KENNAS

ARE YOU THINKING OF INVESTING IN THE

PROPERTY MARKET?

- Chartered Accountants
- Business & Tax Consultants
- Financial Planners

A history of shaping financial success

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Backed by 125 years of shaping financial success for our clients, Kennas can help you achieve success in your choice of investment. We do this by constantly looking for ways to help your financial situation, using a range of unique tools and techniques.

One way we help you to succeed is by providing you with the right knowledge to take control of your own financial success. This booklet provides valuable information specific to your consideration of the purchase of an investment property. We hope it assists to build your knowledge and make the best decisions about your investment.

1. CUTTING THROUGH THE MARKET LINGO

If you've already started doing some research on property investing, and you may have even started talking to agents in the field, you're no doubt hearing all sorts of differing opinions. Which areas are better to invest in, regional vs major cities, or developing towns? Where are the growth areas?

You will have seen property developers making promises on returns and guaranteed tax refunds.

Remember that just like most products, property is a huge market and the advertisers would like to convince you that their product is the best and worth buying.

Whether it's the local newspaper talking up housing prices or the property developer of a flash new Gold Coast housing estate, they also prey on the fact that buying property can sometimes have an emotional element. However, the best option end depends on the investor's risk profile and individual circumstances. For example, some may decide to use rental properties as a continued forced way of savings, so a better strategy may be to borrow to purchase shares.

Either way, before signing on the dotted line, it's a worthwhile investment to come in and have a chat to your accountant. We'll give you an unbiased review of the property and determine if this property fits with your personal risk profile along with expected income return and capital growth.

Other areas of consideration we can help you with are determining whether residential or commercial investment property suits your needs better, as well as which entity is best to purchase with. This may even include your own superannuation fund.

2. KEEPING AHEAD OF THE TAXMAN

Owning a rental property means additional reporting requirements for your income tax. A few tips for you to keep in mind when compiling your rental property tax records include:

- if you are renting through a real estate agent, keep all monthly statements as well as the end of year financial statement summary. This will outline total rent collected and expenses deducted.
- if you have borrowed funds to purchase the property, keep your loan statements for the financial year to calculate the total interest charged and loan fees to claim. The costs to set up the loan are also deductible over a five-year period.

See our top ten tips for landlord tax deductions over the page. We also recommend visiting the Australian Taxation Office website for detailed information on rental properties and tax deductions.

You are entitled to a deduction of depreciation on the fixtures and fittings, and in some cases, the entire building cost of the building (capital works deduction). This is a great way to boost your return on investment by reducing the amount of tax you pay.

However, the tricky bit is determining the value of these items to depreciate as well as the effective life. This is where a quantity surveyor can come in handy. Incidentally, the fee you pay the quantity surveyor to produce their report is also a deduction.

To find out more, or to request a quote, visit the BMT tax depreciation Quantity Surveyors website.

3. UNDERSTANDING INVESTMENTS CASH FLOW AND RETURN

Choosing property as an investment vehicle is a big decision and usually a long-term commitment. It's important to get an idea of your investment's rate of return and cashflow. This can be hard to gauge in this type of investment because of the number of different expenses and outlays associated with owning a rental property - as well as the volatility of the rental market.

Kennas have developed a tool to assist you with analysing your expected rate of return and expected cash flow over a period of time. This tool incorporates the yearly running and borrowing costs as well as the expected capital growth. It gives you the ability to plan when you are expected to repay the borrowings in full.

The normal fee for reviewing your proposed purchase is $495.00 including GST, and this will assist you in understanding the key drivers of your property investment return.

4. NEGATIVE GEARING

You are probably already familiar with this term and it may have been one of the reasons you are considering a rental property as an investment. But what does negative gearing mean?

Basically, when you finance the purchase of a property, along with other ownership and maintenance costs, when deducted against the rental income received, results in a loss. This can be offset as a deduction against your other taxable income.

This savings in tax can help contribute to the return of investment of the property, however it will also mean that you will need a cashflow source other than received from a tenant to cover the costs. Also, when you are paying principal and interest on your loan repayments, the negative gearing scenario will only have a limited time frame (as you are paying a higher proportion of interest at the beginning of the loan).

Therefore, it's important to have capital growth as a goal, to make this investment worthwhile in the long run.

5. POSITIVE GEARING

Just like the term suggests, positive gearing is different to negative gearing in that your rental yields are higher than your deductible expense, which means that your investment is paying for itself right now and won't need to find additional cashflow to fund it, however, you will need to keep in mind that you will be required to pay income tax at your marginal rates on this net profit at the end of the tax year for which you should budget.

Kennas offers a comprehensive tax estimate service which can greatly assist in planning and budgeting for this cost in a timely manner. We can also offer advice prior to year-end on how to minimise tax liability as much as possible.

6. CAPITAL GROWTH

So what happens when you decide to realise your investment and sell? When the time comes, hopefully you've experienced a healthy increase in the property market and are able to sell to capitalise on this. It will mean you are faced with a capital gain on your property.

A capital gain is a result of the sale price and associated selling costs of the property being higher than the purchase price and associated purchase costs. This profit (if you own the property for more than 12 months, then half the profit) is included in your taxable income in the year the contract was signed for sale.

