Guide to

Residential Depreciation

Disclaimer: The information is provided by New Vision Real Estate. It is a general guide and does not constitute financial, legal or taxation advice. All figures are supplied as examples and may not represent your personal circumstances.

You acknowledge and agree you must undertake your own analysis and obtain independent legal, financial and taxation advice before using, relying or acting on any information supplied on this website.

Neither New Vision Real Estate, nor its Directors, Shareholders or Advisors make any representation or warranty as to the accuracy or completeness of information found in these typical examples. Nor will they have any liability to you or any other party for any representations (expressed or implied) contained in, or any omissions from, that information.

CONTENTS

Property depreciation 101	04
How depreciation is calculated	06
Case studies	10
What is a tax depreciation schedule?	10
Depreciation questions answered	18
About New Vision Real Estate	20
Key terms	24

Congratulations! You have taken the first step to maximising your cash flow.

This guide will help you understand:

- How you can claim more on your investment property
- What property depreciation is
- What a tax depreciation schedule is and why you need one
- How to get a tax depreciation schedule.

PROPERTY DEPRECIATION 101

What is depreciation?

Depreciation is the natural wear and tear of a property and its assets over time. As the owner of an income-producing property, you can claim this depreciation as a tax deduction every year.

How does depreciation save you money?

Depreciation is the second biggest tax deduction for investment property owners after loan interest. It can reduce your taxable income by a significant amount each year, often thousands of dollars, which means you will pay less tax and have more money back in your pocket!

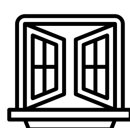
Taxable income - depreciation deductions = Less tax to pay

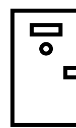
What can be depreciated?

There are two categories when it comes to claiming tax depreciation: capital works and plant and equipment deductions.

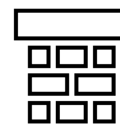
1. Capital works

Capital works deductions can be claimed for the building's structure and fixed assets. Examples are:


Windows

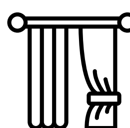

Doors, locks and door handles

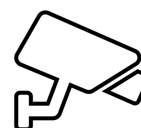
Bathtubs

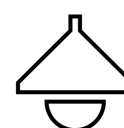

Doors, locks and door handles

2. Plant and equipment

Plant and equipment deductions can be claimed for easily removable and mechanical fixtures and fittings. Examples are:


Blinds and curtains

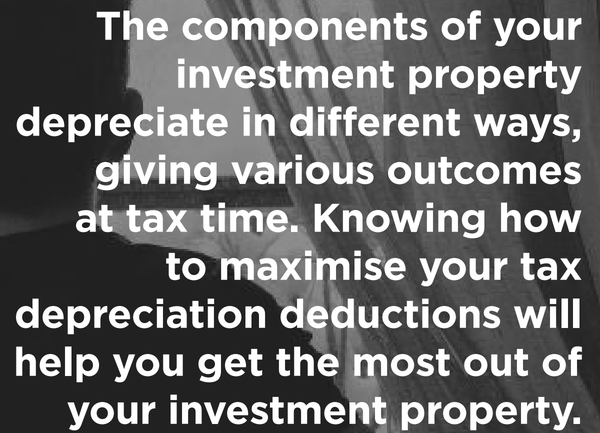

Security systems


Light fittings

Hot water systems

Being a property investor means you can claim more at tax time than ever before. Interest repayments, council rates, repairs, insurance and property management fees are just some of the tax deductions you can claim. But there is one other deduction that is easily missed, and it's called depreciation.

Get a FREE depreciation estimate before requesting a tax depreciation schedule.



The components of your investment property depreciate in different ways, giving various outcomes at tax time. Knowing how to maximise your tax depreciation deductions will help you get the most out of your investment property.

HOW **DEPRECIATION** IS CALCULATED

Capital works

Claiming capital works deductions is relatively straightforward. Capital works deductions can be claimed from the date construction was completed. Deductions are calculated at a constant annual rate as follows:

- 4 per cent over 25 years for properties that commenced construction between 18 July 1985 and 15 September 1987
- 2.5 per cent over 40 years for properties constructed from 15 September 1987 onward

Don't worry if your property was built before 1985, it could still hold capital works deductions. Renovated properties often carry significant capital works deductions, even if the renovation was completed by a previous owner!

