



## STEP 4 – PROPERTY TAXATION

Finance & Property  
Research Pty Ltd  
www.property-buyers-research.com

Property Investment Returns can be greatly influenced by the impact of taxation. This section addresses Income Tax, Depreciation, Capital Gains Tax or (CGT), Goods and Services Tax (GST) and Land Tax.

### 1. INCOME TAX

Deductible expenses depend on the purpose of the investment and the nature of the expenditure.

<b>Deductible Expense</b>	
Advertising	Interest
Bank Bill Line Fee	Land Tax
Bank Fees & Charges (Non Loan)	Legal Costs (See (2) below)
Borrowing Expenses (See (1) below)	Loan Discharge Costs
Building Write-Off	Management Fees & Commission
Cleaning	Mortgage Insurance
Depreciation	Plant & Equipment less than \$300
Electricity & Gas	Property Journals
Environmental Impact Studies	Rates & Taxes
Environmental Protection Expenditure	Repairs
Gardening Costs	Strata Levies
Head Rental	Telephone
Insurance Premiums	Travel

#### (1) Borrowing Expenses (Amortised)

Bank Charges  
Establishment Fees  
Fees for Guarantee  
GST on above  
Legal Fees (portion)  
Loan Procurement Fees  
Loan Stamp Duty  
Mortgage Insurance  
Registration Fees  
Search Fees  
Survey Fees  
Valuation Fees

#### (2) Legal Fees

Some portions of the legal fees can either be expensed or amortised

#### (3) Non Deductible Items (Capital Cost)

Advertising for Sale  
Agents Commission on Sale  
Alterations & Extensions  
Capital Expenditure  
Legals on Purchase and Sale (relating to capital items)  
Repairs immediately after purchase  
Stamp Duty

(The above however are deductible for CGT purposes)

Interest Deductions

Interest on loans held to purchase non income producing property is not tax deductible.

For example, non income producing vacant land, holiday houses not available for letting, fall into the same category as wine, stamps, jewellery etc., although primarily held for investment purposes, is not deductible.

However the interest does form part of the cost base for capital gains tax purposes.

Tax Losses

Incurred after the 1988/89 financial year can be carried forward in perpetuity, with losses before this date carried forward for only 7 years.

Apportionment

If there is owner occupation of say a holiday unit, the ATO may rule an apportionment on a time basis, if the owner does not pay a commercial rental.

**MARGINAL RATES (EXCLUDING MEDICARE LEVY)**

	<u>Taxable Income</u>	<u>Tax Rate 2009-2010</u>
<b>Individuals -</b> Partners  (Partnership income is split before Distribution and payment @ the Individuals rate)	0-\$6,000 \$6,001-\$35,000  \$35,001-\$80,000  \$80,001-\$180,000  \$180,001 and over	Nil 15c for each \$1 over \$6,000 \$4,350 + 30c for each \$1 over \$35,000 \$17,850 + 38c for each \$1 over \$80,000 \$55,850 + 45c for each \$1 over \$180,000
<b>Company</b>	Total Taxable Income	30%
<b>Shareholder</b> Dividends paid by a company are said to be fully franked (or partly franked) if they are paid from company income fully or partly taxed at company rates. A Shareholder who receives a franked dividend can claim a rebate. This amounts to the tax previously paid by the company. Obviously unfranked dividends do not entitle the shareholder to any rebate.		Shareholders Marginal Rate
<b>Trusts</b> The beneficiary or unit holder pays tax if it is distributed. The trustee pays tax on any income that is not distributed. (Taxable losses cannot be distributed).		Beneficiary or Unit holders Marginal Rate
<b>Superannuation Funds</b>		15%

**Depreciation – General**

Claims for depreciation can have a big impact on returns from property and is frequently overlooked.

This is very often because of the lack of information provided at acquisition time.

We strongly recommend that with all income producing property, a Quantity Surveyor be engaged following purchase. They can confirm that their fee will be more than recovered in tax benefits in the first year. Approximate estimates can be given over the phone.



Details and contact can be made online at [www.capitalclaims.com.au](http://www.capitalclaims.com.au) or phone 1300 922 220.

#### **Depreciation – Partnerships & Trusts**

Partnership & Trust beneficiaries can claim depreciation allowances as a tax deduction, proportional to their income entitlement %. The distribution of unassessed income (apart from building depreciation allowance) can increase the capital gains tax of a trust beneficiary or unit holder.

#### **Depreciation – Companies**

If the depreciation allowance claimed by companies are passed on to increase the shareholders dividend, then that portion of the dividend will be unfranked. Therefore it will be taxed when received by the shareholder.

Such dividends are not as tax effective for company shareholders as they would be with other structures/holding vehicles.

