MAVERICK™

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FEATURED

Choose to increase your cash flow now or later

Select the best method to fit your investment strategy

The Australian Taxation Office (ATO) allows investors to choose between two methods of claiming depreciation on the fixtures and fittings within their investment properties. These are the diminishing value and the prime cost methods of depreciation.

Every property investor is likely to have a different investment strategy, so it is important for them to understand how their choice between the two different methods of claiming depreciation will affect their cash flow.

The diminishing value and prime cost methods both claim the total depreciation value available over the life of a property. However, the two methods use different formulas to calculate depreciation deductions, achieving different short and long term cash flow positions for the property investor.

Legislation allows property investors who use the diminishing value method to increase the rate an asset depreciates at, therefore increasing deductions sooner. This method calculates the depreciation based upon the reduced written down value remaining so the deduction diminishes over time.

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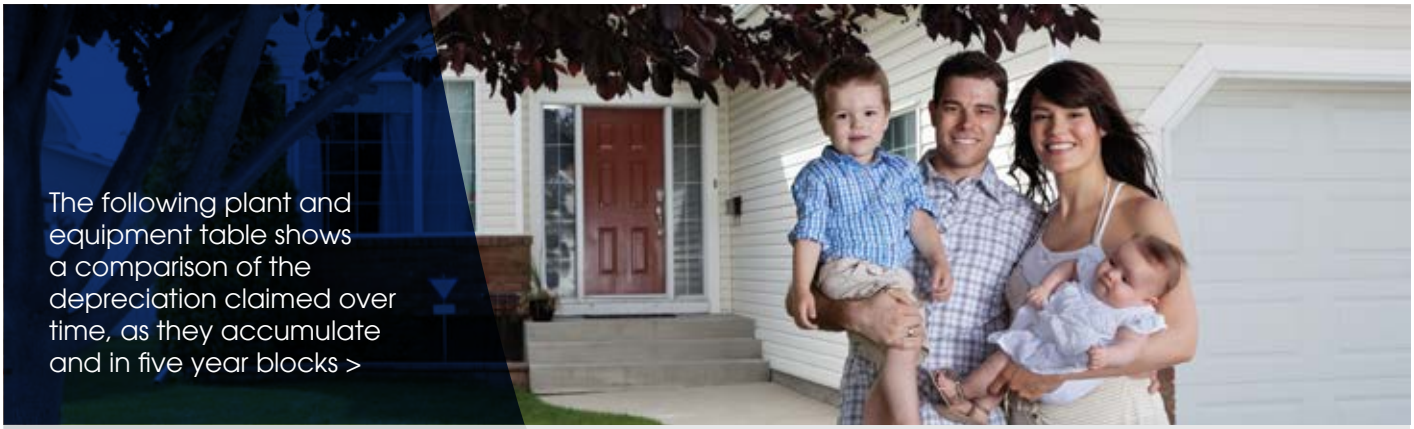
BMT Tax Depreciation
QUANTITY SURVEYORS

> “In the eleven to fifteen year period, the prime cost claim was $5,026 compared with only $2,305.”

The prime cost method uses a lower percentage rate of depreciation and results in a consistent deduction per year, spreading the deductions out more evenly over time.

To investigate how the outcome varies over a five, ten and fifteen year period for both methods, a sample of BMT Tax Depreciation Schedules was analysed for properties which contained assets totalling $33,000 in value.



The following plant and equipment table shows a comparison of the depreciation claimed over time, as they accumulate and in five year blocks >

Diminishing value method (total plant and equipment value $33,000)			
	1-5 years	1-10 years	1-15 years
Average cumulative depreciation claimed	$21,991 (67%)	$30,174 (91%)	$32,479 (98%)
	1-5 years	6-10 years	11-15 years
5 yr. term amount	$21,991 (67%)	$8,183 (25%)	$2,305 (7%)

Prime cost method (total plant and equipment value $33,000)			
	1-5 years	1-10 years	1-15 years
Average cumulative depreciation claimed	$13,912 (42%)	$27,762 (84%)	$32,788 (99%)
	1-5 years	6-10 years	11-15 years
5 yr. term amount	$13,912 (42%)	$13,850 (42%)	$5,026 (15%)

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The figures in this table are based on the depreciable claim for plant and equipment only for the sample reports analysed.

The analysis found that investors who chose the diminishing value method had claimed 67% of the depreciation available in the first five years. By comparison, 42% of the depreciation available had been claimed by investors who chose the prime cost method over the same period.

At the ten year period, investors who chose the diminishing value method had claimed 91% of the deductions available, while investors who chose the prime cost method had only claimed 84% of the total deductions available.

