature of a dry tax charge on a notional gain would be wholly disproportionate, and justifies an carve out for investment assets, like BTR and PBSA.

Question 8: What are the implications of models 1, 2a and 2b for businesses?

63. Model 1 (the company based approach) could provide an element of simplicity which may appeal to more straight forward businesses which carry out predominantly residential development activity. However, we are concerned that a mixed use developer (that develops a combination of commercial and residential development), could be in a position where they need to carry out significant administration and compliance, simply to determine whether or

not they would be within scope of this tax – and potentially end up paying tax on profits derived from commercial development activity, which is not the target of these rules.

64. We consider that model 2 (the activity based approach) will be fairer for businesses which carry out a mixture of activities – ensuring that only those profits relating to residential development fall within scope.

Question 9: Which approach is preferred?

65. We would recommend model 2, using tax figures, rather than accounting figures. However, it could be optional for businesses to elect to apply model one, where this would simplify their compliance obligation.

Question 10: Which of these would be administratively easier for major residential property developers to operate?

66. As noted in our response to question 7, both approaches will be incredibly complex for BTR and PBSA developers and investors – because the valuation of notional profits relating to a residential development will be challenging and subjective, and it will require such businesses to record 'profit' in a way that is not currently captured as current legislation does not require activity to be accounted for or taxed in the manner proposed. The main administrative concern is that businesses will have to run two sets of tax calculations to generate the tax basis for both RPDT and Corporation Tax.

67. While model one would be administratively simpler for those developers that carry out predominantly residential development, it risks creating a huge cliff edge for some businesses with mixed activities. This cliff edge should be avoided; hence our preferred approach would be model 2.

Question 11: Where should the significance test be set for model 1?

68. If government decide to go with model 1, the significance threshold should be set at a very high level, to limit the number of businesses that could be impacted by the cliff edge. There is precedent from the Corporate Interest Restriction Public Infrastructure rules (PIE) which suggests that 'significant' would be in the region of 90% - we would suggest that the threshold should be no lower than this, otherwise potentially large sums of profits relating to non-residential development activity risk being brought within scope.

Question 12: What would be the best approach to achieving an apportionment for income and expenditure that is fair without being unduly burdensome?

69. We consider that a fair approach is one that targets genuine economic profits – to that end, it would be disproportionate to impose this tax on investment properties – and in particular, a dry tax charge on notional profits would be particularly punitive. As such, we recommend that investment assets like BTR and BSA should be carved out of the charge.

70. Furthermore, we consider that the RPDT should be a surcharge within corporation tax on trading profits from residential development which is in scope.

71. If government are concerned that business models would temporarily switch to investment asset classes in order to mitigate this tax, there is precedent for appropriate safeguards within

existing tax and planning rules. For example, it would be possible to relatively easily apply something similar to the protections in the REIT rules for disposals of assets shortly after construction is completed. Any in scope building which is sold within 3 years of a development could automatically be treated as within scope of RPDT – regardless of whether it was intended for investment, or simply a higher rate of tax could be applied to those gains/profits.

72. Alternatively the planning rules already allow for local authorities to claw back some of their affordable housing contributions which would otherwise have been due if a developer changes the use of their development (e.g. from BTR to BTS) within say 10-15yrs of completing a development – this mechanism could also provide some helpful precedent for an appropriate safeguard.

73. Corporation tax already distinguishes between trading and investment returns – as such, this would also cause the least additional administrative burden to taxpayers, and crucially not change the finely balanced economic position for those undertaking BTR development activity.

74. There are already established mechanism for 'just and reasonable' apportionments within the tax system that can be utilised here. We would not support any further restrictions to interest costs and losses (as we consider the existing restrictions within corporation tax are already punitive).

75. It is also worth noting that generally capital allowances aren't available to developers (or to a lot of residential property), so this would reduce the complexity of any just and reasonable apportionment of taxable profit.

Question 13: To help inform the design, what are the sector's expectations for future losses?