Figure 1: Capital improvement deductions

Asset	Original value at purchase	First full financial year deductions
Bath	$1,640	$41
Tiling	$10,600	$265
Retaining Wall	$32,000	$800

Ten-year-old house purchased two years ago.

Plant and equipment

Calculating plant and equipment depreciation is more complex. Each asset's condition, quality and effective life determine the allowances available.

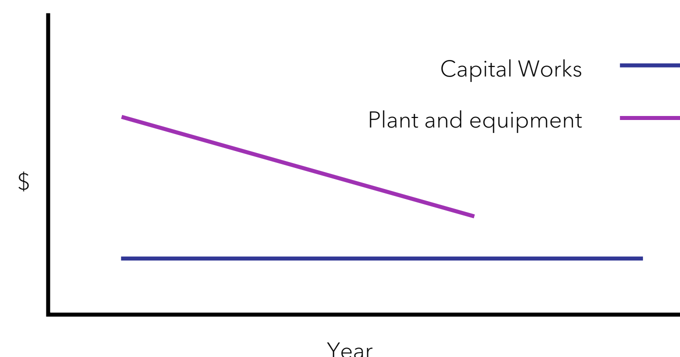
The effective life is how long the asset can be used to produce income. Assets that perform similar jobs can have different effective lives. For example, carpet has an effective life of eight years, while floating timber floors have an effective life of 15 years.

There are also two methods that can be used to depreciate plant and equipment assets: the diminishing value method and the prime cost method. Both methods use the same asset start values but achieve different short and long-term deductions and therefore cash flow outcomes.

Diminishing value method

The diminishing value method calculates deductions as a percentage of the asset's depreciable balance. This means deductions are higher in earlier years (Figure 2).

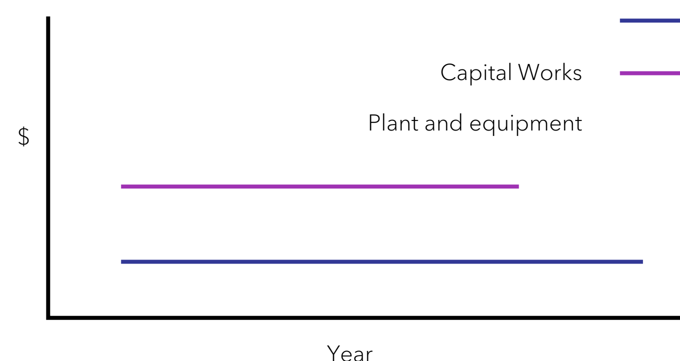
Figure 2: Capital works plus plant and equipment using diminishing value method



Prime cost method

The prime cost method calculates deductions each year as a percentage of the asset's cost. The result is that deductions are spread out over time with a more even claim each financial year (Figure 3).

Figure 3: Capital works plus plant and equipment using prime cost method



You can only choose one of these depreciation methods for the lifetime of your depreciation schedule, so it's important to understand how this choice will affect your investment before you claim. A specialist quantity surveyor and a trusted accountant can help you decide what's best aligned with your investment strategy.

Example:

Chris has an investment property which he intends to sell in five years. He is keen to maximise his cash flow before then.

Chris needs to replace some flooring in the property. He doesn't mind what type of flooring is installed but wants it to yield the highest tax deductions while he still owns the property.

Chris investigates the difference between installing carpet and floating timber floorboards. Chris discovers that carpet has an effective life of eight years, and that it depreciates at 25% under the diminishing value method and 12.5% under the prime cost method.

He finds that floating floorboards have an effective life of 15 years, and they depreciate at 13.33% under the diminishing value method and 6.67% under the prime cost method.

If Chris installs $8,000 worth of carpet, he can claim $2,000 in depreciation deductions in the first full financial year under the diminishing value method. These deductions will decrease each year until they run out. The five-year cumulative deductions under this method total $6,102. Under the prime cost method, Chris can claim $1,000 per year for eight years. The five-year cumulative deductions under this method total $5,000.

