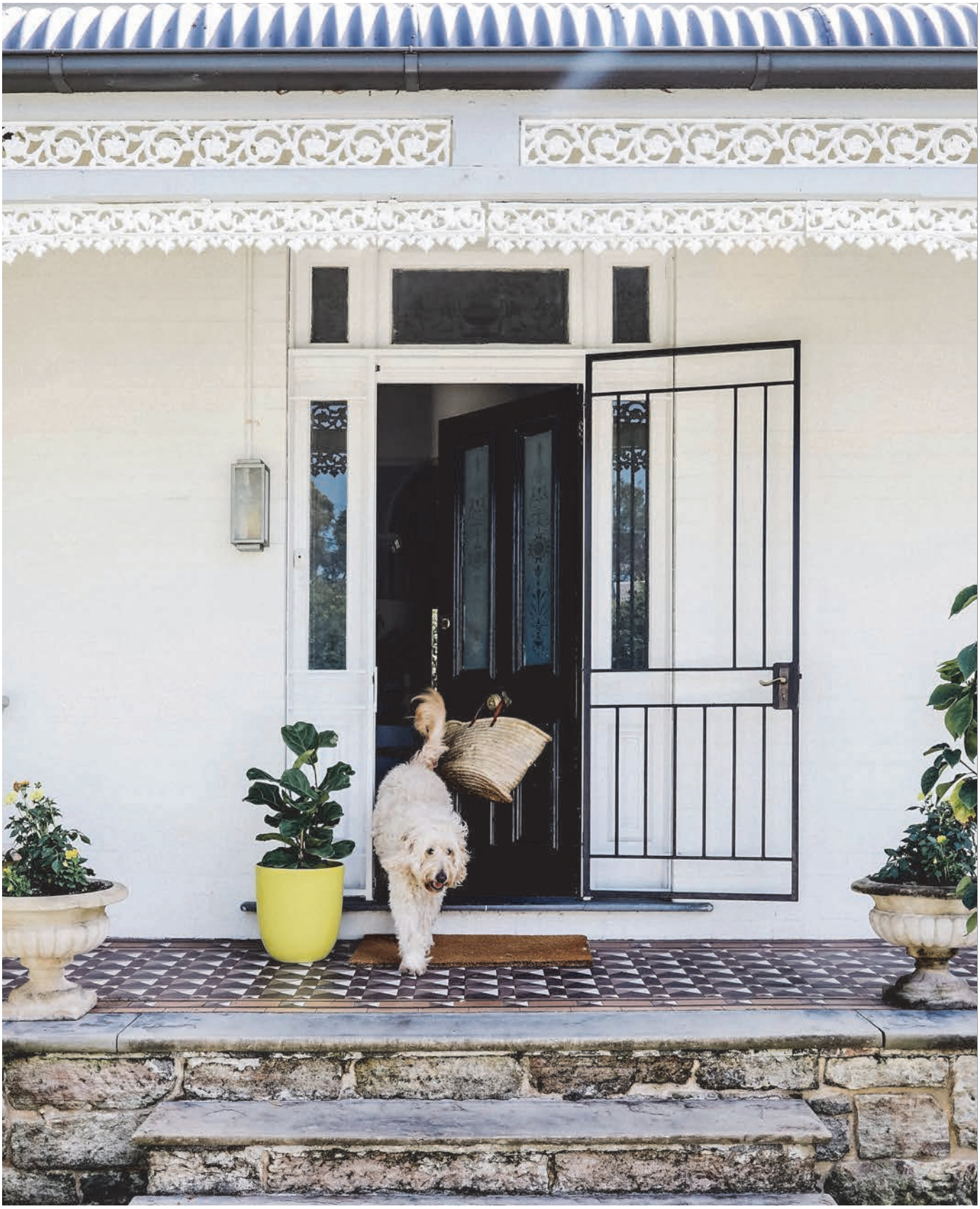
Investing?