76. No developer or investor would embark on a development if there was an expectation of a loss.

77. It is worth noting that the in-house BTR sector will generally account for and be taxed on its business on an investment basis and accordingly will be required to recognise profits and losses as they arise, rather than a BTS developer that will generally only recognise costs when proceeds are generated.

78. Therefore, a BTR investor will be heavily penalised by a restriction on losses, as it will generally make losses during the development phase of the building - from interest costs, marketing costs and a variety of other costs in the year(s) prior to completion of the property being constructed. (It is worth noting that this is a slight generalisation, and there will be some BTS businesses will also be penalised by a restriction on losses, but from a sectoral perspective , it is likely that the BTR sector will be more heavily impacted).

79. Furthermore, it is also interesting to note in this context that while each development will be a little different, a BTR investment will typically only 'break even' after about 10 years, and in some cases up to 20 years post development.

Question 14: Do you consider there is any method of allowing carried forward losses, which can provide both fairness and minimal administrative burden?

80. It is essential that losses in relation to a development can be factored into the profits subject to tax. Developments of scale will take several years to complete, from purchasing land, getting planning permission, construction, marketing etc. Throughout this period, costs will be incurred

which will generate losses – and in the BTR context, it is very common to use loan financing, so the interest costs incurred over this time will also generate significant losses. In order to ensure that true economic profits are subject to tax, as a minimum, losses which have been generated in respect of a development must be able to be offset when calculating the taxable profits.

81. Businesses will be able to track all the costs and losses associated with the development phase – indeed, that is how they would calculate their economic profits.

82. As noted in response to question 12, we would suggest that leveraging off the existing corporation tax system and applying the RPDT to trading profits from residential development which is in scope would be the simplest and fairest approach.

83. The existing loss relief rules would apply – and taxpayers would be required to make a fair and reasonable apportionment between residential development trading activities which are in scope, and other trading activities, to the extent they have completed a mixed use development, for example. Any additional admin burden would be worth it for a business where the amounts involved are material. If amounts involved are immaterial for a business, and the admin burden is not justifiable, they could simply elect not to use any carried forward losses.

Question 15: What are the implications of excluding interest and funding costs from the measure of profits for RPDT purposes?

84. It would be damaging to any business which uses debt finance. Interest costs are a genuine cost of business – and therefore restricting interest costs would impose a higher effective rate of tax on those businesses which have used debt finance – the tax would move away from a genuine tax on profitability, to be closer to a tax on sales or even more akin to a levy in the case of the tax imposing a dry tax charge.

85. For BTR developments, particularly for BTR in-house development, the absence of interest and funding costs, fundamentally ignores the economics of this type of development. The ability to borrow development money more cheaply and for shorter periods of time is what makes in-house BTR product quicker and ultimately more affordable to construct, thus delivering more houses more quickly to the UK market.

86. There is also a risk that not allowing losses generated by interest costs would further distort the impact of this tax for BTR developments – because the in-house BTR sector will generally account for and be taxed on its business on an investment basis and accordingly will be required to recognise profits and losses as they arise, rather than a BTS developer that will generally only recognise these costs when proceeds are generated.

87. By way of example, if we take a £200m residential development (possibly c350 apartments) at 50% leverage, with an 8% interest cost. For an investment (BTR) developer that could be as much as £8m of losses recognised in 1 year during the development phase that would be treated as an unutilised loss. A trader would realise all of this cost against income as it is released to the P&L and therefore their profits subject to this tax would immediately be £8m lower on an identical development appraisal, simply as a result of the decision to exclude tax losses.

88. The huge disparity in taxation methodology between BTS (trading) and BTR (investment) development means that excluding the use of brought forward losses is not only unfair but

actually extends the tax base for investment businesses compared to trading businesses. This is on top of the unfairness of having to pay tax on profits that have not been realised.

89. The BTR sector is still in its early stages of maturity and it is still competing against traditional large BTS developers to find suitable land on which to build. To impose an effective higher rate of tax will stymie development of the sector and ultimately lead to lower numbers of homes being built, and a slow-down in the professionalisation of the UK rental sector.

