Written Submission for Pre-Budget Consultations in Advance of the 2024 Federal Budget

CANADIAN RENTAL HOUSING PROVIDERS FOR AFFORDABLE HOUSING

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Submitted: August 4, 2023

2024 List of Recommendations

Recommendation 1: That the government create a fund and financing program to allow non-profits, cooperatives and community land trusts to cost-effectively acquire existing rental housing properties, making them permanently affordable.

Recommendation 2: That the government develop a stable and predictable regulatory environment to support and incentivize the construction and operation of purpose-built rental housing. This would include, but not be limited to:

a) Making no changes to the tax treatment of real estate investment trusts (REITs) and concluding the review in this regard;
b) Waiving the GST and the federal portion of the HST on new purpose-built rental housing; and
c) Amending capital cost allowance (CCA) rules to allow for accelerated depreciation rates for new purpose-built rental housing, allowing deferral of a gain from the disposition of a property where a replacement property is acquired, and removing the restriction on CCA for investors whose principal business is not real estate.

Recommendation 3: That the government and CMHC reform the MLI Select program to encourage more affordable housing construction, by:

a) Making a one-time capital injection to CMHC to allow for a reversal of recent increases to the rates and changes to the schedule of tax payments;
b) Amending rules to allow for tax expenses to be paid over the life of the insurance contract; and
c) Adjusting and expanding qualifications for the MLI Select program in order to protect more affordable housing in more communities, and to make building and preserving affordable housing the preferred investment versus building and operating with conventional financing and market rents.

Recommendation 4: That the government create a new federally funded benefit – the Homelessness Prevention and Housing Benefit (HPHB) - in complement to the Canada Housing Benefit (CHB). Such a benefit would slow the growth of new homelessness and accelerate getting those experiencing homelessness into adequate housing.

Introduction

Canadian rental housing providers for affordable housing are Canada's five largest publicly-traded apartment REITs: Canadian Apartment Properties REIT (CAPREIT), Boardwalk REIT, Killam Apartment REIT, InterRent REIT & Minto Apartment REIT. We formed in 2022 to advocate for federal public policy that addresses Canada's housing supply and affordability crisis.

Since our submission in 2022 ahead of Budget 2023, the housing situation in Canada has only worsened. While we can all take pride in our country's population surpassing 40 million people, housing production has not kept pace with this needed growth. Even as CMHC has called for more than doubling the pace of construction through 2030, housing starts are down this year as builders face rising interest rates, rising CMHC insurance rates, labour supply shortages, and continued anti-development political machinations at the local level.

While we are encouraged by the government's recently launched Housing Accelerator Fund and a shift in tone from many leaders towards a politics of housing abundance, there is much more to be done to encourage the housing production necessary to supply every Canadian with adequate housing at a price they can afford, as legislated in the National Housing Strategy Act, 2019.

Canada's publicly-traded apartment REITs are part of the solution.

Today, we own and manage over 120,000 apartments in every province except Manitoba. Last year, we compared our July 2022 rents to CMHC's 2019 local renters' household income data. We found that 53% of our homes met the definition of affordable, which is to say rental rates of less than 30% of income. At the end of Q1 2023, our average rent is $1,394. While CMHC has not provided updated data on renter household income, wage growth over the last four years would suggest that we remain the largest private-sector providers of affordable housing for Canadians.

What follows are our updated recommendations for how the federal government can create a stable and predictable regulatory environment to support and incentivize investment in new rental housing supply, to protect existing affordable rental housing in perpetuity in our most vulnerable communities, and to make housing affordable for our fellow one in ten Canadians in core housing need.

Recommendations

1. Fund affordable housing acquisition

The most affordable housing is the housing that is already built. New construction is necessary to deliver more housing supply, but it can cost two to three times as much as acquiring existing properties. Delivering newly constructed affordable housing is not viable without significant subsidies. Large foreign investors, such as private equity funds, scoop up property portfolios worldwide for a reason: it's a cost-effective way to invest in real estate.

Today, more than half of our suites meet CMHC's definition of affordable housing, and many more are just above the margin. As such, many of our buildings would be good candidates for acquisition by non-profits, cooperatives or land trusts (collectively, non-profits), who could then make these homes affordable in perpetuity. We join a chorus of advocates, including the Canadian Housing and Renewal Association (CHRA), calling on the federal government to develop the necessary supportive financing and funding programs as part of the National Housing Strategy to facilitate the acquisition of existing housing by non-profits.

Further, the federal government should consider waiving, deferring, or reducing the taxation of capital gains for sellers of properties to non-profits to encourage housing providers to vend into such a program rather than selling into a competitive, private market.