Investment Guide



A Guide For Investing

RayWhite

Whether you own one investment property or many, there are numerous financial factors that can affect the return on your investment and its long-term viability.

It is important to understand how these factors may have an impact, both now and in the future, as many investors aren't aware of where improvements in their return can be made.

This guide has been produced to help landlords make better property investment decisions, and highlight where professional advice should be sought.

Kind Regards

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“What's the best structure to hold my property portfolio in?”

Picking the best ownership structure for your investment property is something that's often overlooked by prospective landlords, and for good reason.

It’s an area that is generally poorly understood without seeking professional advice. There are a number of benefits to picking a structure outside the common sole proprietorship/partnership model, e.g. owning it in your own name.

The following outlines the three main types of property ownership in Australia. Each provides a different mix of limited liability, compliance costs and tax efficiency. Your own circumstances will be unique compared to another investor so the following information is intended as a guide only.

We recommend that you seek appropriate professional advice before settling on any particular ownership structure for your rental property.

Sole proprietorship/ partnership

This is the most common form of property ownership in Australia. Your investment property is owned personally, with no limitation on personal liability. An advantage of sole proprietorship is that there are minimal compliance costs associated with this popular structure.

Trust

Commonly known as a ‘Family Trust’, there are two main advantages to having your rental property owned by a trust.

Asset protection is the most obvious advantage as the beneficiaries of the trust don’t actually own the assets held in trust. The trustees do so on behalf of the beneficiaries.

We recommend you seek professional advice from your lawyer about the finer points of trust law and asset protection if this is your intention.

From a taxation point of view, a trust provides you with the tax benefits of income splitting. You can send any taxable trust income to beneficiaries (anyone over 18, as you’re limited to a nominal amount per year for those aged 18 or under), who will then pay tax on this at their marginal tax rate. Which may provide flexibility and potential tax savings.

Compliance costs can be high for trusts and if income splitting is the reason for putting your investment(s) into a trust, do make sure that your tax savings outweigh any professional fees incurred during the year.

Company

An investment property under this structure enjoys the benefits of limited liability because it is a completely separate and distinct legal entity from its owners, but there are limitations to the tax efficiencies that can be applied.

Companies will attract higher compliance costs and there are some possible complications with capital gains when selling any property to related parties. This fact needs to be considered if you are planning on holding multiple rental properties in the same company.

One of the tax benefits that companies enjoy is the automatic deductibility of interest, regardless of the intention of the loan. This is in contrast with the other business structures outlined here, where interest is only deductible on loans that were originally taken out on the property. Again, there are complications around taking out loans and drawing cash out of the company, and it is a very different situation when compared to the sole proprietor/partnership model.

We recommend seeking the professional advice of a chartered accountant about whether a company structure is right for your investment.

Comparable Returns - Property vs Shares

Residential rental property has always been a staple of Australian real estate in terms of creating wealth, or 'getting ahead'. It's easy to understand, tangible and, when leveraged, can provide significant capital gains.

It's important to understand the role that leverage plays when investing in residential property. Residential real estate within Australia has provided great capital and revenue returns.

While on the face of it there doesn't appear a great advantage to owning property over investing in the stock market, leveraging can change this to the investor's advantage. Imagine this example: You have a house deposit of $100,000 and you buy a nice property for $500,000. The balance of $400,000 is lent to you by the bank at an attractive interest rate.

In five years' time you decide to sell the property and achieve a sale price of $600,000. What has happened to your initial investment? It's doubled. Leveraging has allowed you to make a 100% capital return on your investment at a rate of 14 - 15% per year. Had the property been positively geared, this return would have been even greater.

By understanding leverage you can pinpoint the benefits of property ownership and why it can be such a strong investment choice, as well as providing a better return for you than shares.

