THE AUSTRALIAN

Shifting tax rules make life tougher for property investors

JAMES GERRARD THE AUSTRALIAN 12:00AM April 3, 2018

Shifting tax rules for investment property have made it tougher for those wanting to build wealth in this asset class. In particular, there has been one key change that has largely flown under the radar and may hit property investors hard as it approaches its first full year since implementation.

On the financing side, lending restrictions imposed by the regulator APRA on interest-only loans have pushed interest rates for investors up by almost 1 per cent and made it harder to get investment loans.

Meanwhile, on the taxation side, there has been a clamp down on travel-related expenses for residential property.

Though the travel clampdown has been widely publicised with stories of property owners flying to holiday destinations to inspect properties, the much more important issue of depreciation changes have gathered less attention. For property investors who exchanged contracts on second hand property after 7:30pm on May 9, 2017, they generally will not be able to claim depreciation for plant and equipment assets unless they purchased those assets directly and incurred the cost including installation. In other words, if you purchase an established property, even if it is only a few months old, unless you bought it brand new from the developer, you will not be able to claim any tax deduction on plant and equipment.

If you owned investment property before May 9, 2017, don't worry, your tax deductibility on plant and equipment has been grandfathered and you will be able to claim depreciation as normal in your tax return.

The quantum of this change for new property investors is significant.

Bradley Beer, CEO of BMT Tax Depreciation, a specialist tax depreciation firm says: "The government has hit property investors with a sledgehammer. The average plant and equipment depreciation deductions for a brand new two bedroom $500,000 property would be around $33,401 over the life of the property with average first full year depreciation on plant and equipment running at approximately $5785."

Many people are unaware of the new rules which may catch out property bargain hunters, among others.

Shamren Odisho of
i-property solutions, a Sydney based buyers agency, says: “We have a preference to purchase investment properties that are a few years old. The buildings are generally settled in terms of faults and issues resulting from construction and there is not the same pricing premium as with a brand new property”.

Although different plant and equipment items have varying number of years they can be depreciated, generally the tax benefits are the greatest in the first seven years.

Odisho says: “We have been educating clients on the reduced tax benefits of buying an established property as it can impact their post tax cash flow potentially by thousands of dollars per year.” In terms of what can be claimed if eligible, the top five items are air conditioners, carpets, hot water systems, stoves and blinds.

If you are an investment property owner, keep in mind there are still depreciation deductions available for established property.

Beer at BMT says: “The capital works allowance, which is the component investors can deduct for the building structure, remains unchanged. These deductions typically make up 85 to 90 per cent of the total depreciation claim and include walls, the roof, doors, kitchen cupboards and more. These deductions can be claimed at a rate of 2.5 per cent per year for a maximum of 40 years for any property in which construction commenced after September 15, 1987.”

Separately, there are other less obvious paths by which other depreciation tax deductions can be secured.

Beer says: “If you renovate an existing property and buy brand new plant and equipment, these items are tax deductible under a depreciation schedule. Similarly, if you purchase an established property which is considered to be substantially renovated by the previous owner for selling purposes, then an investor can claim depreciation on the new plant and equipment assets along with any new or old qualifying capital works deductions available.”

If you purchase an investment property constructed after September 15, 1987, you should ask for a copy of the previous owner's depreciation schedule — remember current and future property owners can claim annual depreciation deductions on the original building structure and any qualifying additional capital works additions for the remainder of the 40-year period.

If you don't have a quantity surveyor report, best to speak with your accountant about whether the exercise would be worthwhile.

Beer says: "Interestingly, about 50 per cent of our residential depreciation schedules are for second-hand properties and we don't see this changing as there is still a lot that can be claimed when getting the right advice."

Accountant Tim Ricardo agrees and says: "Getting good advice can alter the tax outcome by thousands of dollars per year when maximising the use of existing rules. For instance, when doing a renovation on an investment property where deprecation has been claimed on plant and equipment, owners should be aware of so-called 'scrapping provisions' where they may be able to claim a tax deduction on the balance of unused depreciation when getting rid of old items."

Ultimately, the message investors need to be aware of is that the rules are now more complex when thinking about depreciation benefits and it will usually be money well spent getting advice from an accountant and quantity surveyor on what you can claim.

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