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Depreciation for commercial property

Tyron Hyde explains the difference between residential and commercial properties when it comes to claiming depreciation allowance

Let's face it: compared to residential property, commercial property has been smashed.

The number of transactions has plummeted, and the transactions that have occurred are well below the value of two to three years ago.

The Australian Financial Review recently ran an article suggesting that the Australian Stock Exchange Building in Sydney is likely to be sold for $150m – which is almost $100m less than it was bought for three years ago!

So now may be the right time to go from being tenant to master of your domain by buying that building from your landlord.

If you do, you must consider the tax depreciation allowances that are available for commercial property, since they differ from the allowances you can claim on residential property.

Difference #1: You can occupy the commercial property and still claim tax depreciation

If you purchase a residential property to live in, you cannot claim depreciation on that property as it is not income producing. But with commercial property, you can spend as much time in the office as you like, and the Australian Taxation Office still won't consider it as your principal place of residence!

Many people buy commercial property in their own name or self-managed super fund, and then lease the property back to the business they own. This enables the individual taxpayer or super fund to claim the depreciation allowance, which can be substantial. And best of all, it's totally legal!

Difference #2: Older buildings qualify for the building allowance

Building allowance refers to the decline in value of the bricks and mortar of your property. The date when construction commenced usually determines whether you can claim the depreciation of the structure against your taxable income.

With residential property, construction must have commenced after 18 July 1985 to be eligible (see the graph below).

However, with commercial property, the building can be three years older and still qualify. That is, construction of a commercial property needs to have commenced after 20 July 1982 in order to qualify.

Difference #3: The items you can claim and at what rate also differ

Each year the Tax Commissioner publishes a list of what items you can and cannot claim.

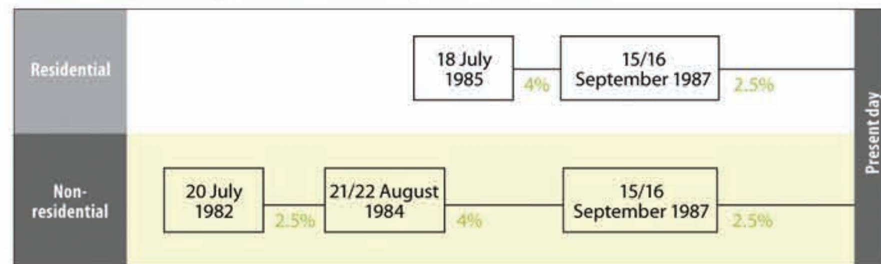
Residential property owners have their own definitive lists, detailing the items of plant and equipment that can be claimed. For instance, you can claim the decline in value of items like ovens, dishwashers and blinds against your taxable income.

Commercial property owners don't have their own 'special list', but some differences are pointed out in the *Effective Life Schedule* published by the Australian Taxation Office (ATO). For instance, carpet in residential property can be claimed over a 10-year period – but in commercial property, carpet is claimed over an eight-year period. This is because the ATO recognises that carpets will wear and tear faster in a commercial property due to the higher volume of people walking on them.

Some other differences include blinds – which according to the ATO last longer in commercial buildings and can be claimed over 20 years, as opposed to residential buildings where they are claimed over a 10-year period.

The latest Schedule of Effective Life is known as Tax Ruling TR 2009/4 and also highlights industry-specific items. For instance, if your business is a restaurant, the ATO has a completely separate category of items you can claim. There is a very detailed list of businesses that are separated right down to pig farming! You can find the details at http://law.ato.gov.au/atolaw/view.htm?DocID=TXR/TR20094/NAT/ATO/00001

The commencement of construction dictates what building allowance you can claim



Let's do some number crunching

So how does commercial property stack up against residential in relation to depreciation?

There are some similarities between the two. For instance, the higher the quality of the commercial property, the higher the depreciation – this is the same in residential property. And the taller the building a commercial property is, the higher the depreciation allowance (the same thing happens with residential property). This is due to taller buildings having more services, such as lifts and fire services.

Just like residential property, the newer the building the higher the depreciation allowance will be. Using the Washington Brown Depreciation Calculator* I have exported data about commercial and residential properties (see the table above). The results show that the depreciation in a commercial suite is somewhere in between a high-rise and low-rise residential apartment. You will also get more depreciation on a commercial suite as opposed to a factory unit. This is because a factory unit does not have as much plant and equipment, and is almost completely made of concrete and steel.

Commercial vs residential

Price & Type	Year 1	Year 2	Year 3
$500,000 New commercial suite	$12,000	$10,000	$9,000
$500,000 High-rise residential	$13,000	$11,000	$9,000
$500,000 Low-rise unit	$11,000	$9,000	$8,000
$500,000 Industrial suite	$9,000	$8,000	$7,000

In summary

If you are the tenant in a commercial property, and think now might be a good time to become the owner/occupier, don't forget to claim those tax depreciation allowances available to you as a landlord. If the original costs of construction are unknown, instruct a qualified quantity surveyor to estimate them. ■

**Results from the Washington Brown Depreciation Calculator may vary from time to time as the calculator is dynamic and changes as more properties are inputted.*

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