#### **Depreciation – Plant & Equipment – claimed under division 40**

There are two methods of calculating depreciation;

1. Diminishing Value (reducing value) method; or
2. Prime Cost (straight line) method.

Once a method is chosen it cannot be changed.

If the maximum amount of depreciation claimed is required in the earlier period, then the Diminishing Balance method is appropriate.

For assets acquired after 11.45a.m. on 21<sup>st</sup> September 1999, the prime cost percentage is 100 divided by effective life and the diminishing value percentage is 150 divided by effective life.

This does not apply to small business taxpayers.

#### **Depreciation – Building – claimed under division 43**

All on a Compulsory Prime Cost basis i.e. constant yearly amount.

### **Building Depreciation Rates**

Type of income producing building	Construction commenced	Rate of allowance % p.a.
Hotel or other traveler accommodation	20/8/79 – 21/8/84	2.5
	22/8/84 – 15/9/87	4.0
	16/9/87 – 26/2/92	2.5
	After 26/2/92	4.0
Commercial/Industrial	18/7/82 – 21/8/84	2.5
	22/8/84 – 15/9/87	4.0
	16/9/87 – 26/2/92	2.5
Commercial	After 26/2/92	2.5
Industrial	After 26/2/92	4.0
Residential	19/7/85 – 15/9/87	4.0
	After 15/9/87	2.5
Associated infrastructure (Site services etc.)	After 26/2/92	2.5



Items deemed “Capital Expenditure” are depreciated not expensed.

Therefore when buying existing property, the following can be included in your depreciation claim.

Capital Expenditure includes -

- Architects Fees
- Engineers Fees
- Holding Charges
- Excavation & Foundation Works

Property acquisition and land clearing are not Capital Expenses.


Completed Building - Builders profit must be deducted (I.T. 2640)

**New Versus Old Houses**

The present value of future taxation benefits can be quite dramatic with new houses versus old.

We can calculate the net lump sum or alternatively the weekly benefit after referring to the following two tables provided by Quantity Surveyors and depreciation specialists, Capital Claims – [www.capitalclaims.com.au](http://www.capitalclaims.com.au)

**Rental Property Depreciation Estimate**



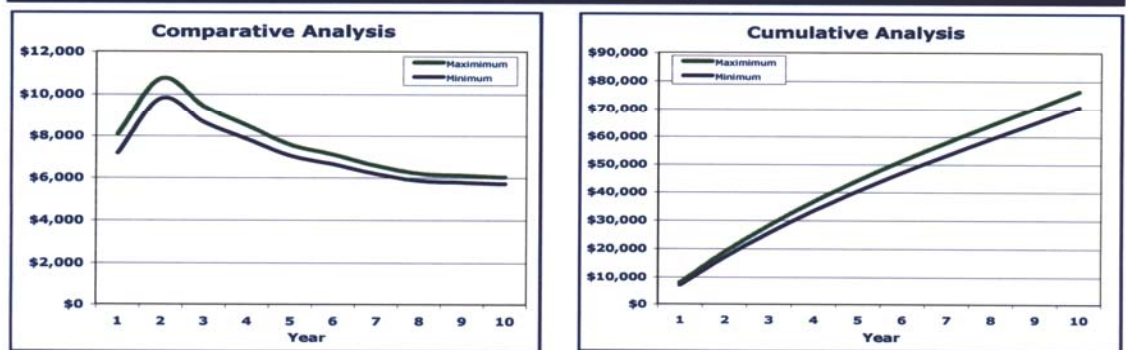
**Capital Claims**  
-Property Depreciation Specialists-

**Typical 4 Bedroom  
Brick Vener Property  
Brand New**

**This Estimate Cannot Be Applied For Taxation Purposes**

Estimated Depreciation Range For The First 10 Years of Ownership						
Year	Division 40		Division 43		Total (Divisions 40 & 43)	
	Min	Max	Min	Max	Min	Max
1	5,563	6,401	1,618	1,684	7,181	8,085
2	4,847	5,577	4,963	5,166	9,810	10,743
3	3,691	4,247	4,963	5,166	8,654	9,413
4	2,890	3,324	4,963	5,166	7,853	8,490
5	2,098	2,414	4,963	5,166	7,061	7,580
6	1,693	1,947	4,963	5,166	6,656	7,113
7	1,229	1,413	4,963	5,166	6,192	6,579
8	912	1,050	4,963	5,166	5,875	6,216
9	834	960	4,963	5,166	5,797	6,126
10	765	881	4,963	5,166	5,728	6,047
11 +	1,902	2,188	4,529	4,714	6,431	6,902
<b>Total</b>	<b>\$26,424</b>	<b>\$30,402</b>	<b>\$50,817</b>	<b>\$52,892</b>	<b>\$77,241</b>	<b>\$83,294</b>

**Graphical Representation Of Estimated Depreciation Claims Available**




The estimations applied within this report have utilised the Diminishing Value method combined with Low Cost and Low Value Pooling for Division 40 assets. Division 43 has been estimated utilising the Prime Cost Method. The figures within this report are for estimation purposes only and should not be applied for taxation purposes. No Pro Rata adjustments have been applied.