If Chris spends the same amount on floorboards, he can claim $1,066 in depreciation deductions in the first full financial year under the diminishing value method. These deductions will decrease each year until they run out. The five-year cumulative deductions under this method total $4,086. Under the prime cost method, Chris can claim $536 per year for 15 years. The five-year cumulative deductions under this method total $2,680. (Figures 4 and 5).

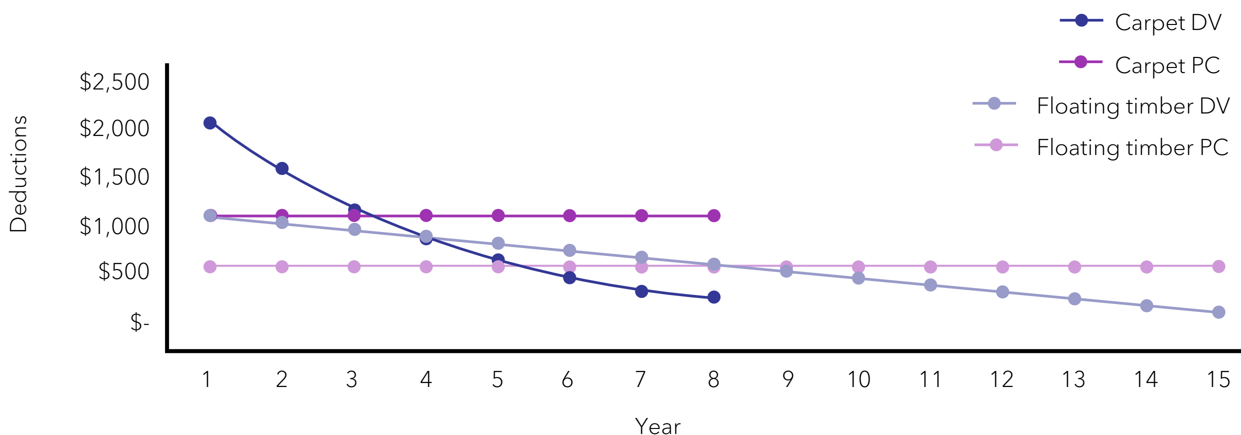
Since it delivers the highest cumulative tax deductions over five years, Chris chooses to install carpet.

Figure 4: Carpet versus floating floorboards

Asset	Carpet	Floating floorboards
Effective life	8 years	15 years
Percentage with DV	25%	13.33%
Percentage with PC	12.5%	6.6%
Five-year cumulative deductions on asset costing $8,000 with DV	$6,102	$4,086
Five-year cumulative deductions on asset costing $8,000 with PC	$5,000	$2,680

DV = diminishing value. PC = prime cost

Figure 5: Carpet versus floating floorboards



Immediate deductions and pooling

Plant and equipment assets can also be claimed as an immediate deduction or placed in a low-value pool if they meet the following criteria.

Immediate deductions
The 'immediate deduction' is a straight-forward incentive for residential property investors. It allows an immediate tax deduction for any new asset that costs $300 or less.

To be an 'immediate deduction' an asset must:

- **Not cost more than $300,** unless owned by multiple investors. For example, if two investors own equal shares in a rental (50:50) and purchase a ceiling fan worth $500, both could claim the immediate deduction. This is because each investor owns a 50 per cent portion of the asset, coming to $250.
- **Not be part of a set.** These are assets that are interdependent on each other, marketed as a set or designed and intended for use together. Examples include a bed ensemble where the total for the base and mattress is over $300, or a dining table and chairs where the combined total of the parts is over $300.
- **Not be substantially identical.** The make, model, colour, shape, function, brand, design, texture and composition of each asset is considered under this test. To be substantially identical, assets must have been purchased in the same financial year. Examples include five identical bar stools that are $100 each.
- **Not be for business use.** Residential property assets often meet this test, but not always. For example, if lawn maintenance is managed by the property owner and the lawn mower is kept at the investment property but is also used for the owner's small landscaping business, then the percentage the mower was used for business income would need to be apportioned.

Low-value pooling, low-value vs low-cost

Assets that cost, or have a value, less than $1,000 can be placed in a low-value pool. This pool unlocks depreciation sooner, as it utilises accelerated rates.