Chapter 4: Allowance and rate

Question 16: Do you agree that the same approach regarding treatment of carried forward losses for the calculation of the profits for the tax should apply for the calculation of profits for the allowance?

90. No, we consider that it should be possible to carry forward the allowance (and likewise we consider that it should be possible to carry forward losses). The tax should focus on the overall profit of a development, and should not depend on the timing of the sales or completion – otherwise the government would risk creating an incentive to slow down and smooth out build out rates.

91. BTR investors are already incentivised to complete their BTR development as quickly as possible – to ensure that they can start generating rental income as soon as possible. In contrast, a BTS business will typically spread out the construction of a large site, to avoid saturating the market, as this would negatively impact on the price of their product. To that end, on a comparably sized site, a BTR developer could be penalised for building out the whole site at once, while a BTS business may take several years to build out a sell a comparably sized site.

Question 17: Do you think it is more appropriate for the definition of a group for the purposes of this tax to be based on a tax rule or an accounting standard?

92. If this tax is due to apply to joint ventures, as well as corporate groups, accounting definitions are probably better as these are defined and consistently applied in accounting standards.

Question 18: Which existing definition of a group for tax or accounting purposes do you think would be most appropriate for this purpose?

93. If it based on accounting definitions – the consolidated group would seem appropriate.

Question 19: What rules, in addition to your preferred group definition, do you consider would be required to ensure that the threshold is applied to a single economic entity?

94. It would be helpful if widely held entities can elect to be treated as a 'single economic entity' in their own right, and perform any compliance in relation to this tax in the entity itself, rather than be required to report details to investors above. For a widely held entity, the compliance burden of reporting to a large number of investors would be significant.

Joint ventures

Question 20: What would you consider to be appropriate measures of economic participation in a joint venture?

95. The corporation tax rules apply to joint ventures in a number of existing ways including for the REIT rules and the corporate interest restriction rules - whilst these may not be perfect they are at least understood by the industry.

Question 21: What would you consider to be an appropriate hurdle for a participator becoming liable to tax in respect of the joint venture?

96. See response to question 20 – if we can align with existing tax rules on the treatment of joint ventures, this would be preferable.

Question 22: Do you have any other observations regarding the use of joint venture structures in the UK residential property development sector?

97. Joint ventures are incredibly common for investment property – both large scale commercial and residential rental asset classes. They are an incredibly effective way to share resources, leverage off expertise, and spread risks.

98. We agree that a mechanism to ensure that there is no double tax for the JV entity and the participators will be important.

99. It will also be important to ensure that tax exempt investors, like pension funds, are able to retain their tax exempt status, even when investing through a joint venture arrangement.

Question 23: Do you agree that these principles should guide the decision on the rate of the tax?

100. These principles of tax design seem reasonable – and should also guide decisions in respect of the base of the tax.

101. Based on these principles, we consider that rental asset classes, like BTR and PBSA should be carved out of the tax – or at the very least the tax should apply only to trading profits within corporation tax – to ensure that only those businesses making genuine economic profits fall within scope.

102. As currently proposed, the tax would have a disproportionate impact on BTR investors and developers, which would negatively impact on viability of development of this asset class, and associated affordable housing contributions. Given the potential contributions this sector could make to housing supply, and the associated improvements to the professionalisation of the rental sector, this would be contrary to government's wider objectives on housing.

Chapter 5: Interaction with the Gateway 2 levy

Question 24: Do you have any initial views on the cumulative impact of the RPDT and the Gateway 2 levy?

103. It will be helpful to understand the thinking behind the need for a difference in approach to these two taxes, so further detail will be welcome in due course.

104. Given BTR developments are typically higher rise than BTS developments, they will be caught more r by a levy targeted at high rise development. This further justifies the carve out for BTR we have suggested and will ensure a more even impact between BTR and BTS developers.