To Discuss the contents of this report please contact Mark Wilkins at Capital Claims  
on (02) 4920 6500 or [markw@capitalclaims.com.au](mailto:markw@capitalclaims.com.au)



## Rental Property Depreciation Estimate



**Capital Claims**  
-Property Depreciation Specialists-

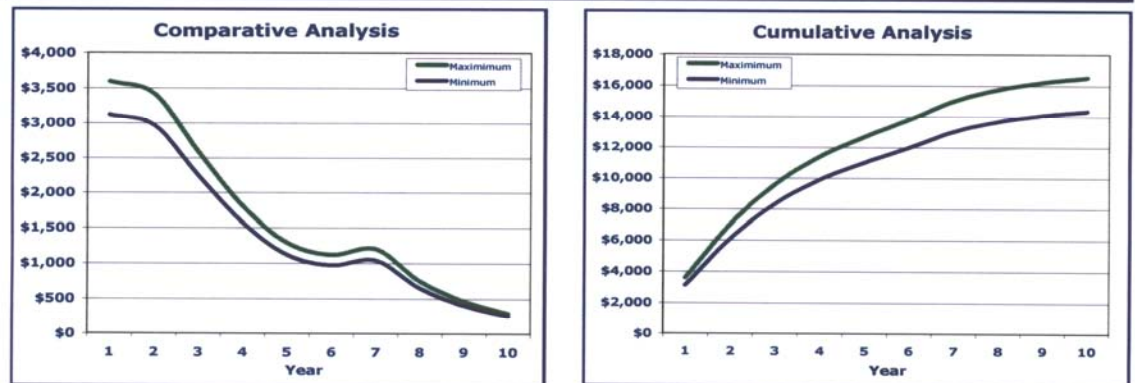
**Typical 4 Bedroom  
Weatherboard Property  
30 Years Old**

**This Estimate Cannot Be Applied For Taxation Purposes**

### Estimated Depreciation Range For The First 10 Years of Ownership

Year	Division 40		Division 43		Total (Divisions 40 & 43)	
	Min	Max	Min	Max	Min	Max
1	3,124	3,594	0	0	3,124	3,594
2	2,969	3,415	0	0	2,969	3,415
3	2,247	2,585	0	0	2,247	2,585
4	1,573	1,809	0	0	1,573	1,809
5	1,121	1,289	0	0	1,121	1,289
6	976	1,122	0	0	976	1,122
7	1,044	1,202	0	0	1,044	1,202
8	652	750	0	0	652	750
9	407	469	0	0	407	469
10	255	293	0	0	255	293
11 +	425	489	4,529	4,714	4,954	5,203
<b>Total</b>	<b>\$14,793</b>	<b>\$17,017</b>	<b>\$4,529</b>	<b>\$4,714</b>	<b>\$19,322</b>	<b>\$21,731</b>

### Graphical Representation Of Estimated Depreciation Claims Available



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## 2. CAPITAL GAINS TAX (CGT)

This is payable on all property purchased and subsequently sold with both transactions occurring after 19<sup>th</sup> September 1985.

To arrive at the taxable gains, certain deductions are allowable. These are treated as the cost base.



**Cost Base****(a) Purchase Costs**

<b>Expenditure</b>
Advertising costs to find a seller
Agents Fees
Cost of land/building
GST
Initial repairs
Land Tax
Legal Fees
Registration of transfer
Stamp Duty on transfer
Surveyors Report
Tax Advice
Valuation Fees

**(b) Sale Costs**

Advertising costs to find a buyer
Auctioneer's fee
Lease break costs
Legal
Rates adjustments
Surveyor's report
Tax Advice
Transfer costs
Valuation costs re apportionment – for purposes of ITAA (eg Sec.160ZH(12)-(14))

**(c) Trading Costs**

Capital improvements
Costs in fighting compulsory acquisition (even if unsuccessful)
Demolition Costs
Extensions (incl. Architects costs)
Insurance Premiums (Buildings)
Interest
Lease Variations
Legal costs defending a demolition order
Legal costs incurred in establishing title to an inherited asset
Pest Inspections
Rates & Land Taxes
Regular capital refurbishment
Repairs & Maintenance
Subdivision Costs

**Paper Profit attracts CGT**

Even if no cash payment is received for the property e.g. the purchase price or part thereof is carried on 1<sup>st</sup> Mortgage by the developer, CGT is payable on the full agreed purchase price. Despite the fact that there is no realised cash profit with which to pay the tax.