The Australian Taxation Office (ATO) outlines a clear difference between low-cost assets and low-value assets:

- Low-cost assets are depreciable assets with an opening value of less than $1,000 in the year of acquisition.
- Low-value assets have depreciated over one or more years and now have a written down value of less than $1,000. This means the asset's value was more than $1,000 in the year of acquisition but the residual value of depreciation is now less than $1,000.

Assets contained within the pool can be claimed at a rate of 18.75 per cent in the year of purchase regardless of the length of time that the property has been owned and rented. After the first year, the remaining balance of the item can be claimed at a rate of 37.5 per cent per year.

Assets placed in the low value pool must be depreciated using the diminishing value method. It's important to note that once an asset has been allocated to the pool, it must remain there.

Example:

Jenny purchased carpet for her investment property in January 2017. At the time of purchase, the opening value of the carpet was $1,100 but using the diminishing value rate, by July 2017, the carpet's residual value was $990. After six months of depreciation, the carpet had a written down value of less than $1,000 and was classified as a low-value asset.

The ATO states that once you choose to allocate a low-cost asset to a low-value pool, you must then add all other low-cost assets you acquire within that income year and future income years to the low-value pool. However, with low-value assets, you can decide whether or not you wish to add individual low-value assets to the pool.

Did you know?

Depreciation legislation was amended in 2017. The change meant that depreciation could not be claimed for second-hand plant and equipment assets.

Residential owners can still claim for any new plant and equipment assets added to the property such as an oven or dishwasher, as well as the full capital works deductions which make up 85-90 per cent of the total claim.

CASE STUDY

Michael purchased a brand-new house for **$600,000.** His property is rented for **$545** a week, or **$28,340** per annum.

First year expenses for the property including interest rates, management fees and maintenance total **$39,067**. There are also **$11,200** in depreciation deductions.

Michael turns his cash flow position from -$130 to -$50 by claiming depreciation. He saves **$4,160** in the first year alone.

A new house purchased for $600,000	Without depreciation claim	With depreciation claim
Annual rental income	$28,340	$28,340
Annual property expenses	$39,067	$39,067
Pre-tax cash flow (income less expenses)	-$10,727	-$10,727
Depreciation claim	$0	$11,200
Total taxation loss	**-$10,727**	**-$21,927**
Tax refund (tax loss x tax rate of 37%)	$3,969	$8,113
Annual costs (pre-tax cash flow + tax refund)	-$6,758	-$2,614
Weekly cost	-$130	-$50
Difference of $80 per week		

Case studies and figures are based upon tax depreciation schedules completed by New Vision Real Estate and do not represent any particular person or investment property scenario. The tax depreciation deductions in this case study have been calculated based on the diminishing value method of depreciation and are based upon a first full year of ownership. A marginal tax rate of 37% has been used for this example.

Cash flow **BEFORE** depreciation

Cash flow **AFTER** depreciation

CASE STUDY

Janice purchased a new three-bedroom townhouse for **$780,000.** Her property is rented for **$550** a week or **$28,600** per annum.

Expenses for the property including interest, management fees and maintenance total **$32,000** for the year.

New Vision Real Estate finds **$18,400** in depreciation deductions. By claiming depreciation, Janice saves **$6,812** in the first year alone.

A new house purchased for $780,000	Without depreciation claim	With depreciation claim
Annual rental income	$28,600	$28,600
Annual property expenses	$32,000	$32,000
Pre-tax cash flow (income less expenses)	-$3,400	-$3,400
Depreciation claim	$0	$18,400
Total taxation loss	**-$3,400**	**-$21,800**
Tax refund (tax loss x tax rate of 37%)	$1,258	$8,066
Annual costs (pre-tax cash flow + tax refund)	-$2,142	$4,666
Weekly cost	-$41	$90
Difference of $131 per week		

Case studies and figures are based upon tax depreciation schedules completed by New Vision Real Estate and do not represent any particular person or investment property scenario. The tax depreciation deductions in this case study have been calculated based on the diminishing value method of depreciation and are based upon a first full year of ownership.

Cash flow **BEFORE** depreciation

Cash flow **AFTER** depreciation

WHAT IS A **TAX DEPRECIATION** SCHEDULE

What is a tax depreciation schedule?

A tax depreciation schedule is a report which outlines all the available investment property depreciation deductions you can claim at tax time.

