ASK THE EXPERT

Negative Gearing in the Spotlight

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Q *There have been increasing conversation in Australia about possible changes to the tax benefits around "Negative Gearing" for property investors, what does it all mean?*

A Australians have always had a good regard for property investment which has been well founded due to the long term reliability of the Australian market.

Negative Gearing is the practice where you borrow to acquire an investment asset, and the interest cost is greater than the income derived from the asset creating a loss. Obviously a loss is not a desired outcome when investing, so the main consideration of negative gearing is the belief that the future capital gain in the asset will be greater than the holding cost and result in an overall profit over time.

In Australia, this loss is allowed as a full income tax deduction each year, which makes it attractive (and legal) to undertake negative gearing as a sensible tax planning strategy.

You can negative gear any type of asset such as shares, business, managed investments or property.

Property has always been the most popular for a number of reasons including the availability of finance, safety of the market, general acceptance and understanding as well as the emotional comfort of a physical asset.

Almost 2 million Australians have taken this path and it is a very common and accepted practise however the continuing poor state of Australia's Federal Budget has meant that anything that might increase government revenue is being considered and there has been a stronger focus on negative gearing as an easy target.

This is somewhat concerning as landlords are an important element of a sensible property market, with approximately 30% of Australians being renters. The tax incentive has meant that many landlords are more willing to accept a deficit of rent versus expenses and keep rents at reasonable levels, so there is genuine concern that removing the ability to claim may push rents up further.

The property industry is also a very important element of the economy, so any actions to discourage investment there could prove damaging and need to be carefully considered.

We are yet to see the formal policy options for the current Turnbull Government, however it has been leaked that they may consider limiting the claims to a certain amount of properties, perhaps up to 5 per person and may be stop allowing it as a tax deduction. We will have to wait until the May Budget to see what, if anything happens there.

The Labor Opposition has been more upfront stating that it will change the current system from 1st July 2017 to only allow negative gearing to be claimed on newly constructed property while at the same time reducing the current Capital Gains Tax discount on investment property owned by Australian tax residents from 50% to 25%. The former Labor Government already removed the Capital Gains Tax discount for non-resident taxpayers (including expats) in May 2012.

Labor has confirmed that anyone currently with negative geared properties will not lose their entitlement to claim for properties owned prior to 1st July 2017, so if you are thinking they may win the election and bring this policy to effect, you may want to consider buying an established property sooner than later.

Regardless of what changes may occur, the simple fact remains that any property acquisition should be made on the merit of the property and the income and growth prospects it offers. The tax benefits are only just a consequence of the decision and should never be the main reason to act.

Australia's property market remains undersupplied in most areas and the strong population growth provides stability. We look forward to keeping you informed of any changes that actually occur.

Contact us at tax@smats.net with any specific question you may have or to get our professional team to assist you with your Australian Taxation requirements.