Depreciation 101

Tyron Hyde explains the basics of depreciation and how it can boost your tax savings

1 What is property depreciation?
Just like you claim wear and tear on a car purchased for income-producing purposes, you can also claim the depreciation of your investment property against your taxable income. There are two types of allowances available: depreciation on plant and equipment, and depreciation on building allowance. Plant and equipment refers to items within the building such as ovens, dishwashers, carpet, blinds, etc. Building allowance refers to construction costs of the building itself, such as concrete and brickwork. Both these costs can be offset against your assessable income.

2 How do you make a claim for depreciation allowance?
In order to make a claim for depreciation you need a report that breaks down the property into different categories. This report is called a depreciation schedule.

The amount the depreciation schedule says you can claim effectively reduces your taxable income.

In a depreciation schedule a quantity surveyor will separate the plant items (oven, dishwasher, etc) from the structural elements such as bricks and concrete.

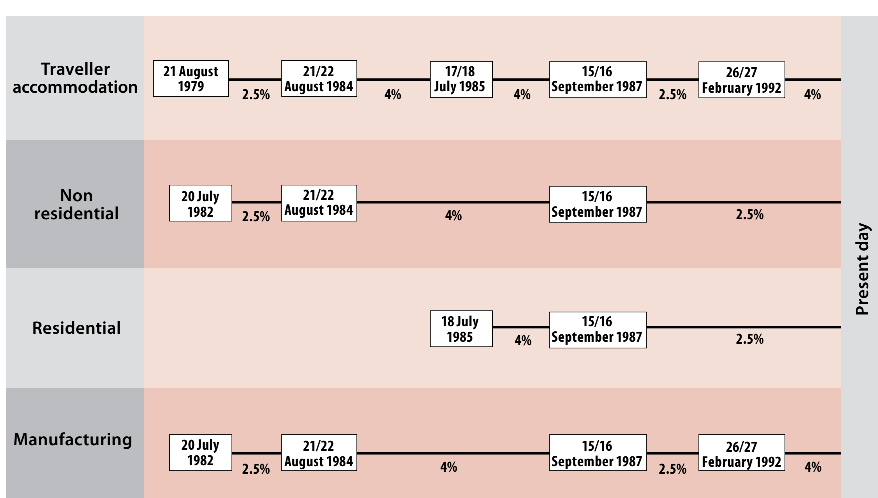
Why? Because different elements have different rates of depreciation, which are generally based upon how long the item will last.

For instance, if an oven costing $1,000 has a 10-year life – you can claim $100 against your taxable income for 10 years using the Prime Cost Method of depreciation.

3 When do I need the depreciation schedule and how often should I have it prepared?
You should get the depreciation schedule prepared straight after settlement, if possible. That way the quantity surveyor will see your property in the true state of what you have purchased. And if the tenant hasn't moved in yet, that's a bonus, as it will avoid disruption.

Chart 1: Does your building qualify?

The commencement of construction dictates what building allowance you can claim



The good news is – you only need to have the depreciation schedule prepared ONCE – not every year as some people think.

4 Is my property too old to claim property depreciation?
The simple answer is no. If your residential property was built after July 1985 you will be able to claim both building allowance and plant and equipment. If construction on your property commenced prior to this date, you can only claim depreciation on plant and equipment (ie carpet, blinds, oven, etc). But it will still be worthwhile to do so.

Commercial and industrial properties are subject to varying cut-off dates.

Chart 1 below shows the relevant timelines for differing types of property construction.

5 Who should prepare your depreciation schedule?
If your residential property was built after 1985 your accountant is not allowed to estimate the construction costs. Tax Ruling 97/25 issue by the Australian Taxation Office (ATO) has identified quantity surveyors as properly qualified to make the appropriate estimate of the construction costs, where those costs are unknown. Real estate agents, property managers and valuers are not allowed to make this estimate.

6 How will the quantity surveyor assess the property for depreciation purposes?
The Australian Institute of Quantity Surveyors (AIQS) Code of Practice stipulates that site inspections are necessary to satisfy ATO requirements.

A trained quantity surveyor will ensure all depreciable items are noted down and photographed. This guarantees that you won't miss out on any deductions. The documentation can then be used as evidence in the event of an audit. They will also liaise directly with the tenant or property manager in order to cause minimal disruption to the tenant.

The best time to get a quantity surveyor to inspect your property is immediately after settlement before the tenant has moved in.

7 My property is renovated. Can I still claim?
Yes. We will need to know how much you spent on renovations. This is an ATO obligation. If the previous owner completed the renovations you are still entitled to claim depreciation. In either case, where the cost of renovation is unknown, a quantity surveyor has been identified by the ATO as being appropriately qualified to make that estimation.

8 How much will my property depreciation schedule cost?
The cost of preparing a tax depreciation schedule varies according to the type of property you've purchased, its location, size and numerous other factors. Generally, you will find most of the leading quantity surveying companies offer a money-back guarantee that says you will save twice your fee in the first year or they give you the report for free. Quantity surveyors' fees are also 100% tax deductible.

9 How much tax will I save?
Each property is different and many varying factors must be considered when preparing a property depreciation schedule. There are several depreciation calculators on the market. I suggest you Google 'depreciation calculator' to find one. I wouldn't bother paying for a property depreciation estimate – the best ones on the market are free in my opinion.

10 How long will it take to complete my schedule?
Your depreciation schedule will take approximately two to three weeks to complete, as long as the quantity surveyor can inspect your property without delay.

11 I bought my property three years ago. Can I still make a claim?
Yes, you can. Your accountant can amend your previous tax returns up to two years back. There are some exceptions so please contact your tax agent or the ATO for clarification. ■

Tyron Hyde is director of quantity surveying firm Washington Brown. Visit www.washingtonbrown.com.au

Legal Q&A

Geri Forsaith, licensed conveyancer with Sydney Property Conveyancing, answers a reader's question on when does a mortgage become legally binding to both the borrower and lender?

Q When does a loan becomes 'yours' and at what date are lenders obligated to lend you money on the terms and conditions they have specified? On the day we took out our mortgage the bank informed us that a new $8 per month account keeping fee was now going to be charged on the loan. This fee was imposed between the time that we sat down and negotiated (and applied) for the loan and the time we actually took it out.

A When obtaining a loan, each purchaser, known as the mortgagor, will be provided by their lender, known as the mortgagee, a set of loan documents plus their terms and conditions that will set out, among other details, the mortgagee's fees and charges.

Loans for residential property are regulated by the Consumer Credit Code and mortgagees are required to disclose all relevant information, including interest rates and fees about your loan, before entering into the loan agreement.

The mortgagee may vary any provision of the loan agreement as they choose before and after the loan has been advanced. If a Consumer Credit Code, the Code of Banking Practice or the Electronic Funds Transfer Code of Conduct applies to your loan agreement, the mortgagee may only make changes in accordance with those codes. These changes must be notified to you in writing either directly or by media advertisement.

The change will take effect from the time specified in their notice.

The mortgagee will not make the loan advance until all their settlement requirements are met – a few of these requirements are:

- The title to each security property is satisfactory
- All searches, certificates and valuations relating to the security property have been provided and are satisfactory
- Evidence of council, water and other rates and taxes have been paid for the security property
- Nothing has happened since you first applied for the loan that may be detrimental to your financial situation

Your loan will become 'yours' when settlement of your purchase has taken place, and typically the first loan repayment will be due 30 days after settlement date. To ensure you are fully informed of your loan terms and conditions, it is wise to obtain advice from your conveyancer/solicitor before signing your loan agreement.