RENTAL PROPERTIES
Information & Guidance

SMN accountants

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If you are considering purchasing a rental property or using your existing home, it is important to consider and get advice on the potential tax implications.

When you own a rental property, you need to:

- keep records right from the start, so you can meet your tax obligations
- work out how to divide income and expenses (if you co-own the property)
- pay installments towards your end-of-year tax liability if necessary.

At SMN Accountants we can inform you of your options and help provide you with the necessary tools to enable you in managing a rental property.

KEY TIPS

1. Keep records
2. Claim correct expenses
3. Apportion expenses accordingly

[01] INCOME

All rent and rent-related income you receive must be included in your tax return – whether paid to you or your agent.

1.1. Assessable Income

- The income received is taxable to the owners of the property in the same proportion as the ownership interest as shown on the title.

- The rent received must be at normal market rates to be able to claim all the expenses in full. If you rent at below market rent (to family or friends perhaps), you can only claim deductions up to the amount of rent charged.

- The rent must be declared in the year it is received.

1.2. Co-Ownership of rental property

The way that rental income and expenses are divided between co-owners varies depending on whether the co-owners are joint tenants, tenants in common or there is a partnership carrying on a business of letting rental properties.

Co-owners who are not carrying on a business of letting rental properties must divide the income and expenses for the rental property in line with their legal interest in the property. If they own the property as:

- joint tenants, they each hold an equal interest in the property

- tenants in common, they may hold unequal interests in the property, for example, one may hold a 20% interest and the other an 80% interest.

[02] EXPENSES

You can claim a deduction for your rental property related expenses for the period your property is rented or is genuinely available for rent.

2.1. Types of deductible expenses

2.1.1. Repairs

- Repairs made to the property during the period it is leased are deductible but generally not repairs carried out within the initial 12 months of owning the property (these can be used to reduce a capital gain on disposal).

- Improvements you make to the property are not deductible in full. They need to be depreciated and claimed over their effective life (see depreciation).

2.1.2. Depreciation

When you purchase a rental property, you are generally treated for tax purposes as having bought a building, plus various separate items of 'plant'. Items of plant are depreciating assets, such as air conditioners, stoves and other items. The purchase price accordingly needs to be allocated between the 'building' and various depreciating assets.

You can deduct an amount equal to the decline in value for an income year of a depreciating asset that you held for any time during the year. However, your deduction is reduced to the extent you use the asset for a purpose other than a taxable purpose. From 1 July 2017, your deduction is also reduced by the extent you installed or used the asset in your residential rental property to derive rental income and the asset was a second-hand depreciating asset (unless an exception applies).

2.1.3. Capital Works

- If the building is under 25 years old you will be entitled to claim a deduction of 2.5% per year of the original cost of construction of the building for up to 40 years from the original date of construction.

- If you do not know the building cost (**Note**: this is not the purchase price) you can contract a quantity surveyor to determine the building costs and prepare the depreciation schedules for the property and determine what can be claimed.

2.1.4. Loan Interest

If you take out a loan to purchase a rental property, you can claim the interest charged on that loan, or a portion of the interest, as a deduction. However, the property must be rented, or genuinely available for rental, in the income year for which you claim a deduction.

You cannot claim a deduction for interest expenses you incur if:

- you start to use the property for private purposes, or
- you refinance an investment loan for private purposes or otherwise use the loan for a private purpose.

If the expenses were incurred partly for a private purpose, you must apportion the expense accordingly.

2.2. Expenses that can be deducted immediately

Expenses for which you may be entitled to an immediate deduction in the income year you incur the expense include:

- advertising for tenants
- bank charges
- body corporate fees
- cleaning
- council rates
- electricity and gas
- gardening
- lawn mowing
- in-house audio/video service charges
- insurance
- land tax
- legal expenses re leases etc.
- lease costs
- pest control
- mortgage discharge expenses
- property agent's fees
- quantity surveyor's fees
- security
- stationery
- postage
- telephone
- water charges
- lenders mortgage insurance (usually written off over the shorter of the term of the loan or 5 years)

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2.3. Expenses that cannot be deducted

- expenses incurred through the personal use of your investment property;
- the repayments of the principal sum borrowed to purchase the investment property;
- solicitor and conveyancer fees for the purchase or sale of the property;
- other expenses incurred during the purchase or sale of the investment property; and
- stamp duty fees charged on the transfer of property into your name.
- travel expenses to carry out the inspection of your rental property yourself used to be claimable but unfortunately no longer can be claimed.

2.4. Keeping records

Keep records of both income and expenses relating to your rental property.

Records of rental expenses must be in English, or be readily translatable into English, and include the:

- name of the supplier
- amount of the expense
- nature of the goods or services
- date the expense was incurred
- date of the document.

If a document does not show the payment date, use independent evidence, such as a bank statement, to show the date the expense was incurred.

Keep records of your rental income and expenses for five years from 31 October or, if you lodge later, for five years from the date you lodge your tax return. If at the end of this period you are in a dispute with us that relates to your rental property, keep the relevant records until the dispute is resolved.

The following list provides some examples of records you should keep to make it easier to complete your tax return:

- loan documents
- land tax assessments
- credit card records
- tenant leases
- bank statements
- rent records from managing agents.
- receipts for expenses, e.g. repairs, maintenance, insurance & purchases of depreciable assets

[03] TAX CONSIDERATIONS

You may make a capital gain or capital loss when you sell (or otherwise cease to own) a rental property that you acquired after 19 September 1985.