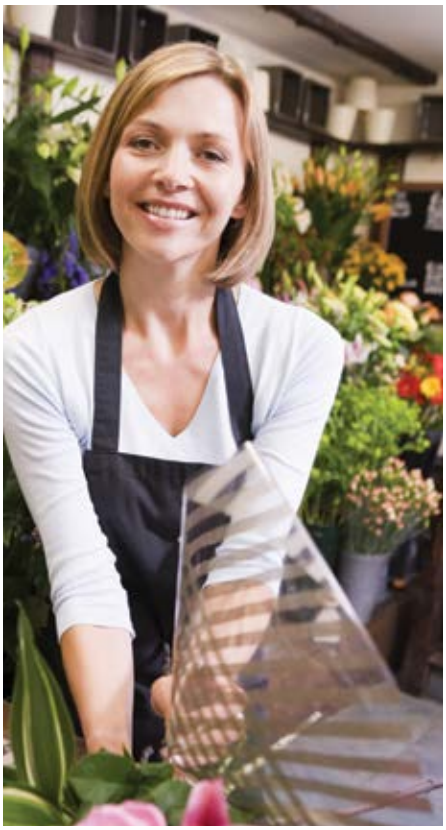
After fifteen years investors using each method had claimed almost all the deductions available, with 98% of deductions claimed using the diminishing value method and 99% using the prime cost method. The remaining depreciation claim of $521 for the diminishing value method or $212 from the prime cost method after fifteen years would be claimed over the balance of the life of the property.

As the example shows, investors who choose the diminishing value method claim greater depreciation deductions in the earlier years of owning the property. From the sample we can see $21,991 in depreciation deductions were claimed using this method by comparison to $13,912 using the prime cost method in the first five years. If an investor is only planning on holding a property for a shorter period of time, they wish to build their investment portfolio quickly or they want to save quickly to budget for a renovation to the property, this method might be their preference.

Alternatively, those who prefer to claim deductions at a more constant rate over a longer period of time may choose the prime cost method of depreciation. As can be seen in the sample, those who chose this method would be able to claim higher deductions in the eleven to fifteen year period, where the total claim using the prime cost method was $5,026 compared with only $2,305 using the diminishing value method.

A property investor can only use one method to claim depreciation deductions. Once an investor chooses the depreciation method used for an asset, it cannot be changed. It is recommended that investors discuss which method best suits their individual situation with an Accountant and to consult with a Quantity Surveyor who will find the highest possible deductions for each of the two methods.

To see each alternative formula, scan this QR code or visit bmtqs.com.au/formulas



TECHNICAL

Be super aware

Self Managed Super Funds, property and depreciation

Over the last six years, the total number of Self Managed Super Funds (SMSFs) in Australia grew from 399,474 to 509,992 according to statistics from the Australian Taxation Office (ATO).

Those who elect to put their superannuation into a SMSF gain more control over where their retirement funds are being invested because they, as members, become a trustee. Trustees of SMSFs can choose to invest in almost any investment product, subject to restrictions set by the ATO and the Superannuation Industry Supervision (SIS) Act.

> “Gain more control over where your retirement funds are being invested.”

In September 2007, amendments were inserted into the SIS Act 1993 which enabled the trustees of a SMSF to set up a structure allowing them to borrow money in order to invest in real estate. As a result, over the past few years BMT Tax Depreciation has experienced a significant increase in the number of tax depreciation schedule requests from SMSFs.

A number of requirements surround this new legislation. One of the most important rules a property investor should note is that all transactions within a SMSF must be made and maintained at a distance. For example, if a SMSF owns residential properties, the trustee will not be able to personally rent them. The ATO sees this as a personal benefit. However, if a SMSF owns commercial properties, a trustee’s business may rent the premises provided the corporation pays what is seen to be a fair market value rent.

Claiming depreciation for SMSF properties

There are tax implications when the trustees of a SMSF choose to invest in real estate. As with any other property investment, SMSF trustees who invest in real estate are entitled to a capital works deduction for the wear and tear on a building’s structure and also for the depreciation of all plant and equipment items contained inside and outside the property.

WHAT’S NEW

New

Immediate write-off threshold now in place

- Changes made last year to the immediate write-off threshold for small business have now been reversed back to $1,000
- Assets exceeding the $1,000 threshold will be allocated to a general small business pool for depreciation claims

To request more information email newruling@bmtqs.com.au

“Add $2,340 to your retirement.”

Case study

In the following example, a SMSF owns a two bedroom apartment purchased for $620,000 with a rental income of $650 per week, resulting in a total income of $33,800 per annum.

