ASK THE EXPERT

Mixed Loan Interest Claim

smatsgroup since 1995

Q *I am going to buy a house in London using some of my loan in Australia, can I claim the interest against my Australian tax?*

A The Australian property market has fared better than most through the Global Financial Crisis and lending has remained available. This combined with a strong Australian dollar means that many people are considering taking the equity out to assist with the purchase of property out of Australia either as a residence or investment.

There are no restrictions in Australia to doing this provided you can demonstrate to the Bank that you can afford to additional borrowing.

From an Australian tax perspective the interest on the new loan will not be allowed as a tax deduction while you are living abroad because of the fact that it is not a taxable activity in Australia for non resident taxpayers (which includes genuine Expatriates).

This is true regardless of whether you live in the property or rent it out.

When you return to Australia this situation may change.

For anyone living in Australia they are taxed on their worldwide income and capital gains. When something is taxable in Australia, then all costs incurred in making that income become tax deductable.

Hence if you had used the loan originally to purchase the overseas property and then rented the property out on your return to Australia, the loan now becomes fully deductable against your overseas rental income.

This could make a big difference to your tax position on return and affect your strategy on debt reduction.

During your time abroad, you should consider how long you intend to have the property and if you would like to keep it on your return to Australia.

If so, then keeping the debt at the highest level is the prudent course of action, especially if you intend to rent it out once you return to Australia. This will maximise the loan value and tax effectiveness on return to Australia and preserve your cash for extinguishing other private loans or to acquire your Australian residence with the minimum of debt.

If you are definitely going to sell the property prior to or on return to Australia and living in the property, then debt reduction may be the most appropriate option, especially if it is your private home, to keep the holding costs to a minimum and build up additional equity.

The hard part is being sure which option is most likely as circumstances can change quickly.

As a result, usually the low or no debt reduction option is best to maintain until the time comes to relocate to Australia and you can weigh up the best choice given the prevailing conditions at that point in time.

If you do decide to keep the property indefinitely on your return, which is often the case, then the borrowing will be a welcome situation and help to keep your Australian taxation to a minimum.

Steve Douglas is the co-founder and Managing Director of Australasian Taxation Services (ATS), established in Singapore in 1995. ATS provides specialist taxation services to people of any nationality investing in Australian property, as well as Australian expatriates living overseas. Areas of specialisation include the Australian taxation aspects of property investment, as well as expatriate and migration planning.