**Capital Losses**

If the cost base exceeds the purchase price, this produces a capital loss.



Capital losses can be offset against realised capital gains but not against normal income. Unused capital losses can be carried forward indefinitely, but can be trapped inside the vehicle in which they were created e.g. a company.

#### *Principal Place of Residence*

The general exemption under section 160ZZQ is extended under certain circumstances including **temporary absence** and choosing between **two residences** owned by a family.

The principal place of residence can be rented out whilst maintaining principal residence status.

**Subdividing** the family home does not constitute a disposal for CGT. Even building on the second block does not attract capital gains tax, until sold.

Pre capital gains status (i.e. before 19/9/85) is retained on subdivision, however the capital improvement component added after that date is subject to indexed threshold adjustments.

(See Taxation Determination TD7).

### **New CGT Provisions v Previous Legislation**

On or after 1/10/99 CGT was reduced by 50% for individuals and 1/3<sup>rd</sup> for Trusts with cessation of indexation post 30/9/99.

On the surface this sounds good. However the political rhetoric by the Coalition Government that tax was “halved” is not borne out by calculation. The new basis actually provides worse results for investors than the old. This is even worse for companies who received no rate reduction.

Now that indexation using CPI has been excluded from the tax cost base, investors will be paying tax on inflation. In other words they will pay tax even where there has been no capital gain in “real” terms.

## **3. LAND TAX (State Government)**

### **NEW SOUTH WALES**

#### **Exemptions**

##### **Principal place of residence**

Your principal place of residence is generally exempt from land tax. You can usually only claim an exemption for a principal place of residence on one property.

If you use your land as your principal place of residence and for non-residential purposes, for example, if you run a business on your land, you may be eligible for a reduction in land tax for the proportion used as your residence.

If a company is an owner or part owner, they are not entitled to an exemption for a principal place of residence.

Land intended as the owners' principal place of residence, provided you do not own another property which is currently your exempt principal place of residence. You may be eligible for an exemption if you:

- (a) have purchased unoccupied land where you intend to build your principal place of residence (your home), or
- (b) are renovating an existing home that you intend to occupy as your principal place of residence.



### Concession for sale of former residence

If you have recently purchased a house that you have moved into, or intend to move into, but are still trying to sell your former home you may be able to claim an exemption for both properties. To qualify for this concession, strict time frames apply. If the properties are rented, this concession will not apply.

Other exemptions include:

- land that is zoned rural or non-urban and used for primary production is exempt from land tax. For all other land the dominant use must be primary production to qualify for the exemption.
- land used and occupied primarily for boarding houses anywhere in .NSW, or certain property used for low cost accommodation within a five kilometre radius of the Sydney GPO.
- retirement villages, aged care establishments and nursing homes.
- religious and charitable institutions.

Read more about qualifying for a land tax exemption or concession at [www.osr.nsw.gov.au](http://www.osr.nsw.gov.au)

## 4. GST – (Federal)

### Rural

GST is not payable on farm land.

### Commercial

In determining whether GST is payable on commercial/industrial property first establish if the Vendor is registered for GST. If so, then GST is payable on the sale. If not, GST cannot be charged. GST is not payable on “going concerns”.

To prevent putting a cash flow burden on the purchaser (via input tax credit delay), the Margin Scheme can be used. This is described later in this section.

### Residential

No GST is payable on family home sales.

New developments for sale attract GST whether undertaken by a developer, or an individual who is not registered for GST. The latter needs to become registered for GST. GST is not payable between the joint venture parties.

Even if the buyer is registered for GST, they cannot claim it back. A.C.C.C. rules state that the GST must be included in the advertised price.

### Leased Property

#### *Residential*

GST is not payable on residential rental payments, (either by lessee or lessor).

#### *Commercial*

The date GST applies to commercial leases depends on the date when a legally binding agreement or the lease is entered into and the tax status of the tenant.

### Development Property

With the exception of variations provided by the Margin Scheme (set out below) GST is payable on all GST taxable inputs.



Therefore in our spreadsheet model relating to developments we show either the margin scheme or full taxation.

### **Margin Scheme**

The margin scheme, in relation to property transactions, allows for a reduced amount of GST to be paid. It applies to the supply of freehold interests in land, strata units and long-term leases, including those held on or before 1 July 2000.

If you are registered, or required to be registered for GST and you make a supply of a freehold interest strata unit or a long-term lease, the supply is subject to GST. GST may be calculated on the full value of the supply or on the margin.

Developers who are selling to purchasers not registered for GST can use the Margin Scheme to reduce the GST payable, by having it payable only on their margin.

The requirements to utilize the margin scheme can be extremely complex. Before utilising the provisions of the margin scheme in a feasibility study, you will need to seek professional accounting advice.

Our software model can incorporate results with and without the margin scheme provisions.

