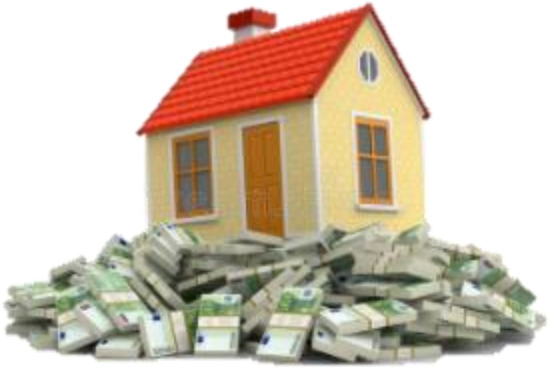
Perriam & Partners Ltd
Chartered Accountants & Business Advisors

RENTAL DEDUCTIBILITY TABLE

A guide to all those expenses you may be entitled to claim against your Rental Property Income

June 2021



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EXPENDITURE	ANALYSIS	TAX TREATMENTS
PURCHASE OF RENTAL PROPERTY	Split land, rental building and chattels to maximise depreciation claim	LAND … capitalise and do not depreciate. BUILDINGS …with effect from 1 April 2011 no depreciation can be claimed on buildings. CHATTELS … capitalise and depreciate (average depreciation rate is 22% DV)
ACCOUNTING FEES (setting up the business e.g. investigating the viability of the property)	Treated as part of the cost of the rental property	**CAPITALISE**
LEGAL FEES (for the purchase of the rental property)	Legal Fees	**FULLY** deductible expense up to $10,000
LEGAL FEES (incurred in arranging a mortgage to finance the rental property)	Legal Fees	**FULLY** deductible expense up to $10,000
LEGAL FEES (for preparing a tenancy agreement)	Legal Fees	**FULLY** deductible expense up to $10,000
PURCHASE/REPLACEMENT OF CHATTELS	i.e. Oven, Heatpump, Freezer etc.	For chattels over $500 up to 17 March 2020 these were required to be capitalised. The threshold has now increased to $5,000 between 17 March 2020 – 17 March 2021. Due to Covid-19 from 17 March 2021 onwards the threshold has been set at $1,000.

<table>
<tr><td>VALUATION FEES
(cost for a Registered Valuer to prepare a valuation report for financing purposes)</td><td>Valuation Fees</td><td>FULLY deductible expense</td></tr>
<tr><td>EXPENSES
(expenditure on a rundown property to improve it substantially and make it fit for renting out)</td><td>May be treated as dilapidation expenses and therefore as part of the cost of the rental property</td><td>CAPITALISE</td></tr>
<tr><td>EXPENSES
(taking down a badly deteriorated wall and putting a conservatory in its place)</td><td>Improvements to rental property</td><td>CAPITALISE as part of building</td></tr>
<tr><td>BANK FEES
(Bank administration fee for the mortgage)</td><td>Loan fee</td><td>FULLY deductible expense</td></tr>
<tr><td>INTEREST
(interest paid on funds borrowed to acquire the property)</td><td>Interest</td><td>The Government announced changes to the deductibility of interest, effective 1 April 2021. A copy of the abatement proves to the deductibility is set out below:
<table>
<tr><th>Income year</th><th>Percent of interest you can claim</th></tr>
<tr><td>1 April 2020–31 March 2021</td><td>100%</td></tr>
<tr><td>1 April 2021–31 March 2022 (transitional year)</td><td>1 April 2021 to 30 September 2021 - 100%
1 October 2021 to 31 March 2022 - 75%</td></tr>
<tr><td>1 April 2022–31 March 2023</td><td>75%</td></tr>
<tr><td>1 April 2023–31 March 2024</td><td>50%</td></tr>
<tr><td>1 April 2024–31 March 2025</td><td>25%</td></tr>
<tr><td>From 1 April 2025 onwards</td><td>0%</td></tr>
</table></td></tr>
<tr><td>MORTGAGE REPAYMENTS
(principal repayments)</td><td>Reduces mortgage balance</td><td>NOT deductible</td></tr>
</table>

RATES (on rental property)	Rates	**FULLY** deductible expense
INSURANCE (on rental property)	Insurance	**FULLY** deductible expense
LIFE INSURANCE (if, and only if it is a requirement of the bank in order to obtain funding)	Insurance	**FULLY** deductible expense
PHONE COSTS & INTERNET CONNECTION (telephone costs if you manage the property)	Telephone and Communication	A **PORTION** of your home telephone costs and/or cell phone costs
CONTINUING EDUCATION (Property and Investments Magazines and Seminars)	Continuing Education	**FULLY** deductible expense
MORTGAGE REPAYMENT INSURANCE (mortgage repayment insurance for mortgage on rental property)	Insurance	**FULLY** deductible expense
DRAWINGS (interest on money borrowed to acquire an asset apart from the rental property, with rental property being used as security for the loan)	Drawings	Private Expenditure. **NOT** deductible
AGENT’S FEES (Agent’s fee to collect the rent and maintain the property)	Agent’s Fees	**FULLY** deductible expense
COMMISSION (commissions paid to the Agent to find tenants for the property)	Agent’s Commission	**FULLY** deductible expense