105. By reducing the viability of higher density developments in urban settings the government will encourage urban sprawl into more greenfield areas. Also, BTR developments are usually built to a very high sustainability standard as institutional owners demand a future-proofed asset over an extended period of time. Disadvantaging this housing type will impact the government's ability to deliver its sustainability agenda alongside its housing agenda.

106. This adds further justification to a carve out for BTR and PBSA developments from the RPDT charge. Alternatively, a mechanism to offset one charge against the other to ensure businesses do not suffer both taxes on the same development would be fairer.

Chapter 6: Reporting

Question 25: Do you agree that the RPDT should be reported using the same periods as for CT?

107. Whilst RPDT continues to be linked to profits then there is no sense in de-coupling reporting periods from normal CT periods. (Indeed, as noted previously, we would advocate for full integration of this tax within CT – by simply adding a surcharge to trading profits from residential developments which are in scope.)

Question 26: Do you see any difficulties applying the CT rules for accounting periods to any of the models and if so, how could they be overcome?

108. There will always be anomalies in relation to taxing profits on long-term projects across multiple years, but this is a consequence of our tax system. However, it is generally understood and accepted by business and HMRC alike.

109. The main concern is around how notional profits might be derived and determined for businesses that do not account for profits or who transfer assets between group companies for very legitimate purposes. In our experience any transfer pricing or valuation based methodology is highly likely to be uncertain and could generate a high number of enquiries from HMRC. If the proposals for this tax are to proceed with an intention to tax notional, unrealised profits there has to be a mechanism to provide business with certainty that the transfer prices or valuations used to determine the tax base will not be subject to years of challenge and uncertainty. Ideally this would need to be reflective of the basis of profits that BTS businesses will be taxed on so as not to create further anomalies in the impact of this tax beyond the many already noted in this response.

Question 27: For models 1 and 2a would there be any difficulties for a given company in knowing that the group's thresholds for the RPDT have been satisfied?

110. Under both models there is likely to be a great deal of uncertainty for all but the largest housebuilder groups as to whether or not the tax will apply and if so to what extent. We question whether the potential tax revenues raised from those smaller developers warrants the creation of such uncertainty for so many medium sized businesses at a time, and in a market where competing with the largest BTS developers for land opportunities is so difficult.

111. Profitability can be significantly affected by a range of commercial factors such as delays to or advancement of completion dates of buildings. For large schemes this could delay or advance the tax by a full 12 months, or be the difference between it applying or not. Once again it is likely to be medium to large investor groups that will face this uncertainty as by definition completion dates for housebuilders tend to be staggered across a large project and equally, sales of properties will not all be triggered on the same date. A developer of a large apartment block for rent will generally sell the entire block of apartments on a single day.

112. Depending on how the 'group' definition is formed there is also a possibility that two or more entirely separately managed and financed businesses could have a common owner that might mean that collectively the threshold is met. It would likely be unclear to either group what the other was doing or reporting.

113. It could also be challenging for some fund structures – for example, where a fund is managed ostensibly separately from the investor.

Question 28: If there is a requirement for separate registration, is 90 days from the end of the accounting period a reasonable timeframe?

114. 90 days is much too soon after the end of an accounting period. Accounts have to be filed within 9 months of the end of the year and as the tax will be referable in some form to profit, the registration should not be required before the accounts are finalised. As such, closer to 12 months after an accounting period ends would be more appropriate.

Chapter 7: Payment and Compliance

Question 29: If possible, would including RPDT amounts within quarterly instalment payments be preferable? Or would this create any issues?

115. Development and completion dates are somewhat uncertain so it is possible (again mostly for medium sized developers) that the RPDT could apply in a different period than expected, sometimes at relatively short notice. Funding the tax at short notice might be problematic for some developers, and will also cost developers that have paid it in advance, as the interest it would obtain from HMRC would be vastly lower than that which the group is likely to be paying to a lender. Excluding it from Quarterly instalments is likely to be preferable for those groups that will face huge uncertainty over whether it will be applicable or not.

116. If government are minded to include payments within quarterly instalments, a potential compromise could be that the rate of interest applied to late paid RPDT is lower given that the profits may only arise at the end of an accounting period.