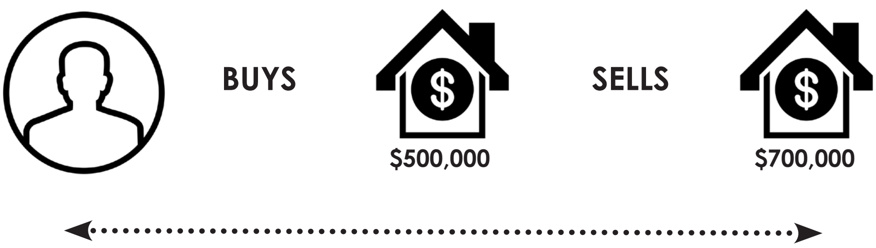
3.1. CGT

In the case of the sale or other disposal of real estate, the time of the event is normally when you enter into the contract (generally the date on the contract), not when you settle. The fact that a contract may be subject to a condition such as finance approval, generally does not affect this date. If there is no contract, the event takes place when the change of ownership occurs.

You will make a capital gain from the sale of your rental property to the extent that the capital proceeds you receive are more than the cost base of the property. You will make a capital loss to the extent that the property's reduced cost base exceeds those capital proceeds. If you are a co-owner of an investment property, you will make a capital gain or loss in accordance with your interest in the property.

The cost base and reduced cost base of a property includes the amount you paid for it together with certain incidental costs associated with acquiring, holding and disposing of it (for example, legal fees, stamp duty and real estate agent's commissions). Certain amounts that you have deducted or which you can deduct are excluded from the property's cost base or reduced cost base. From 1 July 2017, travel expenses you incur relating to your residential rental property are also excluded from the property's cost base or reduced cost base. You may be eligible for the CGT discount (50% reduction in the capital gain) if you have owned the asset for longer than 12 months.

CGT EXAMPLE



COST BASE FOR CGT CALCULATED AS:

COST BASE	Purchase Price	$500,000	**CAPITAL GAIN**	Sale Price	$700,000
	Legal fees	$15,000		Less cost base	$565,000
	Ownerhsip costs	$50,000			
				Gross Capital Gain	**$135,000**
				Less CGT Discount (50%)	($67,500)
	TOTAL:	**$565,000**		**NET Capital Gain**	**$67,500**

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Keeping adequate records of all expenditure will help you correctly work out the amount of capital gain or capital loss you have made when a CGT event happens. You must keep records relating to your ownership and all the costs of acquiring and disposing of property. It will also help to make sure you do not pay more CGT than is necessary.

You must keep records of everything that affects your capital gains and capital losses. Penalties can apply if you do not keep the records for at least five years after the relevant CGT event. If you use the information from those records in a later tax return, you may have to keep records for longer. If you have applied a net capital loss, you should generally keep your records of the CGT event that resulted in the loss until the end of any period of review for the income year in which the capital loss is fully applied. For more information, see Taxation Determination TD 2007/2.

You must keep records in English (or be readily accessible or translatable into English) that include:

- the date you acquired the asset
- the date you disposed of the asset
- the date you received anything in exchange for the asset
- the parties involved
- any amount that would form part of the cost base of the asset n whether you have claimed an income tax deduction for an item of expenditure.

3.2. Negative Gearing

A rental property is negatively geared if it is purchased with the assistance of borrowed funds and the net rental income, after deducting other expenses, is less than the interest on the borrowings.

The overall taxation result of a negatively geared property is that a net rental loss arises. In this case, you may be able to claim a deduction for the full amount of rental expenses against your rental and other income (such as salary, wages or business income) when you complete your tax return for the relevant income year. Where the other income is not sufficient to absorb the loss it is carried forward to the next tax year.

If by negatively gearing a rental property, the rental expenses you claim in your tax return would result in a tax refund, you may reduce your rate of withholding to better match your year-end tax liability.

NOTE: This information sheet is intended as a guide. All actual detail & circumstances differ, please discuss your situation with us.

[04] Rental Property Worksheet

The following completed worksheet is an example of how to work out your net rental income or loss.

A blank worksheet is also provided for you to work out your own net rental income or loss.

	$
Income	
Rental Income	9,500
Other rental income	600
Gross rent	10,100
Expenses	
Advertising	48
Body corporate fees	500
Borrowing expenses	259
Cleaning	100
Council Rates	700
Depreciation	796
Gardening	350
Insurance	495
Interest on loans	11,475
Land tax	200
Legal expenses	150
Pest control	50
Property agent fees & commission	800
Repairs & maintenance	1,000
Capital works	2,345
Stationery, telephone & postage	80
Water charges	350
Sundry	95
Total expenses	19,793
Net rental income or loss (\$10,100 - \$19,793)	- **9,693**

	$
Income	
Rental Income	
Other rental income	
Gross rent	
Expenses	
Advertising	
Body corporate fees	
Borrowing expenses	
Cleaning	
Council Rates	
Depreciation	
Gardening	
Insurance	
Interest on loans	
Land tax	
Legal expenses	
Pest control	
Property agent fees & commission	
Repairs & maintenance	
Capital works	
Stationery, telephone & postage	
Water charges	
Sundry	
Total expenses	
Net rental income or loss (Gross rent less total expenses)	

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