Depreciation – ***now every reason to claim and no reason not to!***

Over recent years a couple of things have held many investors back from claiming their full depreciation entitlement, and accountants from recommending it.

1. Uncertainty over what IRD would allow to be separated from the building such as electrical wiring and plumbing AND
2. The thought of having to repay a majority of the depreciation through depreciation recovery when selling.

BUT these two hurdles have been removed leaving very little downside to claiming your full depreciation entitlement.

Recent Changes summarised

Budget - May 2010

As was widely forecast the Government **removed the ability for property investors to claim building depreciation** in the Budget, commencing April 1 2011, **whilst still allowing the depreciation on Chattels and Fit-out**. The big benefit is that it removes the risk of being hit with a big depreciation recovery bill when you sell the property. In the past this has seen many investors claim little or no depreciation, but no longer. The chattels and fit-out can in most cases be proven to reduce in value and therefore recovery on these items will be removed or significantly reduced.

Interpretation Statement – April 2010

IRD released its Final Interpretation Statement on the “Tax treatment of Residential Rental property for Depreciation purposes”, **finally clearing the confusion surrounding what IRD considers to be part of the building for depreciation purposes. While items such as plumbing, partitioning and electrical reticulation are considered part of the building, investors will be able to claim many "fit-out" items that are allowable, such as fences, air conditioning units and some decks along with the standard chattel items.** With this confusion now clarified (10 years on!!!!!!), we are full steam ahead in regards to the separation of items considered to be chattels as well as items of fit-out.

What you need to do

For properties you currently own

For those investors that haven’t had a breakdown of their assets into the various IRD categories on their latest purchases, you need to think about this, because come April 1st 2011 you will have no depreciation. So now is the time to have a depreciation apportionment completed on those properties purchased in the past few years.

People selling properties that have had chattel valuations completed in the past need to consider an exit report to help minimize depreciation recovery. The timeframe for this can be tight as we will need access to the property.

For those of you that have had a depreciation apportionment completed you need to ensure that items IRD considers to be part of the building, in line with the interpretation statement, are now being claimed at the building depreciation rate of 3% (Diminishing Value) and in April 2011 these will need to be adjusted to 0%, as well as the building structure. To determine if items are considered to be part of the building we now have a three step process to follow but in most cases this will include partitions, electrical wiring, pluming, plumbing fixtures, kitchen cabinets (fitted furniture), tiles, vinyl, garage doors, telecommunications cabling and some decks and canopies depending on the level of fixing to the building. The three steps in summary are as follows;

> **Step 1**: Determine whether the item is in some way attached or connected to the building. An item will not be considered attached for these purposes, if its only means of attachment is being plugged or wired into an electrical outlet (such as a freestanding oven), or attached to a water or gas outlet. If the item is attached to the building, go to step 2.
>
> **Step 2**: Determine whether the item is an integral part of the residential rental property such that a residential rental property would be considered incomplete or unable to function without the item. If the item is not an integral part of the residential rental property, go to step 3.
>
> **Step 3**: Determine whether the item is built-in or attached or connected to the building in such a way that it is part of the “fabric” of the building.

For future purchases

When buying a property in the future make sure you take full advantage of your depreciation entitlements, it’s all about increasing cash-flow. The issues around depreciation recovery are now negligible and we have clarity from IRD around what can be separated from the buildings. Without an apportionment you will get NO depreciation from 1 April 2011.

Make the Most of every Opportunity!!

If selling an existing property have an exit report completed – this will **minimize** your depreciation recovery

Complete a Chattels valuation on those recent property purchases if you haven’t already – this will **maximise** your allowable depreciation claim.

For all future purchases ensure you get a depreciation apportionment completed, without it you will get no depreciation.

Remember those previous hurdles have now been removed.