A depreciation schedule will project capital works deductions and plant and equipment depreciation for the life of the property. This depreciation can be claimed in your tax return each financial year to help you save thousands.

Benefits of a tax depreciation schedule

Most properties, new and old, have depreciation available.

Your schedule contains everything you need to claim depreciation on your investment property. The deductions are broken down to show how much you can claim each financial year. This document is very comprehensive and is often over 30 pages long, but your accountant will know exactly what to look for!

Your schedule only needs to be completed once and lasts a lifetime. You only need to obtain an updated schedule if you add or remove assets or complete a renovation. Even the cost of preparing your schedule is tax deductible.

What is in a schedule?

A comprehensive tax depreciation schedule will contain:

- a detailed 40-year forecast illustrating all depreciable items
- both prime cost and diminishing value methods of depreciation to help you decide which method is best for you
- the effective life and depreciation rate for all plant and equipment (division 40) assets
- low value and small business entity pools and instant asset write-off
- a glossary of terms to help you understand the terminology used throughout the schedule.

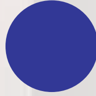
The easiest way to find out how much depreciation you can start claiming is to get an obligation-free estimate.

Request an Estimate

Every residential property investor should have a tax depreciation schedule to substantiate and maximise deductions. It could make a huge difference to your cash flow, giving you back thousands of dollars every year, for up to 40 years.

Example of typical deductions found in an investment property

Plant and equipment deductions


Capital works deductions

Ceiling
$168

Rangehood
$184

Stove
$377

Flooring
$442

Depreciation may seem like a complicated area of taxation. Here are the answers to commonly asked depreciation questions.

DEPRECIATION QUESTIONS ANSWERED

How much depreciation can I claim?

Every property is different, but most properties, new and old, will have some depreciation available.

The property's age, construction type, its size, quality of fixtures and your settlement date affect how much depreciation is available.

To find out how much you can claim, contact New Vision Real Estate for an obligation-free estimate.

When can I start claiming?

You can start claiming depreciation as soon as your property is available to produce income.

If you purchased your investment property part-way through the financial year, for example in January, you could claim deductions from that point in time. Your specialist quantity surveyor can use pro-rata calculations for your first year of ownership so that you don't miss out. If you haven't been claiming depreciation, a tax depreciation schedule can amend previous tax returns and help you claim back missed dollars.

What is a quantity surveyor?

A quantity surveyor is a tertiary qualified professional who specialises in building measurement and estimates the value of construction costs. A specialist quantity surveyor is one of the few professionals recognised by the ATO as having the skills and qualifications to estimate construction costs for depreciation purposes.

What does a specialist quantity surveyor do?

A specialist quantity surveyor documents each asset in a property and calculates the depreciable value to ensure that the investor maximises their deductions. This includes measuring rooms using a laser measurer, recording an asset's brand or model number and photographing improvements at the property. This information is used to prepare a tax depreciation schedule which outlines the depreciation deductions that can be claimed every year at tax time.

Doesn't my accountant do that?

We work together with your accountant to make sure you are claiming the maximum deductions from your investment property. An accountant cannot estimate construction costs for depreciation purposes which is why they will often refer their clients to New Vision Real Estate to obtain a tax depreciation schedule. The schedule enables them to include accurate deductions for the property in your tax return.

What is a site inspection and why do I need one?

A site inspection plays a vital role in the depreciation process, particularly when it comes to supporting your claim in the event of an ATO audit. New Vision Real Estate has a well-established and long-lasting relationship with the ATO, and they often require evidence to justify the deductions. It is important that we can directly give feedback based upon the inspection that we completed, regardless of how long ago that was.

Our site inspections ensure accuracy and usually take less than an hour. Our specialist site inspector will measure the building and floor coverings, note down the construction method, workmanship, materials used and condition of the property. We will look for any evidence of works completed, both recently and anything that might have taken place in the last 30-40 years. The current owner of an income-producing property can often claim deductions for work that was completed by previous owners. We document everything that we can, making notes and taking photographic records.

Can I claim depreciation on a second-hand property?

In November 2017, the Federal Government changed the way investors can claim depreciation for second-hand plant and equipment assets. Specifically, the 2017 legislation means that previously used plant and equipment assets found in second-hand or previously occupied residential investment properties can no longer be claimed.

