Depreciation benefits for first homebuyers

Tyron Hyde explains how first homebuyers can take advantage of the depreciation allowance if they decide to convert their home into a rental down the line

Last month I was having a beer at the North Bondi RSL with some Brazilian friends. Carlos proudly announced to the table that he had just become an Australian citizen.

"Carlos – why, after all these years have you finally become an Australian citizen?" I asked.

"Tyron – are you loco?" he replied, "What other country in the world gives you $24,000 to buy a property."

Good answer!

Then, last week, I was presenting my "Top Nine Tax Depreciation Tips" around the country (see May issue). At the end of every presentation a fresh-faced young person would raise their hand and ask the following question:

"I'm a first homebuyer and I plan to live in my property for a year then move out and turn that property into a rental. Can I still claim depreciation when I move out?"

I suspect this will be a common occurrence. As interest rates potentially increase, and as more people possibly lose their jobs – having someone else pay your mortgage could be a good option.

And the simple answer is yes – first homebuyers can still claim depreciation once they move out. So yes, you can have your cake and eat it too!

The facts

In case you haven't heard – first homebuyers are currently flooding the market looking to take advantage of some generous grants on offer.

While this is a national scheme it is funded and administered under the various states, so visit www.firsthome.gov.au for specific information pertaining to your state.

One theme is constant though – you must occupy the home as your principal place of residence for a continuous period of at least six months commencing within one year of the completion of the transaction to which the application relates.

Tax law: the good news

The Income Tax Assessment Act 1997 determines what types of properties qualify for building allowance deductions.

According to Section 43-90 'Residential Accommodation' is classified as a type of property that can attract building depreciation allowances, providing that was its intended use at the time of completion.

Luckily for first homebuyers, this requirement is satisfied even if the accommodation was intended to be used for private purposes or owner occupied after its completion.

The important part of the act relates to how the property is used in the "current year of use". Put simply – it's ok to live in the property for a year or so, move out, then claim depreciation.

How much can you claim? Let's do some number crunching

The answer will depend on the type of property purchased, how much you paid for it and the original building cost.

The first homebuyer grant favours buyers who purchase a brand new

Scenario 1 – Property investor puchases a new property and rents it out immediately. How much can be claimed?

Diminishing value method	Year 1	Year 2	Year 3	Year 4	Year 5
$300,000 New house	$9,000	$6,000	$6,000	$5,000	$5,000
$500,000 New house	$12,000	$10,000	$9,000	$9,000	$8,000
$300,000 New high-rise	$9,500	$7,000	$6,000	$5,000	$5,000
$500,000 New high-rise	$13,500	$11,000	$10,000	$9,000	$8,000

Prime cost method	Year 1	Year 2	Year 3	Year 4	Year 5
$300,000 New house	$5,000	$5,000	$5,000	$5,000	$5,000
$500,000 New house	$9,000	$9,000	$9,000	$9,000	$9,000
$300,000 New high-rise	$5,000	$5,000	$5,000	$5,000	$5,000
$500,000 New high-rise	$9,000	$9,000	$9,000	$9,000	$9,000

Scenario 2 – First home buyer purchases a property, lives in it for one year, then rents it out. How much can be claimed?

Diminishing value method	Year 1	Year 2	Year 3	Year 4	Year 5
$300,000 New house	NIL	$6,000	$6,000	$5,000	$5,000
$500,000 New house	NIL	$10,000	$9,000	$9,000	$8,000
$300,000 New high-rise	NIL	$7,000	$6,000	$5,000	$5,000
$500,000 New high-rise	NIL	$11,000	$10,000	$9,000	$8,000

Prime cost method	Year 1	Year 2	Year 3	Year 4	Year 5
$300,000 New house	NIL	$6,000	$6,000	$5,000	$5,000
$500,000 New house	NIL	$10,000	$9,000	$9,000	$8,000
$300,000 New high-rise	NIL	$7,000	$6,000	$5,000	$5,000
$500,000 New high-rise	NIL	$11,000	$10,000	$9,000	$8,000

There are two things that become obvious from the above tables:

1. The amount a first homebuyer can claim is ONLY affected while they live in the property.
This makes sense because while you live in the property, it is STILL depreciating – you just can't claim the depreciation as a tax deduction.
2. If I did buy a property as a first homeowner and lived in it for a year, using the diminishing value method would still be more beneficial in the short term.
But it's always best to check with a qualified Quantity Surveyor to ensure you maximise your tax savings.

So what do I recommend?

The intention of this article is not to advise first home buyers whether now is a good time to enter the market or not.
The intention is to let first homebuyer know that if you do turn your castle into a rental – don't ignore the depreciation benefits you're entitled to.
After all, as Kerry Packer once famously said: "Pay your tax – but don't tip them… they are not doing that good a job!"

property. By favouring new property, the government is hoping to stimulate building activity – which is generally the first industry to lead the way out of a recession.

The building industry also stimulates other industries such as retail (people need to buy new TVs, lounges etc). For that reason I have decided to calculate the depreciation on a new property.

Also keep in mind that when quantity surveyors provide reports to investors we generally provide the taxpayer with two options in which they can claim the relevant allowances.

One way is the "diminishing value method" which accelerates the allowances you can claim.

The other method is the "prime cost method" which evenly spreads out the allowances you can claim.

The one you use will depend on how long you intend to use the property as an investment.

Tyron Hyde is director of quantity surveying firm Washington Brown. For more information visit www.washingtonbrown.com.au where you can estimate the likely tax depreciation deductions on your property before you buy it. It's free of charge, and it allows you to compare apples with oranges and see what works best for you.