Question 30: Do you agree that allowing a nominated company to act on behalf of the group would reduce the compliance burden?

117. It would generally be preferable, but for some groups, and particularly those with JV's it may not be suitable for a one-size fits all option. It should be possible for an entity to elect for a fellow group company to be responsible for its tax, but it should be flexible to allow an entity to elect out and perform their own compliance.

Question 31: Do you foresee any difficulties with the nominated company calculating and reporting RPDT liability on behalf of the whole group?

118. Where a Group is managed entirely separately, perhaps due to common ownership by a PE or institutional fund investor, this could be impractical. Similarly, it may be difficult in joint venture situations.

Question 32: Are there any practical issues around the nominated company accessing information from the rest of the group?

119. No comment.

Question 33: Would specific rules be needed for companies whose AP does not coincide with the nominated company's AP?

120. No comment.

Question 34: Do you have any comments on the proposed commencement date?

121. For the tax to be levied on profits arising after 1 April 2022 is significantly penal for those developing rental assets in-house and on medium sized developers who are unlikely to have time to prepare adequately for the tax. By definition, property development takes time so the first profits to be taxed will relate to developments that are already underway, and in most cases, will be subject to financing that has been fixed in advance.

122. For BTS business models, where this tax is more likely to target genuine economic profits, the timeframes may be more manageable, albeit still very tight. However, if the tax is to go forward with the intention to tax notional profits on investors that develop new rental homes, then we would suggest that there will need to be a grandfathering arrangement for these developments – whereby those developments that have already started before the legislation is laid (or at the very least before the date of this consultation), would not be caught by this charge. This would ensure that any future developments can factor in this dry tax charge as part of their viability assessment – and ensure that financing arrangements are in place to fund it.

123. It appears to be the case that the initial concept behind the tax was to tax the very largest residential developers in the UK, almost all of which are taxed as traders, and by definition the calculation of profits is relatively straightforward. The concept of including businesses taxed as investors, would appear to be generating a much more complex and dual basis of taxation. If it is decided that investment businesses should be included in the scope of this tax it must be done appropriately and therefore the proposed timetable is too tight to fully develop and test the new tax regime and associated new tax concepts that will be needed to levy the tax on investment businesses. We would call for a delay to the tax for those businesses so that the legislation can be fully tested and consulted on.

Question 35: Do you have any views on avoidance risks generally, and how these should be minimised?

124. We consider that risk as alluded to on page 11 of the consultation (that developers will seek to rent properties briefly on completion before selling) is completely unfounded. The costs and other complexities of doing so are so significant that this would not happen given the size of business that this tax is aimed at.

125. If government are concerned that a trading business would pretend to change to an investment business to avoid this tax, there are already mechanisms within the tax and planning rules which could provide a helpful precedent to address these risks, in particular:

a. Similar to the REIT rules, any residential property which is sold to a third party within 3yrs of practical completion could automatically fall within scope of the RPDT – regardless of whether it was originally intended as an investment asset. (There could be a carve out for transactions of 6 or more dwellings in one go, akin to the SDLT multiple-dwellings relief, to help identify sales to another investor).

b. Or there is a clawback mechanism within the planning rules – whereby a local authority can clawback s.106 contributions from a developer where the use of the asset changes within a certain period of time after the development. E.g. if a development changes from build-to-rent to build-to-sell within say, 10 years of a development, this could cause a clawback to be imposed.

c. The tax rules also include the so called "Transactions in land" provisions which seek to override investment treatment where land is developed with a view to sale but the 'investor' realises a capital gain perhaps through a sale of shares etc.

Question 36: Do you have any observations on the proposed anti-avoidance provisions, or other avoidance risks?

126. They seem a little over complicated, and focus on fairly unlikely scenarios.

Question 37: Do you think it would be necessary to introduce additional rules to ensure compliance or to make administration of the tax easier?