But depreciation on second-hand properties is still available for all eligible capital works (the structure), which make up 85-90 per cent of depreciation and on all new plant and equipment assets you purchase for the property.

Can I claim depreciation while my property is vacant?

The simple answer is yes. As long as your property is classed as 'genuinely available for rent' depreciation can be claimed.

ABOUT **NEW VISION** REAL ESTATE

New Vision Real Estate specialise in bold, innovative, punchy marketing of the property to attract premium buyers and tenants. We use the most advanced systems to ensure we are at the forefront of technology and marketing to ensure maximum exposure of our listing and in turn achieving record prices and lower days on market.

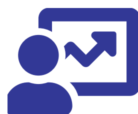
New Vision Real Estate was founded on a passion for people and property. Founder and Director, **Chris Brown**, has earned his stripes in the industry by being down-to-earth, personable and totally committed to being the best at what he does.

Superior customer service leads to a good reputation for which the company is renowned, but this has not come about by accident. A good reputation is earned. **New Vision Real Estate** has the systems in place to ensure that delivery of excellent service is consistent, monitored and revised in line with feedback.

New Vision Real Estate directors and staff believe that superior customer service underpins everything else they do. It's of little value having exceptional marketing strategies to draw people to the business if the customer experience does not match the rhetoric.

Request a Quote

Discover the New Vision Real Estate Difference



Great deductions
On average we find almost $9,000 in first full financial year deductions.

Split schedules
We provide split depreciation schedules on co-owned properties to maximise deductions.

New Vision Real Estate Guarantee
We will find double our fee in deductions in the first financial year or we won't charge for our services.

Site inspections
e use our own staff to conduct inspections Australia wide rather than outsourcing.

Lasts a lifetime
Your schedule lasts a lifetime and the one-off fee is 100 per cent tax deductible.

Free New Vision RE account
View and update your schedule online, track property expenses, research properties and more.

How do I claim depreciation?

1. Get a quote

Find out how much your depreciation schedule will cost by requesting a quote. We can also provide an obligation-free estimate of the likely deductions.

2. Provide details

We'll collect property details then contact your property manager or tenant to arrange access for one of our specialist staff to complete a property inspection.

3. Claim depreciation

Your schedule will be ready within seven days of receiving all information. We can even forward it to your accountant to save you time.

Request a Quote

KEY **TERMS**

Capital gains tax (CGT):	This is the tax paid on the profit made from selling an investment property.
Division 40:	Plant and equipment assets like carpets, blinds and lights are depreciated under Division 40.
Division 43:	Capital works deductions or building write-off are depreciated under Division 43.

Effective life:	Every plant and equipment asset has a dedicated effective life that is set by the Australian Taxation Office.
Joint tenants:	This is where each owner holds equal shares in the property, like a 50:50 split.
Low-value pool:	Both low-value and low-cost assets can be depreciated in a low-value pool. Once in the pool, the asset depreciates at an accelerated rate of 18.75 per cent in the first year and 37.5 per cent in each following year.
Low-value and low-cost assets:	These assets can be depreciated in a low-value pool. An asset is low-cost when its opening value, or how much it costs when you purchase it, is less than $1,000. A low-value asset is one that has a remaining depreciable value of $1,000.
Maintenance:	This is work completed to prevent deterioration to a property, such as oiling a deck. Maintenance costs are treated the same as repairs and can be claimed straight back in the same financial year.
Pro-rata calculation:	This calculation is used to calculate a portion of the financial year claim when your property is only used as an investment for part of the financial year. A pro-rata calculation can also be used when only part of the property produces income, such as renting out a room.
Repairs:	This is work to fix damage or deterioration of a property. For example, replacing a section of a damaged fence or part of a rusted gutter. Repair costs can be claimed straight back in the financial year.
Scrapping:	When you remove assets during a renovation, they are 'scrapped'. The scrapping process allows you to claim any undeducted depreciable value on the removed assets.
Split schedule:	This is used when an investment property is owned by more than one person. A split schedule often results in higher deductions earlier for each owner.
Tenants in common:	This is where each owner of the property holds unequal ownership, such as a 70:30 split.