Expenses for the property such as interest rates, management fees and holding costs totalled to $41,724. Therefore the SMSF has a tax deductible loss for this residential property of $7,924 prior to lodging their tax assessment. The tables below show the difference claiming depreciation will make to a property owned in a SMSF.

Scenario 1 - without depreciation claim:

Pre-tax cash flow		Post-tax cash flow (tax rate 15% SMSF rate)	
Total loss before tax (income - expenses)	- $7,924	Total loss before tax	- $7,924
Cash position per week	- $152	Less tax refund ($7,924 taxable loss x 15%)	- $1,189
		After tax cash position (total loss before tax + tax refund)	- $6,735
		Cash position per week	**- $130**

Scenario 2 - with depreciation claim:

Pre-tax cash flow		Post-tax cash flow (tax rate 15% SMSF rate)	
Total loss before tax (income - expenses)	- $7,924	Total loss before tax (income - expenses - depreciation claim)	- $23,424
Depreciation claim	$15,500	Less tax refund ($23,424 taxable loss x 15%)	- $3,514
Taxable loss including depreciation	- $23,424	After tax cash position (total loss before tax + tax refund)	- $4,410
		Cash position per week	**- $85**

The depreciation estimates in the above case study have been calculated using the diminishing value method of depreciation, are based on a tax rate of 15% and are based on a claim for a property held for a full twelve month period.

2013_TV1

Without claiming depreciation, the SMSF is only able to claim $7,924 and receive a refund of just $1,189, resulting in a negative cash position of -$130 per week. A typical two bedroom apartment would expect around $15,500 in depreciation available in the first full year. By claiming $15,500 in depreciation, the total deductible loss is increased to $23,424. By claiming the 15 per cent on the total deductible loss of $23,424, the SMSF will receive a tax refund of $3,514, thereby adding $2,340 to the retirement fund in the first year.

It is important that SMSF trustees always take advantage of the additional funds available via a depreciation claim. BMT Tax Depreciation advises any SMSF trustees who are considering investing in property to always seek the advice of an Accountant and to consult with a specialist Quantity Surveyor to find out how much depreciation can be applied to their SMSF investment property.

For more information visit bmtqs.com.au/depreciation or call 1300 728 726 to speak to a depreciation expert.

What’s in your schedule?

To ensure every investor’s claim is maximised, BMT have designed a more comprehensive depreciation schedule. Below is a list of what to expect in a BMT Tax Depreciation Schedule:

- **A glossary of terms** simplifies the terminology used for easy understanding
- **A one page overview** explains the total deductions for each depreciation method
- **Both prime cost and diminishing value method** deductions are shown for plant and equipment assets
- **A forty year projection** shows all of the deductions available for the life of the property
- **Low-value and low-cost pooling** are used to accelerate deductions
- **The effective life of each asset** is displayed and a subtotal shown for the division 40 effective life and pooled assets
- **A pro-rata calculation** will be used when a property is acquired part way through a financial year or rented for only a percentage of the year
- **Percentage based grouping of assets** shows a calculation of all assets depreciated at the same percentage rate grouped and totalled
- **Split reports** are available when a property is owned by more than one person, resulting in higher deductions earlier
- **Excel and CSV formats** are provided to Accountants for easy use with software.

BMT Tax Depreciation are proud members of:

Valuable tools for you

Help available on the go with BMT's customised apps

BMT has developed a complete range of specialised property and depreciation apps available online and for mobile devices. These apps have been designed for investors, Property Professionals, Accountants and Developers to access useful information quickly and easily.

BMT Rate Finder Specially designed for Accountants

Finds the effective life and depreciable rate of any plant and equipment asset (commercial or residential).

BMT Resi Rates Specially designed for Property Managers

Finds the effective life and depreciable rate of plant and equipment assets for residential properties which can assist with disputes over damaged assets and maintenance and replacement scheduling.

BMT Tax Depreciation Calculator Specially designed for Property Investors

Estimates the likely deductions available to claim on any existing or prospective investment property, allowing users to easily project their after tax cash flow.

BMT Construction Costs Calculator Specially designed for Developers

Estimates a range of construction costs for any new development including the site works, building margins and basic landscaping.

Download BMT's apps now at bmtqs.com.au/app or try the online version.

MORE FOR YOU

Resolve disputes with Resi Rates

New app helps Property Managers and landlords

We've all heard the horror stories about tenants who damage parts of the building structure or assets contained in an investment property and the disputes that arise over who will pay for this damage.

Whether deliberate or not, disputes over damaged assets often escalate, leaving the Property Manager in the middle trying to bring the situation to a peaceful resolution.

BMT Tax Depreciation has designed a new app which allows Property Managers to search and find the depreciation rate and effective life of any depreciating asset normally found in a residential property. The new app has proven to be effective in helping Property Managers to resolve disputes over damaged assets and with maintenance and replacement scheduling.