Another point to note is that while shares can be used as security for a loan, just as property can, banks are far less likely to consider shares as good security for lending. For this reason it isn't as common that loans are issued for shares, and certainly not at the favorable interest rates that are available for property investors.

We recommend you seek advice from relevant professionals before making any investment decisions.

Tips for renting your property out

THE FOLLOWING 5 TIPS ARE THE MOST COMMON ONES WE PROVIDE TO CLIENTS WHO ARE CONSIDER LEASING THEIR PROPERTY OUT.

Spring clean

Do a thorough clean from the inside, out including walls, windows, skirting boards and every nook and cranny.

De-clutter

Your tenant needs to imagine living in the property. Ridding clutter visibly increases the room size and better showcases the space.

Faultless

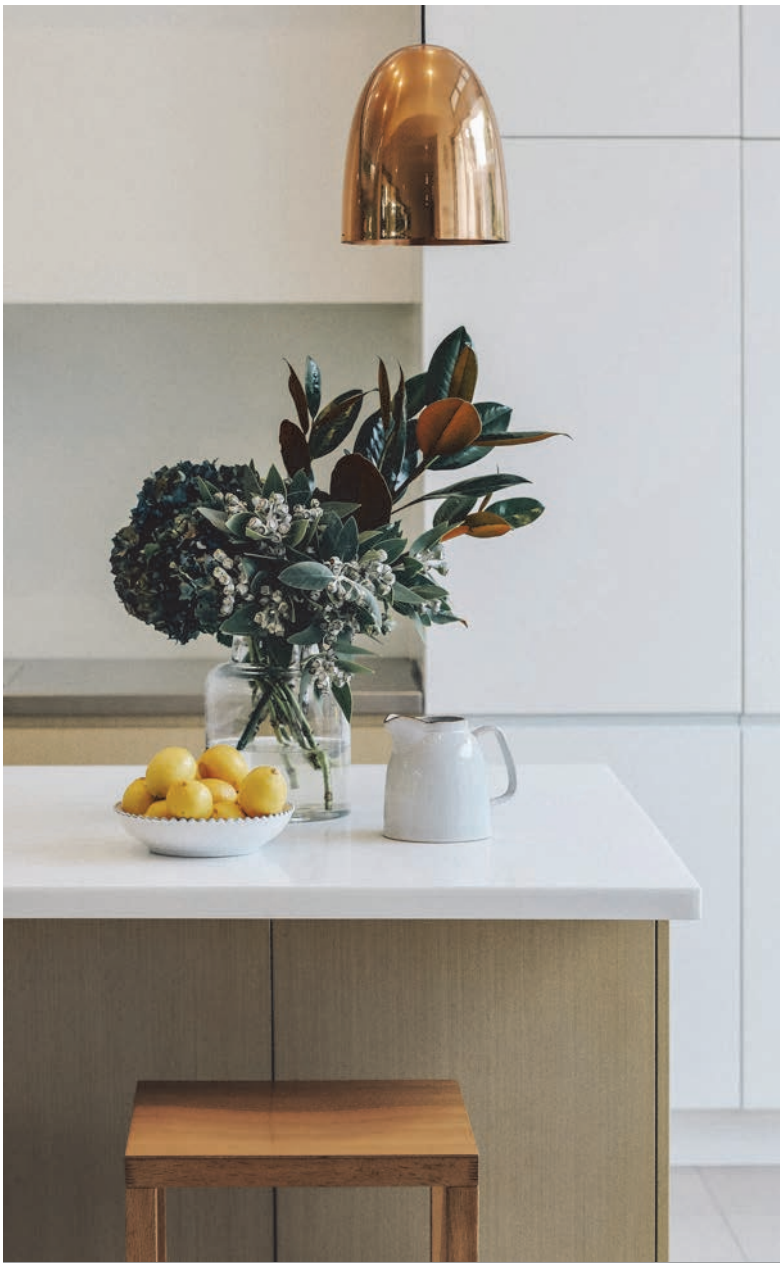
Tenants notice everything. Fix anything that doesn't work, including doors, windows, light bulbs and taps.