127. By extending this tax to all developers of residential property, particularly developers of investment properties (like BTR and PBSA) that will become subject to tax on notional profits whether or not that property is sold – this will generate a huge level of additional legislation, uncertainty and anti-avoidance measures. This will dramatically increase the burden on tax payers and HMRC to manage this tax effectively, for relatively limited tax revenues, given BTR only represents 2-2.5% of new housing supply.

128. Furthermore, it would have a disproportionate impact on viability of housing delivery in the rental sector. For these numerous reasons we do not think that the impact on viability of new rental homes, as well as the additional complexity and administration can be justified by the relatively small amounts of tax that will be raised by extending the scope of the tax to rental asset classes, like BTR and PBSA.

Chapter 8: Assessment of impacts

Question 38: Would you adjust your development plans, build out strategy, or land acquisition strategy in response the implementation of this tax? If yes, how?

129. This tax would have material implications for commercial decisions for BTR schemes, as returns are already marginal and generated over the long term.

130. There are a number of possible options that a business may consider – particularly if a business is unable to afford a dry tax charge:

a. Where possible, a business may seek to slow down build out rates, to minimise the tax that could be due each year – or to maximise the benefit of the £25m allowance.

b. A business may seek to dispose of the land prior to commencement of construction.

c. In extreme, it may be that certain developments are entirely unviable as build to rent, or it may be that the mix of non-residential property at a site might be increased, as it might be necessary to build and sell more commercial property to fund the remaining residential elements.

d. The quality of development required for institutional investment in BTR, either keeping the building in-house or sale to a small market of long-term repeat clients, means compromise on build quality is less prevalent in the BTR sector but there may be an impact on amenities that a development is able to offer.

e. Viability assessments for affordable homes will be impacted by this tax and the Gateway 2 Levy, meaning that to maintain similar levels of viability, fewer affordable homes will be possible on developments that can go ahead.

Question 39: Are there other ways you would adapt your development plans in response to the implementation of this tax? If yes, how?

131. No comment.

Question 40: Are there other potential impacts on housing supply?

132. As illustrated throughout our submission, these proposals will have a disproportionate impact on the BTR sector. It will put BTR investors in an even less competitive position when bidding for land – and it will affect the viability of new BTR developments and the affordable homes quotas that many developers can support and develop.

Question 41: Is there anything further the government might want to consider in relation to the design of the tax which would help minimise the impact on housing supply? Or other housing policy objectives?

133. We would suggest that investment asset classes (like BTR or PBSA) should be carved out entirely (or at worst their inclusion delayed) to provide time to truly determine the impact of this tax on this entirely separate sector.

134. Furthermore, we consider that it would be simpler to apply this tax to trading profits within corporation tax (with appropriate safeguards to mitigate the concern that a business would change their business model in the short term). This would ensure that the tax is targeted at true economic profits.

Question 42: Is there anything the government might want to consider with regards to the impact of the tax on the supply of affordable housing?

135. The impact of this tax and the Gateway 2 levy needs to be fully analysed and understood, however a very simple fact is inescapable, which is that the more the development of

residential property is taxed, the fewer affordable homes that developers will be able to support as part of their viability assessments.

Question 43: Do you have any comments on the summary of impacts

136. The UK residential investment sector has been incredibly successful in recent year at competing for institutional and international capital – which has been deployed in cities across the UK, helping to regenerate our towns and cities. This tax is another cost of investment that will reduce returns for investors, which will limit the institutional and overseas capital coming into the UK, and reduce viability of new developments.

137. In light of the innumerable benefits that BTR can bring to the UK's housing supply and wider government priorities, investment asset classes, including BTR and PBSA should not be within scope of this tax.