REPAIRS & MAINTENANCE (cleaning and rubbish removal)	Repairs and Maintenance	**FULLY** deductible expense
REPAIRS & MAINTENANCE (replacing broken shower head, plastering and painting crack in a wall, replacing a blown element in a hot water cylinder)	Repairs & Maintenance	**FULLY** deductible expense
REPAIRS & MAINTENANCE (redecorating the property to return it to the state it was in when you purchased it for use as a rental property	Repairs & Maintenance	**FULLY** deductible expense
REPAIRS & MAINTENANCE (redecorating expenses or other maintenance, and property is therefore temporarily unavailable for letting)	Repairs & Maintenance	**FULLY** deductible expense
REPAIRS AND MAINTENANCE (replacing a bath with a shower)	Here you have not put the asset back into its original condition. You have changed the nature of this, and it is therefore not an improvement.	**CAPITAL**
ADVERTISING (advertising in newspaper to obtain tenants or tradesman)	Advertising	**FULLY** deductible expense

GENERAL EXPENSES (normally the classification given to small items of expenditure, say less then $25, for items such as stamps stationery etc)	General Expenses	**FULLY** deductible expense
INSPECTION COSTS (costs of inspecting your property)	Inspection Costs The costs of inspecting your property are generally tax deductible providing they are associated with the ongoing maintenance of the tenancy, as opposed to the actual sourcing of an investment property (see below). Costs of travel and inspection *when properties are being acquired* are **not** fully tax deductible. These costs are associated with the acquisition of the property and must be added to the capital cost of acquisition.	**FULLY** deductible expense or treated as a capital cost
ACCOUNTING FEES (Accounting fees in relation to looking at the feasibility of the purchase of a property)	Accounting	**NOT** deductible
ACCOUNTING FEES (Accounting fees for preparing rental income statements and tax returns)	Accounting	**FULLY** deductible expense
EXPENSES (expenses incurred while property is empty and available to be rented out)	Various expenses as detailed above	You may be required to prove the property has been advertised as available to be rented. In most cases these expenses will be **FULLY** deductible

HOME OFFICE EXPENSES (fair and reasonable portion of the house outgoings to conduct the rental business from your home) To justify a claim for home office expenses you will need to prove that you are actively conducting the business from home. Inland Revenue are unlikely to accept that one passively held investment property justifies a claim for home office expenses.	Home Office Expenses If you have your property professionally managed then there may be some difficulty in justifying this claim.	If you use your home to conduct a rental business, you **MAY** be entitled to a partial deduction for the outgoings that relate to the use of the home for business activities. These include: ▪ heating ▪ lighting ▪ rates ▪ insurance ▪ mortgage interest ▪ house and contents insurance ▪ repairs and maintenance ▪ telephone rental ▪ depreciation The portion of outgoings deductible is based on the area used for the business, expressed as a percentage of the total area of the home: Area used for business purposes _______________________ Total area of home _______________________ It is not absolutely necessary to set aside a specific room for business purposes, nor is it necessary for your home to be physically changed to suit the business. However in cases where a separate room is not set aside, it may be appropriate to apportion the outgoings based on criteria such as the amount of time spent on income earning activities at home **as well as** the area used.

DEPRECIATION ON CHATTELS (depreciation allowance for wear and tear and ageing of the chattels, fixtures and fittings)	Depreciation	**WHAT IS DEPRECIATION?** Over time, assets experience wear and tear and their value slowly decrease. Depreciation accounts for this loss by assigning a dollar value to the asset and estimating the amount lost per year. This yearly amount can be claimed as an expense on your tax return and used to reduce your taxable income—less taxable income, less tax needed to be paid. That means more cash left in your back pocket. **WHAT ITEMS CAN YOU CLAIM?** Generally speaking, you should be able to depreciate most of the items in your rental property that aren't a part of the building – these are known as chattels. Examples of chattels that you can claim depreciation on include: – Certain types of air conditioners and heat pumps. – Air ventilation systems. – Clotheslines. – Alarms. – Small appliances. – Curtains and blinds. – Freezers and fridges. – Dishwashers. – Light shades. – Loose furniture. – Stoves. – Satellite dishes. – Washing machines. – Waste disposal units.