Case study

An investor purchased a property two years ago. Before renting the property they installed brand new carpet at a cost of $3,155.

After owning and renting the property for two years, the tenants decided to end their lease. On the exit inspection, the Property Manager discovered substantial damage to the carpet in the property.

As the carpet needed replacing, a dispute arose over whether the costs for the damage should be covered in part by the tenants.

The Property Manager conducted a search on Resi Rates to find out the effective life and depreciation rate for carpet. From their search, they discovered that carpet in a residential property has an effective life of ten years, which works out to a rate of ten per cent per year using the prime cost method.

The Property Manager was able to calculate that based on the effective life of carpet as set by the Australian Taxation Office there was still $2,555 of value left in the existing carpet.

Below is the formula the Property Manager used to calculate the remaining value the property owner would lose due to the exacerbated damage to the carpet.

$3,155 - ($3,155 x 10%) = $2,839.50	**$2,839.50 - ($3,155 x 10%) = $2,524**

The formula above used straight line deductions to work out the remaining depreciable value available.

This information shows that the tenant had destroyed a valuable asset. The Property Manager was then able to use this information to form a case for the tenants to be responsible for paying the remaining $2,524 as damages to the property owner.

Construction costs

Including regional variations

As per standard practice, to adjust costs for various regions simply multiply the construction cost by the regional variations opposite. This will give you an approximate cost for the construction type per square metre in your area.

Regional Variations

Hobart	87 - 97%
Canberra	96 - 104%
Melbourne	98 - 108%
Adelaide	98 - 110%
Sydney	100%
Perth	100 - 120%
Brisbane	105 - 115%
Cairns	115 - 130%
Darwin	110 - 120%

Construction type / Level of finish

Construction type		Low	Medium	High
House	3br brick veneer project home, level block, single level, shelf design	$1,065	$1,270	$1,630
	3br full brick project home, level block, single level, shelf design	$1,090	$1,305	$1,670
	4br brick veneer home, level block, single level, unique design	$1,570	$1,750	$1,950
	4br full brick home, level block, single level, unique design	$1,640	$1,810	$2,010
	3br brick veneer project home, level block, two level, shelf design	$1,110	$1,310	$1,710
	3br full brick project home, level block, two level, shelf design	$1,130	$1,400	$1,790
	4br brick veneer home, level block, two level, unique design	$1,700	$1,900	$2,050
	4br full brick home, level block, two level, unique design	$1,780	$1,970	$2,250
	Architecturally designed executive residence	$2,160	$3,250	$5,050
Townhouse	2br, single level brick veneer townhouse, including allowance for common property	$1,250	$1,490	$1,740
	2br, 2 level brick veneer townhouse, including allowance for common property	$1,350	$1,580	$1,900
	3br, single level brick veneer townhouse, including allowance for common property	$1,235	$1,475	$1,725
	3br, 2 level brick veneer townhouse, including allowance for common property	$1,340	$1,610	$2,270
Unit	3 level walk-up unit complex, concrete structure, ground floor parking	$1,650	$1,820	$2,320
	3 level walk-up unit complex, concrete structure, basement parking	$1,615	$1,785	$2,285
	4-8 level walk-up unit complex, concrete structure, ground floor parking	$1,720	$1,950	$2,650
	4-8 level walk-up unit complex, concrete structure, basement parking	$1,650	$1,920	$2,615
	8 or more level unit complex, including lift and basement car parking	$1,710	$2,280	$3,030
Commercial	1-4 level open plan offices, including A/C & lifts, excluding fit out	$1,480	$1,760	$2,290
	4-8 level open plan offices, including A/C & lifts, excluding fit out	$1,620	$1,850	$2,400
	8 levels and over, including A/C & lifts, excluding fit out	$1,880	$2,064	$2,770
Industrial	High bay warehouse, standard config, concrete floor, metal clad	$810	$885	$980
	High bay warehouse, standard config, concrete floor, pre-cast concrete wall clad	$1,050	$1,110	$1,250
Retail	Suburban shopping mall area including A/C	$1,590	$1,810	$2,100
	Supermarket, including A/C, excluding fit out	$1,380	$1,500	$1,670
Hotel / Motel	Single level boutique motel, including A/C, guest facilities	$2,650	$3,200	$4,500
	Single level tavern/hotel, including A/C, excluding loose item fit out	$1,980	$2,350	$2,650

The above rates are exclusive of GST. Please visit www.bmtqs.com.au for more information.

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Newcastle
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Broadmeadow NSW 2292
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Melbourne VIC 3000
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