Appendix 1: BTR vs BTS funding models – and explanation of 'forward funding'

2. We are aware of a number of different funding models for BTR developments, as set out below:

A. *"**In-house**": BTR long term owner owns the land and carries out the development with an in-house development function.*

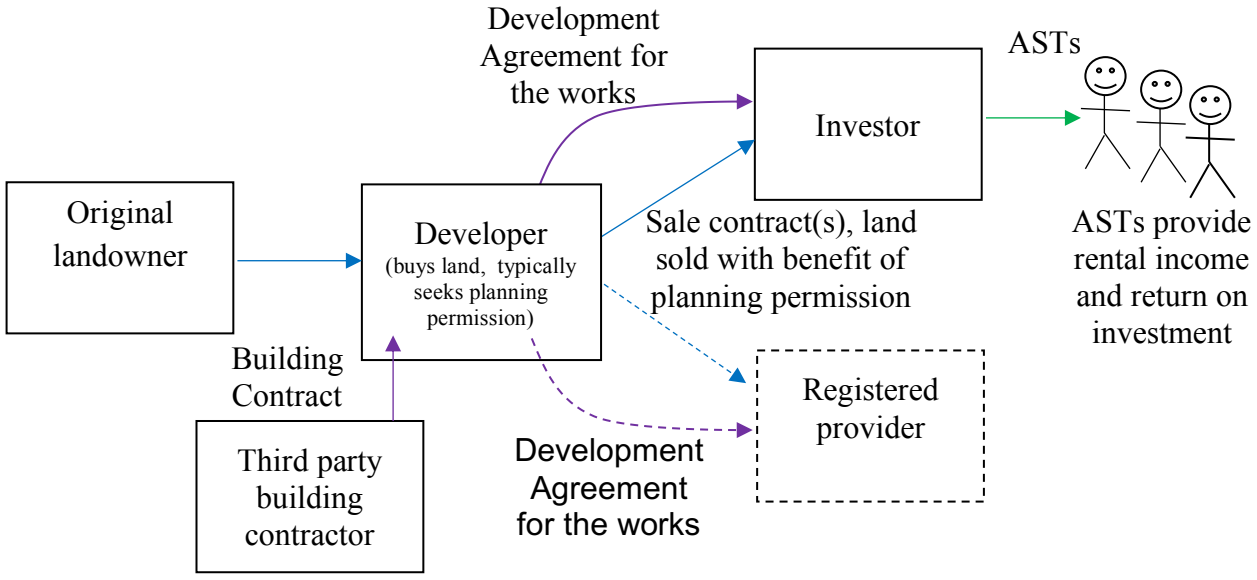
B. *"**Forward funding**": BTR long term owner pays a third party developer to develop a site. There were a few variances on this model – because the long term owner may acquire the land at different points – typically either:*

- **a.** *When planning permission is granted;*
- **b.** *At golden brick (typical for affordable housing developments).*
- **c.** *Or the long term owner owns the land throughout.*

C. ***Forward purchase agreement:** The long term owner would purchase the land and building from a third party developer only once the development is finalised.*

3. An explanation of a forward funded model is set out in a little more detail below, with a comparison to a forward purchase and build-to-sell models for information.

Forward funding



4. In a typical forward funded arrangement a developer will acquire land and will obtain the BTR planning permission. Instead of borrowing to fund the development and selling at practical completion it will sell the land early to the investor (with the price taking account of the planning permission) and enter a development agreement with the investor pursuant to which the developer (or a connected party) will agree that once the land sale completes it will act as developer and construct the building for the investor. The developer will take development risk and typically receives payment for the works plus a development bonus.

5. The investor will commit to pay an overall maximum for the land, the works and the bonus.

6. The developer may enter equivalent arrangements with a registered provider in relation to any affordable housing blocks at the development.

7. The developer will typically enter into a building contract with a third party contractor to carry out the actual works for the developer.