Marketing

A super important but almost always overlooked component. A good manager will present a campaign that will ensure your property gains the right exposure and engagement.

Neutral environment

Decoration tastes are highly personal and we recommend taking a safe, neutral approach any improvements and painting undertaken at the property.



Insurances - Building & Landlord

It's vital to ensure you limit any financial loss and this is why it's important to ensure that you hold the necessary insurance cover to protect not only your asset but also against tenant-related risks.

This being said there are two main types of insurance to consider when owning an investment property

Building Insurance

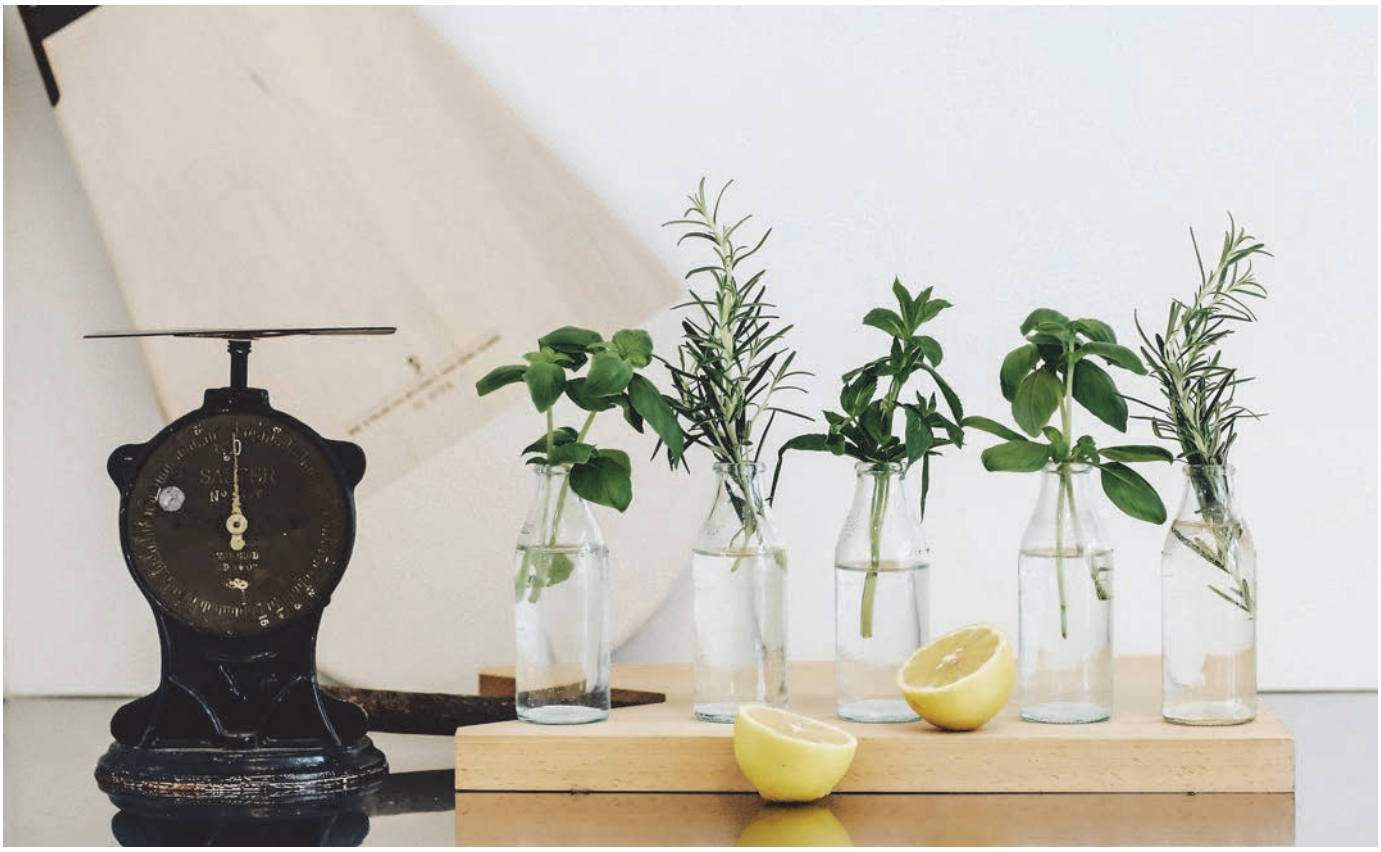
Depending on the cover taken out, Building Insurance can protect you against the costs of repairing damage or in the worst case replacement of your home provided that the damage is caused by an insured event such as storms, fire and floods. Generally speaking permanent fixtures and structures like fences, sheds, garages and solar panels are covered but it doesn't cover the contents inside your home such as personal belongings