2. Supporting and incentivizing purpose-built rental housing

With Canada's housing deficit predicted to stand at 3.5 million homes by 2030 per CMHC, all governments must do what is in their power to create a stable and predictable regulatory environment to support and incentivize new housing of all kinds. Key to this success is a robust purpose-built rental housing sector that allows Canadians to secure suitable housing as their requirements change, for example: when they move to a new city for work, need an extra bedroom for a baby on the way, or wish to downsize in retirement. Without adequate rental housing, the overall housing market cannot function properly. In this regard, we recommend the following:

a) *Maintain the REIT framework to incentivize investment in rental housing*

Members of the committee now benefit from three studies on the tax revenue implications of REITs from EY, KPMG, and the Parliamentary Budget Officer. All have concluded that eliminating the framework would have only marginal implications for revenues, varying from a loss of $19 million to a gain of $53 million per year (which tax relates to *all* REITs, not just residential REITs).

As we face the need for a minimum of $3 trillion of investment by 2030 to build the 5.8 million homes our growing country needs, even $53 million is a distraction at best. What we do know is that changing the REIT tax structure will disrupt the entire real estate market, both residential and commercial, and, critically, will disincentivize investment in rental housing at a time when we need it more than ever.

b) *Waive the GST/HST on new purpose-built rental housing*

Just as putting a price on carbon reduces greenhouse gas emissions, taxes on housing — whether in the form of the HST, development charges or municipal property taxes — disincentivize the construction of much-needed housing supply, both affordable and market-rate.

To incentivize the construction of new housing supply to address the twin crises of supply and affordability, all governments must align their taxation policies with Canada's national housing needs. In this vein, the federal government should remove the GST and the federal portion of the HST from new capital investments in rental housing, as it does for other essentials like non-processed food and children's clothing. This would immediately reduce costs and incentivize building more housing in this difficult fiscal environment for home builders.

c) *Accelerate CCA, defer gains on disposition, and remove the CCA restriction for small investors*

Using a similar tax credit model to that being used to spur green investments, the federal government can incentivize greater investment in new purpose-built rental housing. There is no need to reinvent the wheel. The government can simply reinstate the elevated CCA rates in place before 1972 of 10% on wood-frame buildings and 5% on all others. The increased rate of return for new investments would help overcome competition for capital.

Allowing property owners to defer the recapture of CCA on the disposition of a rental property, conditional on them reinvesting in new buildings of equal or greater value, would create a beneficial cycle, creating more and more of the purpose-built rental housing supply that Canada needs.

Removing the rental property CCA restriction for investors that are not "principal business corporations" would encourage more investment in purpose-built rental housing, in particular by smaller investors.

d) *Maintain the current capital gains inclusion rate of 50%*

Investors, in housing and other businesses, take on risk when allocating their dollars. The federal government rightly takes that risk into account when setting the inclusion rate at 50%, as they have since 2001. This rate has encouraged investment of all kinds in Canada and should be maintained.

3. Reforming MLI Select

Earlier this year, the housing community was shocked by a sudden and dramatic increase in rates and changes to the tax schedule for the successful and productive MLI Select program. We later learned from a statement by CMHC that this was due to the adoption by CMHC of new accounting standards through the International Financial Reporting Standards 17 (IFRS 17) and related changes that came into effect on January 1, 2023. IFRS 17 impacts revenue recognition and increases the capital CMHC must hold. In addition, changes to tax rules now require tax expenses to be payable immediately rather than over the life of the insurance contract. These changes discourage the production and preservation of affordable homes when we need them most.

To counteract this, and encourage new affordable housing, we recommend:

a) that the federal government, as CMHC's lone shareholder, provide a one-time capital injection to counteract the new capital requirements and allow for the return to lower rates; and
b) that tax rules be amended to allow for their expenses to be paid over the life of the insurance contract.

Even before the recent changes, MLI Select suffered from low uptake of the affordable commitments compared to the robust use of the accessibility and climate compatibility provisions of the program. We recommend that the formula be amended by lowering the affordability thresholds (i.e., the percentage of units requiring affordable rents), thereby encouraging greater uptake of the program across a far larger number of properties, and a net increase in the number of affordable homes built under the program umbrella.

Further reductions to rates and fees, and/or decreasing debt service coverage requirements for these loans would help make investing in affordable housing a better return on investment. With the right mix of costs and incentives, the program could make it more advantageous for investors to build affordable housing than using traditional financing and charging market rents.

4. The Homelessness Prevention and Housing Benefit (HPHB)

Last year, we proposed that the government introduce a new emergency support benefit to prevent homelessness. This year, we're adding our voice to the Canadian Alliance to End Homelessness' (the Alliance) proposed HPHB. Such a benefit would slow the growth of new homelessness and accelerate getting people experiencing homelessness into adequate housing. Equally, we continue to urge the government to expand the CHB to help more of our most vulnerable make ends meet. We believe this is essential to the successful realization of the progressive right to adequate housing.

Conclusion

The scale of Canada's housing crisis requires an all-hands-on-deck approach, and the attention of legislators, as our country's greatest present economic challenge. Canada must grow its population to counteract its ageing workforce and realize its full potential. That requires a dramatic shift in our thinking about housing. Canada needs trillions of dollars in new capital to build 5.8 million new homes by 2030. REITs are a powerful tool to harness capital to build, at-scale, middle-class and affordable housing for people from all walks of life. With a stable and supportive regulatory environment, we can incentivize a growing and predictable supply of new housing we need to deliver the homes Canadians require.