



Commercial depreciation sky high

Despite all of the recent changes to depreciation the benefits for commercial property owners are still fantastic. I have covered this in recent articles but thought I should let the figures do the talking. I have decided to highlight a recent example for a property we have completed an apportionment on.

PROPERTY TYPE: 92 room hostel located in Auckland. Configuration is 56 studio rooms and 36 lofted rooms in addition to a managers' flat and office. The complex is built around a central open courtyard, with all rooms enjoying communal use of a kitchen, dining area, TV lounge and laundry. The building originally comprised an office/warehouse structure which was redeveloped to its current use in 2002.

PURCHASE PRICE: \$5,156,862 including \$100,000 of Plant and Equipment

OPTIONS FOR CLAIMING DEPRECIATION:

OPTION ONE – A full depreciation apportionment that separates the purchase price into Land, Buildings, Fit-out, and chattels PLUS a breakdown of the Plant & Equipment purchased for \$100,000.

OPTION TWO –Based on IRD regulations claiming depreciation on the Plant and Equipment of \$100,000 as a pool at 20% Diminishing Value (DV). This rate being the minimum individual rate of any asset within the pool. All other improvements NOT separated from the buildings.

OPTION THREE – Using the IRD transitional option and claiming 15% of the improvements value at 2% Straight Line (SL). This option is available for properties purchased prior to the 1 April 2011.

As this property was purchased in the 2011-2012 tax year this option is not available but I have included this to highlight what levels of depreciation would be available if it had been purchased in a previous tax year and had been claiming depreciation at the building rate only.

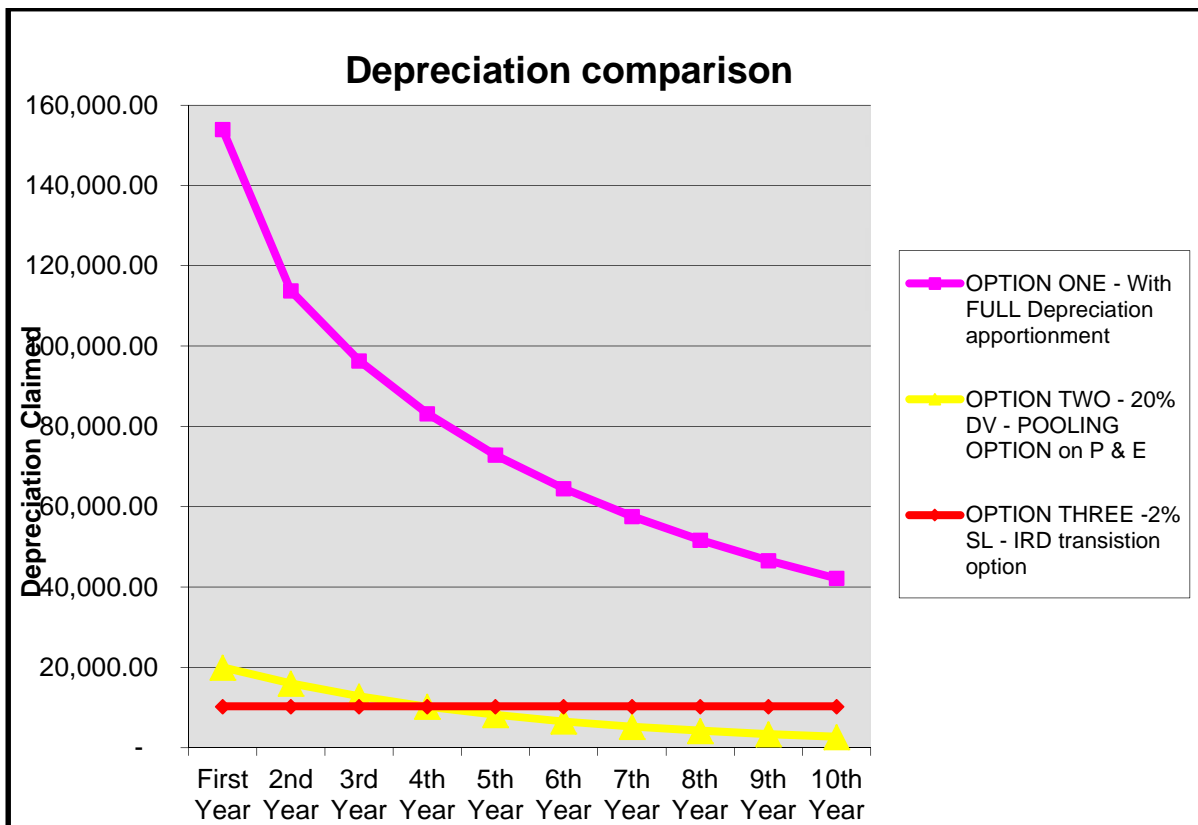
The IRD transitional option allows a one-off adjustment for taxpayers that are currently depreciating commercial and industrial fit-out as part of the building. This allows owners to create a building fit-out depreciation pool of 15% of the building's adjusted tax book value. The pool would be depreciated at 2% straight line

(equivalent to the current building depreciation rate). Taxpayers would be permitted to elect to create a fit-out pool only once - from the start of the 2011/12 income year.

EXISTING PROPERTY OWNERS PLEASE NOTE - IRD have recently released a discussion document that considers not allowing existing commercial property owners, that have only been claiming depreciation at the building rate, to retrospectively adjust their depreciation schedules to accurately separate the value into all of the allowable depreciation categories, as per OPTION ONE. If this discussion document is passed the only option for existing commercial property owners that purchased prior to 1 April 2011 and have completed a tax return is to use OPTION 3 or claim ZERO depreciation going forward. If an existing owner has not yet completed a tax return ALL OPTIONS are potentially still available.