Landlord Insurance

On the other hand, Landlord Insurance is used to cover you for tenant-related losses, over and above the bond, rather than property-specific losses which are covered by a building policy.

Items like loss of rent due to a tenant defaulting, breaking their lease or being evicted, damage caused to your contents by tenants, like a drink spilling on carpets.

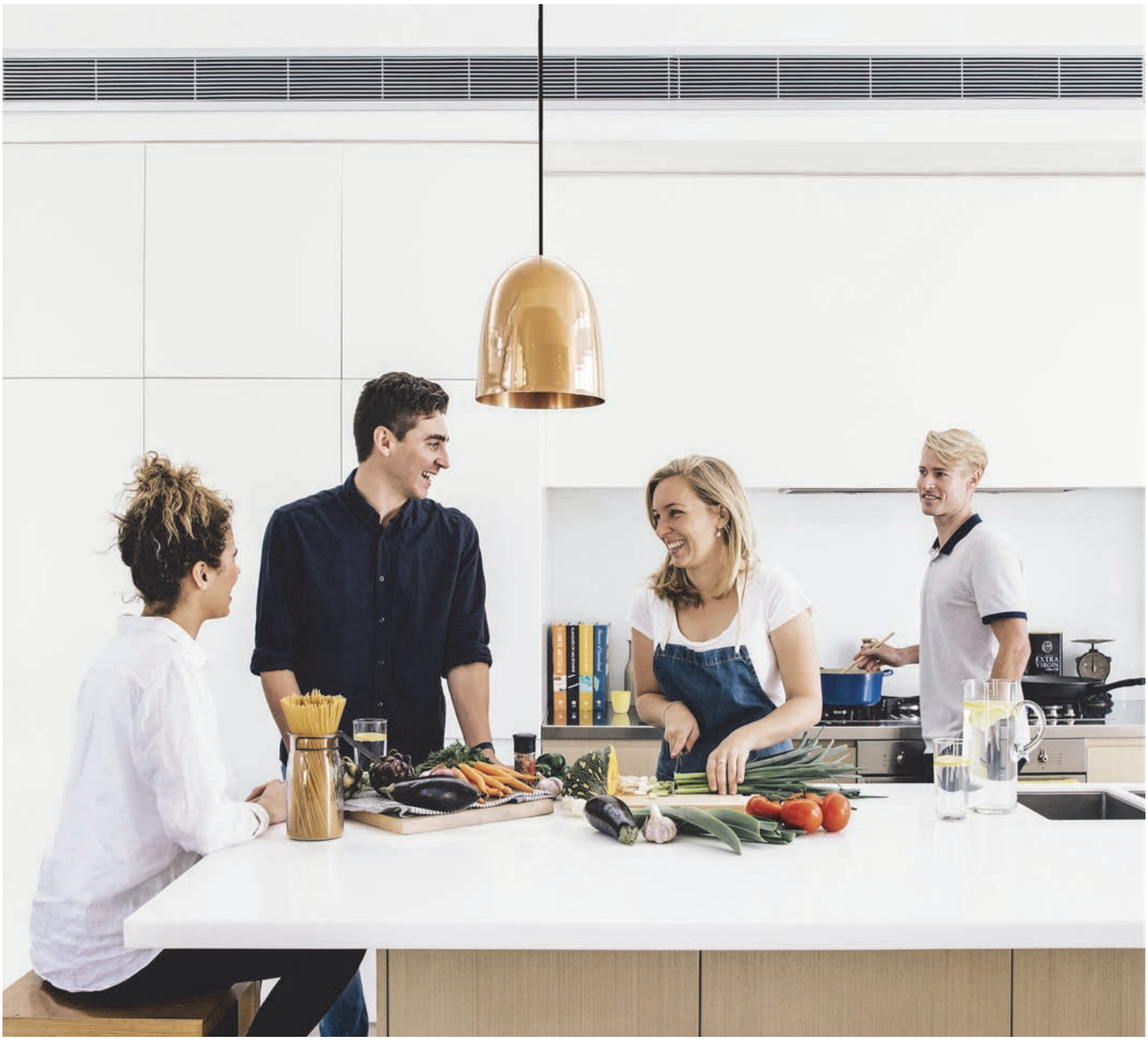
We recommending making sure you read the Product Disclosure Statement (PDS) of any policy you take out and ensure you also understand any excesses and premiums you may be required to pay.



