Property Investment, done properly.

Introduction

One of the most popular and historically proven investment options is residential property. Whether you are a first home buyer, first time property investor, or have an existing property portfolio – we are happy to help.

Various financial factors influence the return on your investment such as the changing economic landscape, government legislation and inflation. To ensure your investment thrives and to make informed decisions on your journey to financial freedom, it's critical to to grasp these critical factors.

In today's ever-evolving financial climate, landlords face challenges like changing lending rules, loan-to-value restrictions, and interest deductibility changes. That's why professional advice and experience are now more invaluable than ever. Seek guidance from experts, be it an external accountant, mortgage broker, or financial adviser.

At Properli, our Financial and Property Investment Advisers enable you to unlock the potential of property ownership and investment to secure a better financial future. We understand that property investment takes hard work and dedication but possess the expertise and experience needed to ensure that you have real tangible results.

This comprehensive guide offers a detailed overview of the key factors that can impact the financial performance of your residential property investment. It also emphasises when and where professional advice becomes imperative.

Invest wisely with sound and impartial advice.

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Why property vs. other investment options?

Investing in residential property has historically been a smart move for New Zealanders who want to build wealth and secure their financial future. Despite recent revisions to lending and taxes, there are still countless reasons why residential property continues to be an incredibly appealing investment choice.

Property is tangible

Compared to other investment options, property is a tangible asset, meaning it can be touched, seen and used. Tangible investments are often considered more concrete and real as opposed to stocks or shares. Property also offers direct ownership, allowing for more control and peace of mind due to reduced risk of fraud or theft.

Property is stable

Historically, over extended periods of investment, real estate tends to exhibit reliable and foreseeable returns. Data from REINZ indicates that property has consistently yielded an average annual capital growth of approximately 6%. Housing is a necessity and as population increases, the demand for property continues to grow.

Property is leverageable

The key benefit of property investment is the power of leverage, allowing you to profit from other people's money, typically from banks. In certain situations, you can borrow the entire purchase price while keeping all the gains for yourself.

Property can provide passive income

While managing a property requires some level of oversight, it can be relatively passive compared to running a business or actively trading. Property management services can manage day-to-day tasks, taking more off your plate and reducing your workload. As debt is paid down, an investment can be positively geared, creating a stable income stream. Rental income and capital growth are provided by property over time.

Property is bankable

Traditionally, residential property investment has been favored by banks in New Zealand. With a unique approach, these banks are willing to finance property purchases up to 100% of their value, subject to individual investor circumstances. This is not a possibility for alternative investment options hereby allowing a significant opportunity for prospective investors.

Types of property

1. Buying existing property

What is considered to be existing property?

An existing property, also known as a resale property, is one that has been previously owned and lived in by someone else. Existing property does not necessarily mean old, any property older than six months is classed as existing. An existing property can offer several advantages compared to buying a newly built property.

Why buy existing property?

These properties are often located in established neighborhoods with existing amenities, community dynamics and transport lines. One key factor of existing properties is character. Depending on the time period the property was built, it may feature unique architectural characteristics, historical significance or other characteristics that may not be present in new properties. This will also make them attractive when reselling. Lastly, existing properties provide opportunity to add value, allowing for a tangible way to increase the property growth.

2. Buying off the plans

What does it mean to buy off the plans?

Buying property 'off the plan' involves purchasing a property that is yet to be constructed. The details of this property will be conveyed using rendered designs and specified information often in an information pack. The materials to be used, fixtures and landscaping will be included in this pack. This option offers affordability and flexibility for both aspiring homeowners and savvy property investors. However, it's important to consider certain factors before making this decision, including the payment structure.

Why buy a property off the plans?

Experience the benefits of owning a newly constructed property – compliant with the latest building code requirements. Secure your purchase at a fixed price, ensuring no unexpected expenses. Additionally, seize the opportunity to invest in an exciting new development or precinct. Furthermore, tenants favour newly built properties, and they tend to have less maintenance than existing - making this option an excellent choice for investment.

3. Buying a new build

What is the defintion of a new build?

By definition, a new build is a property that is being built or has been built and the title has been issued within 6 months of completion. So if you have a property that has been finished today, it will be classed as a new build until the six-month period is over.

New builds in New Zealand can be anything, from residential lots like townhouses, apartments or free standing homes which can be off the plans or fixed-price contracts.

Why buy a new build property?

The ultimate benefits are that it's a new home, with newer fixtures and fittings, as well as a 10-year builders guarantee.

Additionally, you may only need a 5-10% deposit for a new build, rather than the traditionally imposed 20-35% deposit. New builds will also be fitted out with the latest and greatest fittings, fixtures, and materials, meaning you won't be inheriting a legacy leaky second-hand home. New homes will have to be equipped to deal with the latest standards imposed for building and by the government and may even take part in sustainable building. If you are looking for an investment property in a new build, a new home could attract great tenants too. A new build is becoming an affordable and very attractive offering for many first home buyers, with access to government grants, use of Kiwisaver and RBNZ guided rules on relaxed credit policies and deposits.