DEPRECIATION CLAIM SUMMARY

OPTION	Year One	5 Years	10 Years
ONE - With FULL Depreciation Apportionment	\$153,919	\$520,135	\$782,793
TWO – 20% DV – POOLING OPTION on P & E	\$10,245	\$51,226	\$102,452
THREE – 2% SL – IRD transitional option	\$20,000	\$67,232	\$89,263



COPY OF ASSET REGISTER TO HIGHLIGHT DEPRECIATION CATEGORIES AND DEPRECIATION RATES

ASSET DESCRIPTION	RECOMMENDED OPENING BOOK VALUE	DIMINISHING VALUE (DV)	
		SUGGESTED IRD DEPRECIATION RATE (Published)	FULL FINANCIAL YEAR DEPRECIATION
LAND			
LAND (excluding Improvements)	\$ 1,741,808	~	
<u>IMPROVEMENTS COMPRISING</u>			
BUILDINGS			
NOTE This apportionment has been completed on the basis that the property is run as a commercial venture and meets the IRD definition of commercial property.			
BUILDING STRUCTURE (Buildings and Structures)	\$ 2,152,989	0.0%	-
FIXTURES, FITTINGS AND CHATTELS			
(NOTE Some individual values have been removed for privacy reasons)			
AIR CONDITIONERS (Through window type) (Building fit-out)	\$ 1,880	20.0%	\$ 376
BLINDS (Building Fit-out)	\$ 9,756	25.0%	\$ 2,439
CARPETS (Building Fit-out)	\$ 74,512	40.0%	\$ 29,805
DOOR CLOSERS (Building Fit-out)	\$ 1,242	13.0%	\$ 161
DRIVEWAYS AND PATHS (Buildings and Structures)	\$ 16,834	4.0%	\$ 673
ELECTRICAL RETICULATION (Building Fit-out)	\$ 75,601	8.0%	\$ 6,048
FIRE ALARM SYSTEM (Building Fit-out)	\$ 2,177	10.0%	\$ 218
FIRE EXTINGUISHER (Factory and other sundries)	\$ 113	13.0%	\$ 15
FIRE HOSE REELS (Building Fit-out)	\$ 3,363	8.0%	\$ 269
FITTED FURNITURE (Building Fit-out)	\$ 17,194	13.0%	\$ 2,235
FREESTANDING FIRE PLACE (Building fit-out default)	\$ 2,227	10.0%	\$ 223
HANDRAILS (Building Fit-out)		8.0%	
HEATER (Electric) (Building Fit-out)		67.0%	
HEATING SYSTEM (Building Fit-out)		10.0%	
LIGHT FITTINGS (Building Fit-out)		20.0%	
MIRRORS (Default class - Building Fit-out)		10.0%	
PARTITIONS (Non load bearing) (Building Fit-out)		10.0%	
PLUMBING (Building Fit-out)		8.0%	
PLUMBING FIXTURES (Building Fit-out)		8.0%	
RETAINING WALL (Wooden) (Buildings and Structures)		8.0%	
SPRINKLER SYSTEM (Building Fit-out)		8.0%	
STOVE (Domestic type) (Residential Rental Property Chattels)		25.0%	
TELECOMMUNICATIONS CABLING (Land based) (Telecommunications)		13.0%	
VENTILATING FAN (Building Fit-out)		20.0%	
VENTILATING FAN (roof mounted) (Building Fit-out)		13.0%	

VINYL FLOORING (Building Fit-out)			20.0%	
WASTE DISPOSAL (Hotel)			25.0%	
	Sub Total	\$ 1,162,065		\$ 128,367
PLANT & EQUIPMENT (As specified on Purchase Agreement)				
(NOTE Some individual values have been removed for privacy reasons)				
APPLIANCES (domestic type) (Hotel)	\$	389	30.0%	\$ 117
BBQ (Residential Rental default)	\$	101	40.0%	\$ 40
BEDDING (Hotel)	\$	4,334	67.0%	\$ 2,904
BEDS (Hotel)	\$	17,784	20.0%	\$ 3,557
BEDS (Hotel)	\$	1,267	20.0%	\$ 253
CARPET CLEANING MACHINE (Cleaning)			25.0%	
CROCKERY, CUTLERY, UTENSILS (Hotel)			67.0%	
DRYER (Laundry)			25.0%	
FITNESS EQUIPMENT (Leisure)			40.0%	
FURNITURE (loose) (Hotel) inc Bookcase, bedside cabinets, arm chairs, desk chairs, dining chairs, lounge chairs, outdoor chairs, office desk, sofas, coffee tables, dining tables, outdoor tables.			20.0%	
LAWNMOWERS (Residential Rental)			50.0%	
MICROWAVE OVENS (Residential Rental)			30.0%	
PERSONAL COMPUTER (Computer)			50.0%	
POLISHER (floor) (Cleaning)			25.0%	
PRINTER (Computer)			40.0%	
PRINTS (Hotel)			20.0%	
REFRIGERATORS (domestic type) (Residential Rental)			25.0%	
SECURITY SYSTEMS (Building fit-out)			20.0%	
STEREO (Residential Rental)			40.0%	
STOVES (Domestic type) (Residential rental)			25.0%	
TELEVISION (Hotel)			40.0%	
TOOLS (loose) (Factory)			40.0%	
VACUUM CLEANERS (commercial type) (Cleaning)			40.0%	
WASHING MACHINES (Laundry)			25.0%	
	Sub Total	\$ 100,000		\$ 24,725
	GRAND TOTAL	\$ 5,156,862		\$ 153,092

The Inland Revenue Requirements and regulations around depreciation are complicated. If you have any questions or concerns please feel free to email me - steve.t@valuit.co.nz