Claimable Expenses

Many landlords aren't aware of the claims that can be made on property management fees and other expenses associated with owning an investment property.

To maximise the full potential of your investment it is important to properly understand what can and can't be claimed.



Expenses you can claim

Insurance & rates

You can claim back the full cost of insuring your rental property and the council rates associated with the ownership of the property.

Interest

You can claim the interest charged on money you've borrowed to buy your rental property. However, if you borrowed part of the money for another purpose, or topped up the mortgage for another purpose, e.g. to consolidate debt or to buy the house you live in, you can only claim the interest that relates directly to the rental property.

Fees & commission

You can claim 100% of the fees or commission paid to property managers who collect the rent, maintain your rental, or find tenants for you. Accountant fees You can claim the fees charged by an accountant for:

- Your accounts to be managed
- Tax returns to be prepared
- Advice

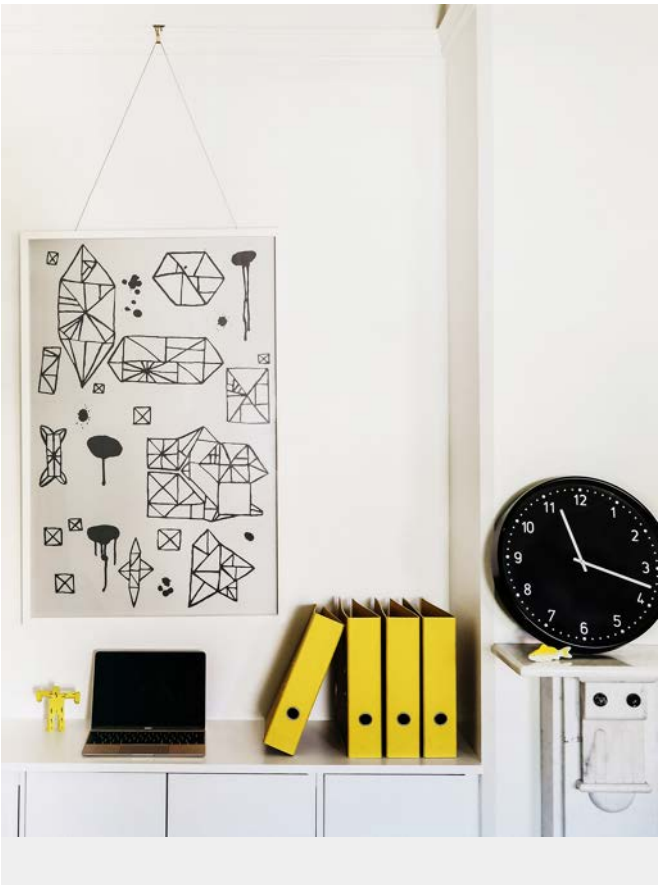
Legal fees

If you're in the business of providing residential rental accommodation, you can also claim legal fees incurred when selling a rental property from your portfolio.