		Inland Revenue assigns each of these items a useable life from 3 – 15 years along with its dollar value, allowing you to calculate depreciation on each. **HOW DO I CLAIM?** You can use one of two methods to calculate depreciation: Diminishing value: depreciation is calculated as a percentage of the item's tax value, which means your depreciation reduces each year. Straight line: your asset depreciates every year by the same amount – a percentage of its original cost price/value. To use these methods, you'll obviously need to know the value of your chattels. This is easy if you bought them as you can simply use the price on the receipt. If you didn't (or can't), you'll need to research the market value of the asset and use that. Another important thing to note is that in some cases you may be able to instantly claim the entire value of newly purchased assets under $1,000 as depreciation. Keep in mind, Inland Revenue does audit property investors so you must be confident that any values are correct before you use them to avoid any issues—and keep records of receipts.
DEPRECIATION ON BUILDINGS	Depreciation	Depreciation on residential rental property is not claimable. It is only available as a claim on commercial property.

NON DEDUCTIBLE EXPENSES

For tax purposes, you cannot deduct capital or private expenses from your rental income. Capital expenses are costs you incur to increase the value of your capital asset.

Private expenses are incurred for your own benefit, and are not connected with producing taxable income. All of these things are NON DEDUCTIBLE expenses:

- The principal portion of your mortgage repayments.
- Interest on money which has been borrowed for some purpose other than financing the rental property, even if you use the rental property to secure such the loan.
- The cost of repairing or replacing any damaged part of the property, if the repairs or replacement make improvements to the property which increase its value.
- Real estate agents fees.
- The cost of making any additions or improvements to the property.

However, you can capitalise the cost of the last three items and claim depreciation on them as part of the cost of the property.

RENTAL INCOME	ANALYSIS	TAX TREATMENT
RENTAL INCOME (rent received in advance)	Rental Income	Return in the income year it is received unless a company or trust which you would apply the accruals rules
BOND (amounts received for bond and passed on to by Tenancy Services)	Received from tenant and held in trust by Tenancy Services per rental agreement	**NOT** Income
RENTAL INCOME (amounts received from Tenancy Services for payment of damages and rent)	Rental Income	Return in the income year it is received from Tenancy Services
RENTAL INCOME (rent arrears)	Rental Income	Return in the income year it is received unless a company or trust, then you would apply the accruals rules

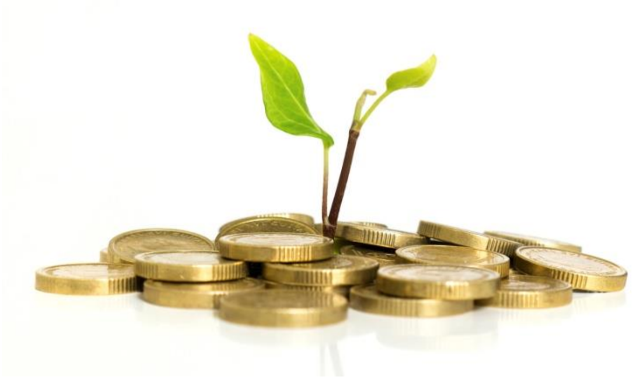
NEW HEALTHY HOMES STANDARDS FOR RENTAL PROPERTIES

New minimum standards will make rental properties drier and warmer. The healthy homes standards, which become law late 2019, aim to improve heating, insulation, ventilation and drainage, reduce moisture and stop draughts.

Ensuring all tenants have a warm and dry home is a priority for the Government, to help improve the wellbeing of New Zealanders and their families. Nearly 600,000 households rent in New Zealand, and research has shown that New Zealand's rental housing is of poorer quality than owner-occupied homes.

THE HEALTHY HOMES STANDARDS	
HEATING	The main living area must have a fixed heating device that can heat the room to at least 18°C.
INSULATION	Ceiling and underfloor insulation must either meet the 2008 Building Code, or (for existing ceiling insulation) have a minimum thickness of 120mm and be in reasonable condition.
VENTILATION	Ventilation must include openable windows in the living room, dining room, kitchen and bedrooms. Rooms with a bath or shower or indoor cooktop must have an appropriately sized extractor fan.
DRAINAGE	Rental properties must have efficient drainage, guttering, downpipes and drains.
MOISTURE	If a rental property has an enclosed subfloor space, a ground moisture barrier must be installed where possible.
DRAUGHTS	Any gaps or holes in walls, ceilings, windows, floors and doors that cause noticeable draughts must be blocked. This includes all unused chimneys and fireplaces.

ADVICE FOR NEW AND EXISTING INVESTORS
Firstly, you should take the approach that it is a long term outlay.



- What direction is the city moving in?
- How much land is available for development?
- Where are their few vacant houses?
- You want to be buying ahead of the wave.

Often the best buys will still be in the traditional areas:

- Close to the city centre.
- Decent size section for “parents and two kids scenario”.

And …

- Always be on the lookout, read the business papers, the internet, watch for international events that can impact on investor sentiment.

