

Your questions answered

Our panel of experts answers more investment questions from API readers.

From rental to home

Q Can you convert an investment property into your primary residence without selling your primary residence? So, if you have an investment property you want to move into, can you make your initial property a rental and the secondary property your residence? The first property is paid off, but we have a loan on the investment one. We've had conflicting answers.

A You can choose to cover either property with your main residence exemption but only from the time you first lived there and only for up to six years after you move out of it. The trouble you have is, unless the property is income producing, the interest on the money borrowed to buy it won't be tax deductible. Moving into the rental will leave you with a large non-deductible interest bill. To shift some of the loan from the original investment property to your original home either you or your spouse could borrow to buy the other one out. The selling spouse could then use the sale proceeds to reduce the debt on the house you're living in. Don't do this without an Australian Tax Office ruling that it won't apply Part IVA (i.e. scheme with the dominant purpose of a tax benefit) to the arrangement. In your ruling request quote Interpretative Decision 2001/79 and make sure you have a valid reason for doing this other than the tax benefit. You'll also need to consider whether the stamp duty costs make it worth your while but there should be no capital gains tax consequences if it has been your main residence up to that date. *Julia Hartman*

Selling up

Q I am a 29-year-old on a good income. I have two investment properties and two blocks of land which I will be selling this year to fund my new residence. Say, for example, I make a capital gain of \$300,000 and capital gains tax (CGT) works out at, say, \$75,000 of this. Is there any way of avoiding this CGT payment, i.e. investing the amount which I'd pay in CGT (\$75,000) back into my super (preferred option) or reinvesting it in commercial real estate?

A If you make a capital gain, the assets were in a trust or individual's name and held for longer than 12 months then you'll receive a 50 per cent discount on the capital gain before paying tax so you'll pay tax on \$150,000. This is the amount you'd need to tax plan for. If you're determined to pay as little tax as possible then you can put up to \$50,000 per person into superannuation each year. For those over 50 this amount is \$100,000. It depends on whether you're employed or self-employed in how you make these super contributions but it would be a lot of cash required to extinguish the tax debt established by the capital gain. Agribusiness investments are another way of extinguishing the tax to be paid on the capital gain of \$150,000. These investments are very tax effective but they're being scaled down considerably

from July 1, 2008. You'd need advice from a financial planner to invest in this type of product. If you use the funds to buy a commercial property you'll pay the full capital gains tax on the \$150,000. I'd recommend you take a more balanced approach and understand that if you have made \$300,000 then you have done well and can make some decisions to reduce the tax but you'll still pay a fair bit for such an excellent result. *Pat Mannix*

Build and sell

Q If I build a duplex on a site and then sell off one side of the duplex straight away, what capital gains tax am I up for? Example: bought land for \$120,000, build of \$300,000, sell one side for \$350,000. What is the gain taxed on if I've made no gain on paper?

A This would most likely be classed as an isolated profit transaction so you'd need to pay income tax on the sale of one side of the duplex. To calculate this you take the full cost of the land and buildings, divide that by two which equals \$210,000. The sale price is \$350,000 so you've made

a profit of \$140,000 and income tax would be paid on this amount at the rate of the structure that the duplex was developed in.

Pat Mannix

Value adding

Q I've just settled on a two-bedroom strata unit with a lock-up garage with internal access in Unley Park, SA, within 8 km to CBD. My question is, is it better to leave it as is or convert the garage to a third bedroom if I can get strata/council approval, leaving only street parking? Factoring in, of course, the cost of conversion and what it will do to cash flow and value to the property.

A The best way to find out is to become a tenant for a day and see what rent three-bedders with on-street car parking get compared to two-bedders with a garage. In a tight rental market you'll probably find the three-bedder with the higher rent will win out, especially if you're close to transport. But maybe the 'black plastic' solution might work for you in the interim. I know a rental house with garage with internal access that the tenants constantly used as a bedroom or office or rumpus, even to the extent that they laid carpet on the floor. When that tenant left, a following tenant wanted to put their car in the garage so the owner laid heavy duty black plastic over the carpet and taped it down. The following tenant preferred the indoor space and was happy to park outside so off came the black plastic. The owner eventually overcame the problem by erecting a professionally designed shade structure outside and over the driveway which acted as a double carport. The cars are always now parked outside under cover and the tenants enjoy more internal space and don't bother with the plastic any more. The cost was only a couple of thousand dollars. Win-win. I've seen those shade structures in use at various unit complexes so check with your body corporate and council.

Geoff Doidge

Not allowed into my property

Q I recently flew to Brisbane for work and thought I'd take the opportunity to look inside my rental property. I duly phoned my property manager and informed her of my intentions, only to be told I couldn't enter. How can this be when I own the property?

A I understand your concerns; however there are certain timeframes (different in most states) you must give a tenant before entering to inspect a property. In Queensland, for example, legislation says you need to give a tenant seven days' notice in writing to enter a dwelling and then add on two days for postage. So because your property is located in Brisbane, you'd need to tell your agent of your impending date at least 10 days prior to your arrival. Just another reminder: legislation also deems that you're not allowed into your property to inspect more than four times per year. The reason is to ensure the "quiet peace and enjoyment" of the tenant. Notification periods are different for each state so I suggest you check with your managing agent.

Karen Herbert

DIY management

Q I have an investment property that I, with my defacto partner, self manage (the property is in my name only). His taxable income is less than \$6000 annually. Can I legally pay him to take over management of the property and, if so, will his wage be a tax-deductible expense for me?

A Yes, you can pay your partner an ongoing management fee to look after your property and claim that fee as a tax-deductible expense. The management fee you pay your partner must reflect a reasonable market rate. I suggest you contact a property manager in your area to determine the going market rate. In addition, any fee paid to your partner must be declared in his tax return and taxed at his marginal rate of tax.

Mark Armstrong

Home or investment property?

Q I'm 30 and considering investing in either Wagga Wagga, NSW or the Frankston area in Melbourne. I'm currently renting in Wagga as I've recently moved here from Melbourne. Would you suggest I buy my own home first and take advantage of the First Home Owner Grant by living in this residence for 12 months then use the equity in this place to buy an

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investment property, or should I buy a property purely as an investment first?

A The First Home Owners Grant Scheme states as a requirement that “you and your spouse/partner must not have occupied for a continuous period of at least six months a residential property in which either of you acquired a relevant interest on or after July 1, 2000 in any state or territory of Australia”. This infers that in fact you can own a property and as long as you buy a property after July 1, 2000 and don’t live in it longer than six months (therefore you rent it to someone else) you can still subsequently claim the grant for a property which you do buy with the intention of owner-occupying at a later date. For you this means that if you actually prefer to buy a property as an investment, you can do so and still claim your grant on a later property if you wish. If, on the other hand, you wish to claim the grant for this property, you must take up residence within 12 months and then reside for a continuous period of six months.

Technically if you wished you could rent the property out for 11 months and 29 days as long as you then moved into it the day after and stayed for six months. At any time you can then use equity to buy further property, and this can occur as soon as the equity is available. There are no restrictions against leveraging a property purchased with a grant into more property, and so your ability to do this will depend entirely on how quickly it grows in value.

Extensive research to determine which of the areas you are considering shows the strongest intrinsic growth drivers will be the key to you acquiring additional property sooner. *Margaret Lomas*

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