Now more than ever Commercial property owners want to PAY LESS TAX!

Many property owners mistakenly believe that with the reduction, announced in the 2010 budget, of the depreciation rate on buildings reducing to zero from the next tax year, that there will be no depreciation deductions available for the property.

While this is true for the **"building"** there still will be depreciation available on the "**fit-out"** of the property and the "**plant"**. How much will depend on their values and what options you advise your clients to take.

In August the IRD and Treasury published an **Issues Paper** to address unintentional negative impacts of the budget on non residential properties, and to propose legislation to implement the required law changes. While these proposals are not finalised at the moment it is widely believed they will be accepted by the government (maybe with some minor changes).

In April 2010 the IRD clarified the rules for residential property but at that time it was not clear if the same rules would apply to non residential. The following in *italics* is quoted from the Issues Paper.

Inland Revenue's interpretation statement IS 10/01 (Residential rental properties – depreciation of items of depreciable property) sets out the Commissioner's view of the law as it relates to the fit-out of residential buildings. Although the statement applies only to residential buildings, if its principles were to apply more widely this could result in a number of items of non residential fit-out, that are currently being depreciated separately, being considered part of the building, and non-depreciable for certain buildings from the beginning of the 2011/12 income year. This could have implications for current practice and could introduce a significant tax bias against fit-out of non-residential buildings.

We propose that a distinction be made for tax depreciation purposes between non-residential and residential fit-out.

The law would be changed to clarify that fit-out associated with commercial, industrial, recreational and certain short-term accommodation (for example: motels, hotels, rest homes, and hospitals) would be able to be separately depreciated. The items of fit-out that would be separately depreciable are described in the Commissioner's "Building Fit-out" asset category. The rates of depreciation for these items would not change as a result of this review.

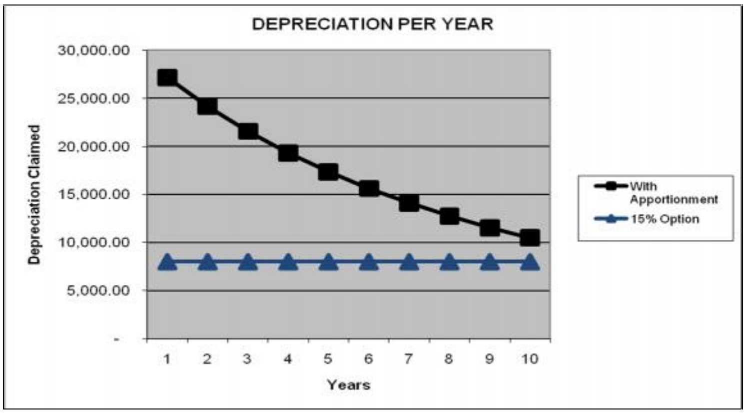
We propose a transitional rule that would allow a one-off adjustment. Under this approach, taxpayers that are currently depreciating commercial and industrial fit-out as part of the building, would create a building fit-out depreciation pool of 15 percent of the building's adjusted tax book value. The pool would be depreciated at 2% straight line (equivalent to the current building depreciation rate). Taxpayers would only be permitted to elect to create a fit-out pool once - from the start of the 2011/12 income year.

What does this mean for commercial property owners?

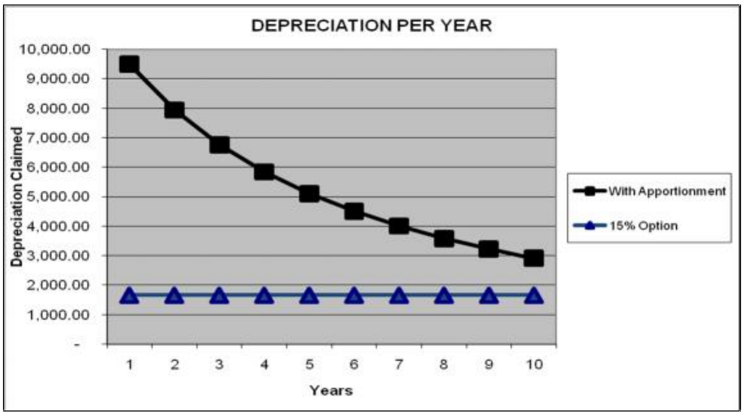
For owners that have already filed tax returns for the property, without separation of fit-out you probably need to use the **Transitional Rule**. If you haven't yet filed a tax return you have the opportunity to have the separation done, using a specialist to produce a detailed **Depreciation Register**.

The following examples are from actual properties we have done full apportionment valuations for, but every property is different – purchase price, level of fit-out owned by property owner, land value, age and condition, etc, so the comparisons are indicative only.

Property Purchase Price $4,100,000					
15% Pool Option		**Dep %**	**Dep Year 1**	**Total 10 Years**	**Tax Saving @28%**
Land	1,400,000	0	0	0	
Building	2,700,000	0	0	0	
Fit-out Pool	405,000	2%SL	8,100	81,000	22,680
With Valuit					
Land	1,400,000	0	0	0	
Building	2,400,000	0	0	0	
Fit-out & Plant	300,000	8-40%DV	27,000	174,000	48,720



Property Purchase Price $981,000					
15% Pool Option		**Dep %**	**Dep Year 1**	**Total 10 Years**	**Tax Saving @28%**
Land	430,000	0	0	0	
Building	551,000	0	0	0	
Fit-out Pool	82,650	2%SL	1,653	16,530	4,628
With Valuit					
Land	430,000	0	0	0	
Building	460,000	0	0	0	
Fit-out & Plant	91,000	8-40%DV	9,500	53,000	14,840



From these tables and graphs you will see that there is significant tax saving and increased cash-flow by having a full apportionment and detailed **Depreciation Register** produced. Talk to your clients and ensure they are maximising their depreciation claim.

There is a limited window for this opportunity so act now!!!