- We should always be one step ahead. Ask yourself, how do these things impact on my properties? If the market starts to run, then do you get out?

Here is a saying from Olly Newland, a New Zealand property guru:

“What you should always be looking for is a return **of** your capital, not a return **on** your capital”.

HERE ARE OUR TOP 9 TAX DEDUCTION MISTAKES

1. Cutting corners on advice
2. Assuming all interest payments are deductible
3. Claiming for ‘maintenance’ when it’s really capital improvements
4. Trying to claim for every little last item
5. Purchasing before you have the right ownership structure in place
6. Moving money and properties around without seeking our advice
7. Missing out on claiming depreciation on chattels
8. Missing out on mileage and mobile phone deductions if you are managing your property
9. Claiming expenses related to selling a property

RETENTION OF BUSINESS RECORDS
Please note that Inland Revenue requires all business records to be retained for a minimum period of SEVEN YEARS.

WHAT MUST BE KEPT?
Business records, which must be kept, include documents which provide a record of your business transactions or which enable these transactions to be traced and verified through the accounting system from start to finish. These include sales invoices, receipts, banking records, creditors' invoices, cheque butts and cash books.

WORKPAPERS
Workpapers are also desirable as they assist in the preparation of proper accounting records for the determination of your business's income tax liability.

INLAND REVENUE AUDITS

An audit is basically a check of the tax records of businesses to make sure that your returns have been filled in correctly and that you have paid the correct amount of tax. An audit can cover Income Tax, GST and PAYE returns. After an audit you may be entitled to a refund or have to pay more tax.

As part of our completing your annual financial statements and tax returns, we ensure where possible, that your exposure to any audit is minimised.

As you are in business you can expect to be audited at some stage.

PUTTING YOUR TAX AFFAIRS RIGHT
If you find that you've made a mistake on a return you've sent in, please contact our office as soon as possible. Telling Inland Revenue what is wrong with your tax affairs before they find out is called a voluntary disclosure.

The advantages of doing this are:

Inland Revenue
Te Tari Taake

- You will not be prosecuted in court.
- The penalty tax charged is far lower, along with "use of money" interest charges.

You can make a voluntary disclosure any time before being informed that you will be audited or investigated. Please call us so that we can suggest how to correct any short paid tax, so as to minimise any resulting inquiry from Inland Revenue.

WHEN ARE YOUR BUSINESS TAX RETURNS DUE TO BE FILED WITH INLAND REVENUE?

Your first financial year ends on the next 31 March. Following this date you have until 31 March the following year to engage our office to prepare and file your tax returns with Inland Revenue. The reason for the extended time period is that you are now linked to our Inland Revenue agency listing and so an automatic extension of time is granted. If this were not the case then you would need to have your tax returns filed by 7 July of the calendar year.

YEAR END RENTAL QUESTIONNAIRE

Available on our website are our end of year rental questionnaires. This has been designed to assist you with putting together the necessary information to enable us to prepare your end of year reports. The more time you attribute to completing this checklist the less time is generally required by our staff members to prepare your annual reports.

Once you have completed the checklist you should then make a time to meet with one of our staff members who will review your checklist and any other information with you.

BRIGHTLINE RULES

If you purchase a residential investment property and/or a holiday home (assuming that your holiday home is not your principal home of residence) then if you sell the property within five/ten years of purchase, you will be taxed on the capital gain.

1 October 2015 → 2 years

28 March 2018 → 5 years

27 March 2021 → 10 years

Here are the four steps in the land sale process of relevance to the bright-line test:

- Contract to purchase (sale and purchase agreement).
- Registration of title for purchase (generally commencement date for Brightline Period)
- Contract to sell (sale and purchase agreement) (Final date for purposes pf Brightline test)
- Registration of title for sale.

BRIGHTLINE RULES
KEY POINTS

1. It is not the settlement date on purchase that is the key date but rather the date that title passes.
2. As to the sale date it is the date that the Vendor signs up a Sale and Purchase Agreement irrespective of whether the contact is conditional or not.
3. Special rules apply to house and land packages and subdivisions.
4. The test applies to all New Zealand tax residents and includes all overseas residential property.
5. Key exclusions include property used for business and/or farmland together with the main home exclusion.
6. You should consult with one of our staff if you have any particular questions relating to these rates.

WHAT DRIVES RENTAL PRICES?

- Summer is generally better than winter to get the best rent.
- Supply and demand, i.e. how many prospective tenants are attracted to the property.
- Obviously, location and proximity to local amenities.
- Property managers who have a better feel of the local market
- Recent legislative changes have resulted in landlords selling up leaving less available rental properties, and thus higher rents.
- Showing the tenants that you care.
- Allowing pets.

The reality is however, so long as we have a rental shortage, rents will remain high and will continue to increase.

Renting your property is no different to any other business – supply and demand is what inevitably sets the price.