You will pay tax on this amount at your normal marginal rate, in the proportion that you own the property. There may be opportunities at the time to reduce the amount of tax you pay on this gain and we would suggest you engage us to provide specific advice to your circumstances at the time.

DID YOU KNOW...

Tax Deductions Rental Properties

TOP 10 TIPS TO HELP RENTAL PROPERTY OWNERS

1. KEEP THE RIGHT RECORDS

You must have evidence of your income and expenses so you can claim everything you are entitled to. Capital gains tax may apply when you sell your rental property, so you need to ensure you keep records over the period you own the property and for five years from the date you sell the property.

2. ENSURE YOUR PROPERTY IS GENUINELY AVAILABLE FOR RENT

Your property must be genuinely available for rent to be able to claim a tax deduction. This means that you must be able to show clear intention to rent the property. So advertise the property so that someone is likely to rent it and set the rent in line with similar properties in the area.

3. GET INITIAL REPAIRS AND CAPITAL IMPROVEMENTS RIGHT

You can't claim initial repairs or improvements as an immediate deduction in the same income year you incurred the expense.

- Repairs must relate directly to wear and tear or other damage that happened as a result of you renting out the property. Initial repairs for damage that existed when the property was purchased, such as replacing broken light fittings and repairing damaged floor boards are not immediately deductible. These costs are instead used to work out your cost base when you sell the property.
- Ongoing repairs that related directly to wear and tear or other damage that happened as a result of you renting out the property such as repairing the hot water system or part of a damaged roof are classed as a repair and can be claimed in full in the same income year that you incurred the expense.
- Replacing an entire structure, like a roof, when only part of it is damaged, or renovating a bathroom, is classified as an improvement and not immediately deductible. These are building costs that you can claim at 2.5% each year for 40 years from the date of completion.
- If you completely replace a damaged item that is detachable from the house, and it costs more than $300.00, the cost must be depreciated over a number of years.

4. CLAIMING BORROWING EXPENSES

If your borrowing expenses are over $100.00, the deduction is spread over five years. If they are $100.00 or less you can claim the full amount in the same income year that the expense was incurred. Borrowing expenses include such things as loan establishment fees, title search fees and costs of preparing and filing mortgage documents.

5. CLAIMING PURCHASE COSTS

You can't claim any deductions for the cost of buying your property. These costs include things such as conveyancing fees and stamp duty (for properties outside the ACT). If you sell your property these costs are then used when working out whether you need to pay capital gains tax.

6. CLAIMING INTEREST ON YOUR LOAN

You can claim interest as a deduction if you take out a loan for your rental property. If you use some of the loan money for personal use, such as going on a holiday, you can't claim the interest on that part of the loan. You can only claim the part of the interest that relates to the rental property.

7. GET CONSTRUCTION COSTS RIGHT

You can claim certain building costs, including extensions, alterations and structural improvements as a capital works deduction. As a general rule you can claim a capital works deduction at 2.5% of the construction cost for 40 years from the date the construction was completed. If the previous owner claimed a capital works deduction they are required to give you the information they used to calculate the costs, so it always pays to ask them for this. If they didn't use the property to produce assessable income you can obtain an estimate from a qualified professional and ensure they use a reasonable basis for their valuation and exclude the cost of the land when working out the construction costs.

8. CLAIMING THE RIGHT PORTION OF YOUR EXPENSES

If your rental property is rented out to family or friends below market rate, you can only claim a deduction for that period up to the amount of rent you received. You can't claim deductions when your family or friends stay free of charge or for periods of personal use.

9. CO-OWNING A PROPERTY

If you co-own a rental property you must declare rental income and claim expenses according to your legal ownership of the property. As joint tenants your legal interest will be an equal split, and as tenants in common you may have different ownership interests.

10. GET YOUR CAPITAL GAINS RIGHT WHEN SELLING

Wen you sell your rental property you will make either a capital gain or capital loss. This is the difference between what it cost you to buy and improve the property, and what you receive when you sell it. If you make a capital gain you will need to include the gain in your tax return for that financial year. If you make a capital loss, you can carry that loss forward and deduct it from capital gains in future years

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Rental Property Schedule

(to complete and return to Kevnes at tax time)

Client:

Year:

Address of property:

Was the property rented or available for rent for the full year? Yes / No

If No, please advise the number of weeks used privately -

For all deductions you wish to claim, you MUST have receipts and other supporting documentation to support your claim. These records must be kept for at least 5 years after you lodge your income tax return.

Income	**$**
Rental Income	
Other rental related income (including bonds)	
Gross Rent	
Expenses	
Advertising for tenants	
Body corporate fees and charges	
Borrowing expenses	
Cleaning	
Council rates	
Gardening and lawn mowing	
Insurance	
Interest on loans	
Land tax	
Legal fees	
Motor vehicle expenses	
Pest control	
Property agent fees and commission	
Repairs and maintenance	
Stationery, telephone and postage	
Water charges	
Sundry rental expenses	
Total Expenses	
NET RENT	

Depreciable Assets Purchased & Sold (e.g. furniture, fittings, improvements)