Note: We advise speaking to your chartered accountant to ensure you meet the criteria to be classed as being 'in the business'.

Repairs & maintenance

You can claim back the costs for any repairs to the property or general maintenance. However, if you're doing the work yourself you can only claim for materials, not your own time.



Expenses you can claim

Repairs & maintenance cont.

If the work is an improvement to the property rather than a repair, then you can't claim that cost as an expense.

The distinction between repairs and improvements can be tricky. If you're unsure whether work done on your property is repairs or maintenance we suggest you talk to a chartered accountant.

Other

Other costs you may be able to claim include:

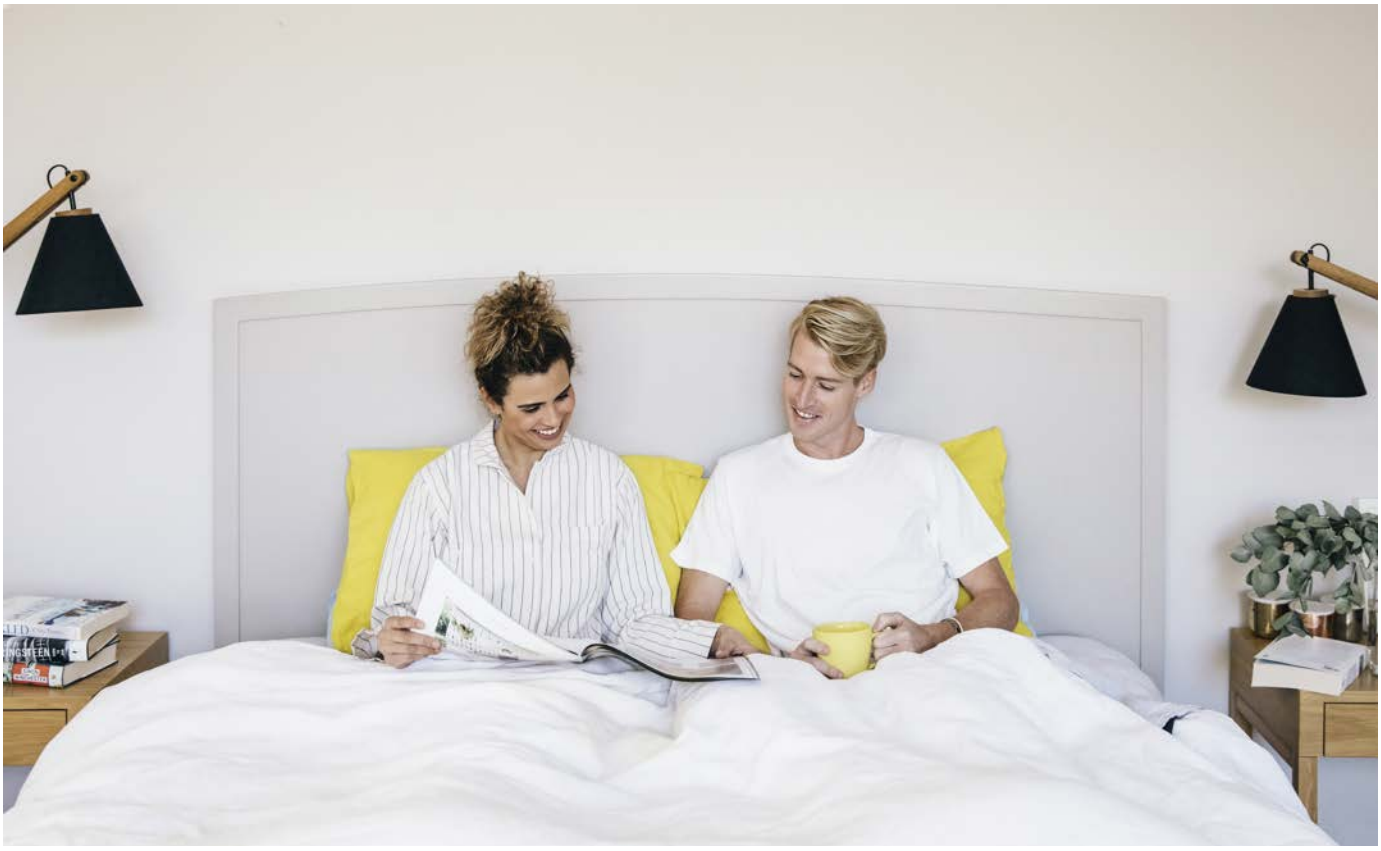
- Body corporate fees
- Valuation fees
- Water rates (only if paid by the landlord)
- Gifts for tenants
- Travel associated with managing your property