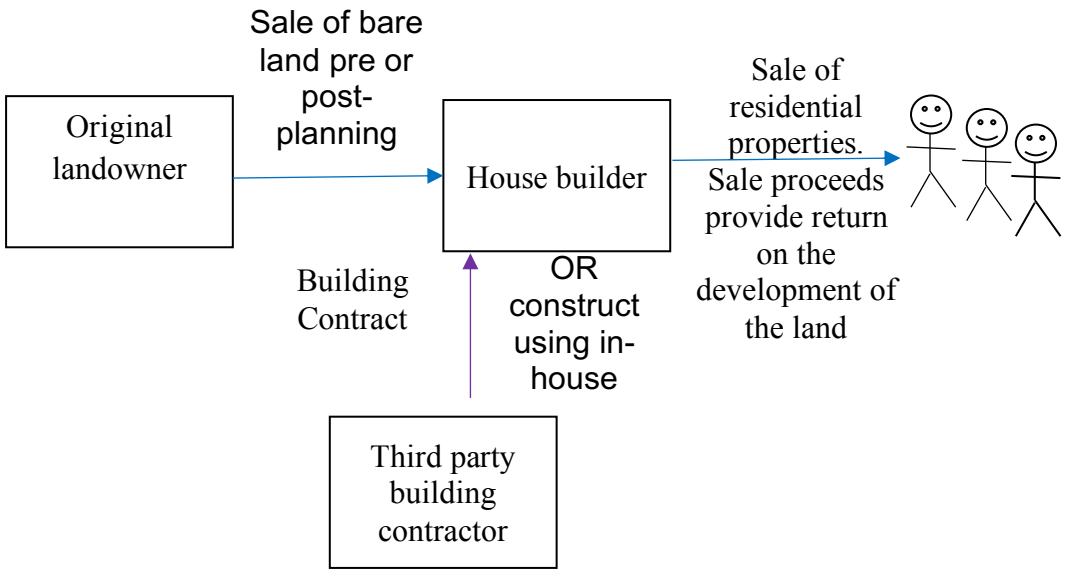
8. Once the building is practically complete the investor will operate and let residential units to residential tenants on assured shorthold tenancies. Before the lettings commence, it may grant a lease to a connected party so that it has a separate operating entity and typically that lease is a long lease at a turnover rent.

9. The land may transfer as bare land or later at so called "golden brick" when the dwellings will be seen as "in construction" for VAT purposes. In the latter scenario the land is sold at "golden brick" for a price that reflects the base land value and the works carried out and the developer agrees with the investor to complete the construction of the building from "golden brick" to practical completion under the development agreement. [Reaching "golden brick" enables the sale to be zero-rated for VAT purposes].

Forward purchase/forward sale agreement

10. In a forward sale arrangement a developer will obtain BTR planning permission and will contract to sell the completed building to the investor (with the contract entered into before the building is completed). The investor may make instalment payments in advance of completion (which are then used by the developer to fund the works) albeit the transfer of the land will not take place until the building is practically complete.

Build to sell model



Appendix 2: Room types and building configuration in the PBSA sector

Typical room types within purpose-built blocks (university and private): illustrations

Taken from Student Accommodation: The Facts

Room Type	Standard	Ensuite	Studio Room
Kitchen	Shared	Shared	In room
Bathroom	Shared	In room	In room
Typical style	Off corridors	Cluster flats	Corridors of studios
Number of rooms (UK -2018)	78,000	232,000	36,200
Notes	The traditional room type and stock vary in size, fit-out and quality. Some rooms have a wash-hand basin. Rooms can be catered or self-catered. Mainly university-owned.	Self-catered, ensuite rooms are the largest stock type in the sector. Size of rooms, social space design, quality of fit-out and bed size vary with price.	The smallest proportion of rooms but the fastest growing stock type due to high rents and commercial favourability. Mainly private sector provision, housing many international postgraduates.

Room format	 *University of Reading*	 *University of Reading*	 *Sanctuary Student*

The sector also includes:

• Flats: one- to three-bed flats or apartments for rent individually or by couples / families;

• Townhouses: a newer (hybrid) accommodation type. A three- or four-storey house, shared by eight to 12 students, with the ground floor dedicated to kitchen and shared lounge facilities. It echoes an off-street property design, but is newly-built, typically on-campus.29 Townhouses have gained popularity because they lend themselves to sociability and are slightly cheaper than en-suite. Bathrooms are shared by two students; and

• Variations on the studio model: there are some rare adaptations of room configuration such as twodios, where students share kitchen facilities.