New build properties only require 5-10% deposit, rather than the traditionally imposed 20-35% deposit which applies to existing properties.

4. Mixed use assets

Mixed-use assets are property (for example holiday homes), with both private and income-earning use. You need to work out the amount of private and income-earning use for each asset, as this decides how much income you declare and what expenses you can claim. If your property is not solely for long-term residential tenancy or if it is used as both a residential tenancy and a short-term holiday rental (think Airbnb), you need to pay close attention.

The recent changes to the Residential Amendments Act 2020 have made it significantly more challenging for landlords to navigate this mixed-use scenario. The rules can be complex and perplexing. That's why we strongly advise consulting an accountant if you believe your property falls into the 'mixed use' category.

To qualify as a mixed-use asset, the property must be unused for 62 days during that tax year. However, residential property used as a long-term rental is excluded from these rules.

If your mixed-use asset earns less than $4,000 in that tax year, you have the option to opt-out of the rules. While this may sound appealing, keep in mind that if you choose this route, you will not be able to claim any expenses against this property. This means that you will also not be able to claim any losses on this property as well, making it important to consider whether opting out is the best choice for your finances.

When it comes to expenses, there are three types of expenses to keep in mind for mixed-use assets. The first type of expense includes any costs related to renting out your property. These can include expenses such as advertising the property for rent or repairs to damage caused by tenants. With these expenses, you can claim 100% of the costs.

The second type of expense is anything that relates to private use of your property. For example, you cannot claim expenses for equipment that is locked away while the property is rented out. These expenses are not deductible since they are considered personal in nature.

Finally, there are expenses that are neither private nor related to renting out the property. This would include any interest on loans secured against the property, rates, insurance, and other similar expenses. These expenses need to be divided and can be claimed as a deduction based on the percentage of use between private and rental purposes.

It's crucial to note that there are more complicated rules when it comes to quarantining losses and what to claim if your property was sold during the tax year. For example, if you're claiming a loss on the rental portion of your property, this loss cannot be offset against any other taxable income in that year. Therefore, it's important to consult a tax professional to ensure that you're following all of the rules and regulations around mixed-use assets and expenses.

Ownership structures

Owning an investment property can be a profitable venture, however, it involves a lot of decision-making and planning to make it a success. One aspect of this planning includes choosing the right ownership structure for your property. While owning an investment property in your own name may seem like the easiest option, it's important to consider the benefits of other ownership structures. We'll outline the four main types of property ownership in New Zealand and help you understand which one is the best fit for you.

1. Trust

There are two main advantages to having your rental property owned by a trust. The first advantage is asset protection. When you own a rental property personally, you are exposed to potential lawsuits and claims against your personal assets. However, if the property is held within a trust, the beneficiaries of the trust don't technically own the assets held in trust. The trustees do, so any potential lawsuits or claims against the property are limited to the trust assets and not your personal ones.

It's important to seek professional advice before setting up a trust. The Trusts Act 2019 has implemented changes that increase responsibility, compliance, and liability of all trustees, so gaining expert advice in this area is essential. It's also best to consult with your lawyer about the finer points of trust law and asset protection if this is your intention.

Taxation is the second advantage of owning your rental property through a trust. A trust provides you with the tax benefits of income splitting. You can send any taxable trust income to beneficiaries, who will then pay tax on this at their marginal tax rate. If this rate is less than the trust tax rate of 33%, then you'll potentially have tax savings. It's important to note that you're limited to sending $1,000 per year to beneficiaries aged 16 or under.

While there are advantages to owning your rental property through a trust, compliance costs can be high. If income splitting is the reason for putting your investment(s) into a trust, consider any professional fees incurred during the year and make sure that your tax savings outweigh them. Accountant fees can be significant and may actually exceed savings.

Always consult with your lawyer to understand the finer points of trust law and asset protection. By weighing the pros and cons, you can make an informed decision on how to structure your investment and protect your assets.

2. Sole Proprietorship/Partnership

Sole Proprietorship or Partnership is the most common form of ownership of property in New Zealand. A sole proprietorship is an unincorporated entity that does exist apart from its sole owner. A partnership is similar although involves two or more people agreeing to operate a business for profit. This means an investment property is owned personally, with no restriction on personal liability.

This method was a straightforward way to offset business losses against personal income in the past. Unfortunately, this changed on the 1st of April 2019 with the implementation of ring-fencing tax losses on investment property.

One benefit of sole proprietorship is the minimal compliance cost associated and simple process.

3. Company

Owned as a limited liability company, an investment property gains the advantage of limited liability, contrasting with sole proprietorship. This is done by existing as a distinct legal entity separate from its proprietors. However, there are constraints on the extent of tax optimisations that can be applied.