You can't claim deductions for capital expenses, private expenses, or expenses that do not relate directly to your rental property.

Depreciation

Depreciation is an allowance you can claim to cover the costs of wear and tear and general ageing of furniture and fittings you've bought for your rental property.

You cannot claim depreciation on the property's land or buildings. This is a complex area and for more information, we suggest you speak with a chartered accountant.



“What Are Expenses You Can't Claim?”

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You can’t claim deductions for capital expenses, private expenses, or expenses that do not relate directly to your rental property.

Capital expenses are the costs of buying a capital asset or increasing its value: for example, the cost of buying the property and making improvements.

Private expenses are things you buy or pay for that are for your own benefit rather than to generate rental income.

Expenses you can’t deduct from your rental income in your tax return:

- The purchase price of a rental property
- Any capital portion of mortgage repayments
- Interest on money you borrow for any purpose other than financing a rental property
- Costs associated with any additions or improvements to the property
- Costs associated with repairing or replacing any damaged part of the property if that work increases the property’s value

Goods & Services Tax (GST)

GST is not charged on residential rent so this means you don’t include rental income in your GST returns (if applicable).

Repairs or upgrades to a substandard investment property

You can’t claim expenses incurred to bring a rental property up to the condition necessary before it can be rented e.g. compliance related healthy homes items that don’t exist at the property already, such as an underfloor moisture barrier.

Initial costs

Any initial costs associated with finding an appropriate rental property, including the cost of valuing or checking the condition of a property before purchasing it.

Other exceptions

If the property isn’t rented for the full year; isn’t occupied by tenants; isn’t available to be rented out at any stage during the year; or is only available for rent for part of the year, then you can’t claim the full year’s ongoing costs such as rates, insurance and interest.

As always, we recommend speaking with your accountant for your financial advice.

WHO WE ARE

Local experts, working for you.

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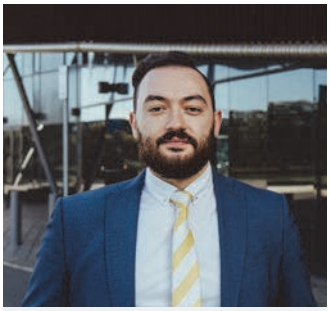

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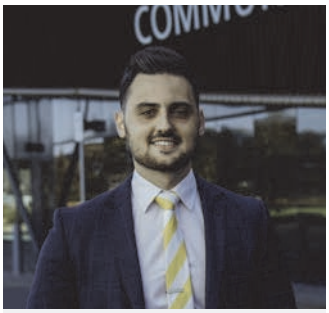

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