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e review
INTELLIGENT ACCOUNTING

Investment Property: Pre & Post 30 June

Anyone with investment property in Australia is probably feeling a little edgy with all the recent media attention on deductions, affordable housing, and negative gearing. I take a look at some of the key tax issues for investors pre and post 30 June.

No more deductions for travelling to and from your investment property

The days of writing-off the costs of travel to and from your residential investment property are about to end. From 1 July 2017, the Government intends to abolish deductions for travel expenses related to inspecting, maintaining, or collecting rent for a residential rental property.

Depreciation changes and how to maximise your deductions now

Investors who purchase residential rental property from Budget night (9 May 2017, 7:30pm) may not be able to claim the same tax deductions as investors who purchased property prior to this date. In the recent Federal Budget, the Government announced its intention to limit the depreciation deductions available.

Investors who directly purchase plant and equipment - such as ovens, air conditioning units, swimming pools, carpets etc., - for their residential investment property after 9 May 2017 will be able to claim depreciation deductions over the effective life of the asset. However, subsequent owners of a property will be unable to claim deductions for plant and equipment purchased by a previous owner of that property. If you are not the original purchaser of the item, you will not be able to use the depreciation rules to your advantage. This is very different to how the rules work now with successive owners being able to claim depreciation deductions.

Investors will still be able to claim capital works deductions including any additional capital works carried out by a previous owner. This is based on the original cost of the construction work rather than what a subsequent owner paid to purchase the property.

There are very limited details about how this Budget announcement will work – as always, the devil will be in the detail once draft legislation is released.

Business as usual for pre 9 May investment property owners

If you bought an investment property recently, are about to renovate, or have not had a depreciation schedule completed previously, you should consider having one completed.

As a property gets older the building and items within it wear out. Property owners of income producing buildings are able to claim a deduction for this wear and tear. Depreciation schedules are completed by quantity surveyors and itemise the depreciation deductions you can claim.

Higher immediate deductions for co-owners

It's not uncommon to have multiple owners of an investment property. Co-ownership can, in some circumstances, quicken the rate depreciation deductions can be claimed for the same asset. This is because depreciation is claimed on each owner's interest. If an owner's interest in an asset is less than $300, they can claim an immediate deduction. In a situation where there are two owners split 50:50, both owners could potentially claim the immediate deduction, bringing the total immediate deduction available up to $600 for a single asset.

The same method can be used when applying low-value pooling. Where an owner's interest in an asset is less than $1,000, these items will qualify to be placed in a low-value pool. This means they can be claimed at an increased rate of 18.75% in the first year regardless of the number of days owned and 37.5% from the second year onwards.

In a situation where ownership is split 50:50, by calculating an owner's interest in each asset first, the owners will qualify to pool assets which cost less than $2,000 in total to the low-value pool.

The value of renovations

It's best to get a depreciation schedule completed before you start renovations so the scrap value of any items you remove can be recognised and written-off as a 100% tax deduction in the year of removal. This is available for both plant and equipment depreciation and capital works deductions. When new work is completed as part of the renovations (i.e., a new roof, walls, or ceiling), this can also be depreciated going forward.

In some circumstances, there may be depreciation deductions available for renovations completed by a previous owner.

"Anyone who owns a rental property, or is thinking about buying a rental property, will be worse off under these proposed changes. For the more than 900,000 taxpayers who claim travel expenses, particularly those with holiday-style properties, the loss of this deduction may well be a game-changer for the viability of their investment. And for those planning on buying, understanding how these changes may impact your tax outcome and cashflow will be vital to making a wise investment decision and avoided overcommitting yourself on your property investment."

JULIAN NICHOLS

Deductions for older properties

Investors in older properties may still be able to claim depreciation costs. This is because a lot of the items in the house will not be the same age as the house or apartment. Hot water systems, ovens, carpets, curtains etc., have probably all been replaced over time. Additional works, extensions or internal refurbishments may also be deductible.

Further restrictions on foreign property investors

We have seen a number of measures over the years restricting access to tax concessions for foreign investors, particularly for residential property investments. The recent Federal Budget goes one step further, restricting access to tax concessions, increasing taxes, and penalising investors who leave property vacant. Measures include:

- **Charge for leaving properties vacant** - Foreign owners of residential Australian property will incur a charge if their property is not occupied or genuinely available on the rental market for at least 6 months each year. The charge, which is expected to be at least $5,000, does not appear to apply to existing investments but those made on or after Budget night, 7:30pm on 9 May 2017.
- **Excluded from main residence exemption** - Foreign and temporary residents will be excluded from the main residence exemption. The main residence exemption excludes private homes from capital gains tax (CGT). Existing properties held prior to 9 May will be grandfathered until 30 June 2019. However, it remains to be seen whether partial relief will be available to those who have been residents of Australia for part of the period they owned the property and whether this change will apply to Australian residents who were classified as a foreign resident for part of the ownership period.
- **Increase in CGT withholding tax** - When someone buys Australian real property (i.e., land and buildings) they are currently required to remit 10% of the purchase price directly to the ATO as part of the settlement process unless the vendor provides a certificate from the ATO indicating that they are an Australian resident. These rules do not currently apply if the property is worth less than $2 million. From 1 July 2017, the CGT withholding rate under these rules will increase by 2.5% to 12.5%. Also, the CGT withholding threshold for foreign tax residents will reduce from $2 million to $750,000, capturing a much wider pool of taxpayers and property transactions.
- **Rules tighten for property purchased through companies or trusts** - Australian property held through companies or trusts by non-residents or temporary residents is also being targeted by expanding the principal assets test to include associates. The move is to prevent foreign residents avoiding Australian CGT liability by splitting indirect interests in Australian real property.
- **Level of foreign investment in developments capped** - a 50% cap is being placed on foreign ownership in new developments.

The push for affordable housing

The Government is very keen to ensure that investment is directed into 'affordable housing.'

The 2017-18 Budget announced an increase in the CGT discount for individuals who choose to invest in affordable housing. The current 50% discount will increase by 10% to 60% for Australian resident individuals who elect to invest in qualifying affordable housing.

In addition, the Government is creating investment opportunities for Managed Investment Trusts (MIT) to set up to acquire, construct or redevelop property to hold as affordable housing. In order for investors to receive concessional taxation treatment through an MIT, the affordable housing must be available for rent for at least 10 years. For foreign investors, MITs are one area where the Government is actively encouraging participation rather than restricting it.