Companies/corporations incur elevated compliance expenses, and potential intricacies arise concerning capital gains when transacting property with affiliated parties. Notably, capital gains can only be distributed in a tax-exempt manner upon the company's dissolution. This consideration becomes crucial if you intend to possess multiple rental properties within the same corporate entity.

One of the fiscal advantages afforded to corporations is the automatic deductibility of interest, irrespective of the loan's purpose. This differs from other ownership options where interest deduction pertains solely to loans initially acquired for property purposes.

It is paramount to recognise the intricacies associated with procuring loans and withdrawing funds from the corporation, a scenario distinct from the proprietorship or partnership models. Engage with a certified accountant to ascertain whether adopting a corporate structure aligns with your investment objectives.

4. Look-through company

A look-through company is a type of business structure designed for tax purposes. In an LTC, the company itself is not taxed on its profits, the profits or losses "look through" the company and are attributed directly to the shareholders.

Loss Attributing Qualifying Companies were succeeded by look through companies. LTC retains the advantages of limited liability inherent in a typical company setup while enhancing tax efficiency considerably for its shareholders.

Taxable gains or losses are directly transmitted to shareholders based on their share of ownership, subsequently attracting taxation at their individual rates. While this model offers less versatility in terms of tax options compared to the distribution avenues accessible to trusts, it generally incurs lower compliance expenses than a trust arrangement. This method can be particularly beneficial to small enterprises or family-owned businesses.

At Properli, we possess the unique capability to connect you with a wide range of professionals who can assist you in successfully navigating the world of property investment. By leveraging the expertise of this network, we can guide you towards establishing an ownership structure that is not only tailored to your specific needs but is also aligned with industry best practices. Rest assured that our extensive contacts and unwavering commitment to excellence will ensure your property investment journey is both beneficial and secure.

AirBnB vs. long term rentals

For certain property owners, AirBnB and similar short-term rental platforms present an alternative and often lucrative avenue for generating rental income. However, before venturing into this income generation approach, landlords should take care to fully comprehend the potential tax consequences, which can differ based on geographical locations.

When comparing the advantages vs disadvantages of short vs long-term tenancy strategies for investment property, these tax implications are worth looking in to.

Recently, many regional authorities have begun targeting properties specifically used for property owners who utilise AirBnB. Auckland Council implemented significant increases for properties used for short-term rental purposes. If your property will be rented out for over 28 days per year, the APTR (Accommodation Provider Targeted Rate) will come in to affect as part of the 10-year Budget 2023-2024 for Auckland. This rate application is explained in detail below:

Number of nights booked per year	APTR rates level (not charged in 2023/2024)	General property rates level
Up to 28	Does not apply	Continue to be rated as residential
29 to 135 (medium occupancy)	25% of APTR if the property is in zone A or B	Rated as 75% residential and 25% business
136 to 180 (moderate occupancy)	50% of APTR if the property is in zone A or B	Rated as 50% residential and 50% business
More than 180 (similar to commercial occupancy rates)	100% of APTR if the property is in zone A or B	Rated as business

The gains that can be realised through a short-term accommodation model will be offset by these rates as a portion will be considered and taxed at a business rate rather than residential.

Short-term residential accommodation is subject to GST in New Zealand. Landlords should be mindful that once their property becomes subject to GST, it will carry tax implications depending on various factors. Rental income generated through short-term accommodation whether one property or multiple, if the income exceeds $60,000 annually must register for GST. If the entity owning the rental property engages in another taxable activity, and the total income from both sources surpasses the $60,000 threshold, they are obliged to register for GST. Otherwise, if the income is below $60,000 but the entity decides to register for GST voluntarily, this would be another GST situation.

Once a property falls under GST registration, GST can be claimed on the purchase price. Although, there are specific regulations that prevent you from claiming the entire amount at once. If you decide to put the rental property on the market for sale or discontinue renting the property out on a short-term basis, and subsequently deregister for GST, you will need to remit 15% GST to the IRD upon the property's sale unless another GST-registered taxpayer purchases it, in which case it would be subject to zero-rated GST.

Essentially, this establishes a tax on any capital gain accrued during the property's ownership. As stated above, it is worth noting that this potential GST cost may outweigh the profits realised from short-term accommodation. In conclusion, it's crucial to carefully evaluate your financial objectives when considering the feasibility of short-term vs long-term tenancies, as the actual financial implications may differ from your initial expectations. Ask your mortgage broker and accountant about these implications prior to engaging in short-term accommodation leasing.

Healthy Homes Standards

The Healthy Homes Standards introduce specific and minimum standards for various elements of rental properties within New Zealand. The standards that must be met surround heating, insulation, ventilation, moisture ingress and drainage and draught stopping.

The outlined requirements for each category must be met when any new or renewed tenancy agreement is signed. If a rental property does not meet all standards at the date of signature/tenancy commencement, it must do so within 90 days.

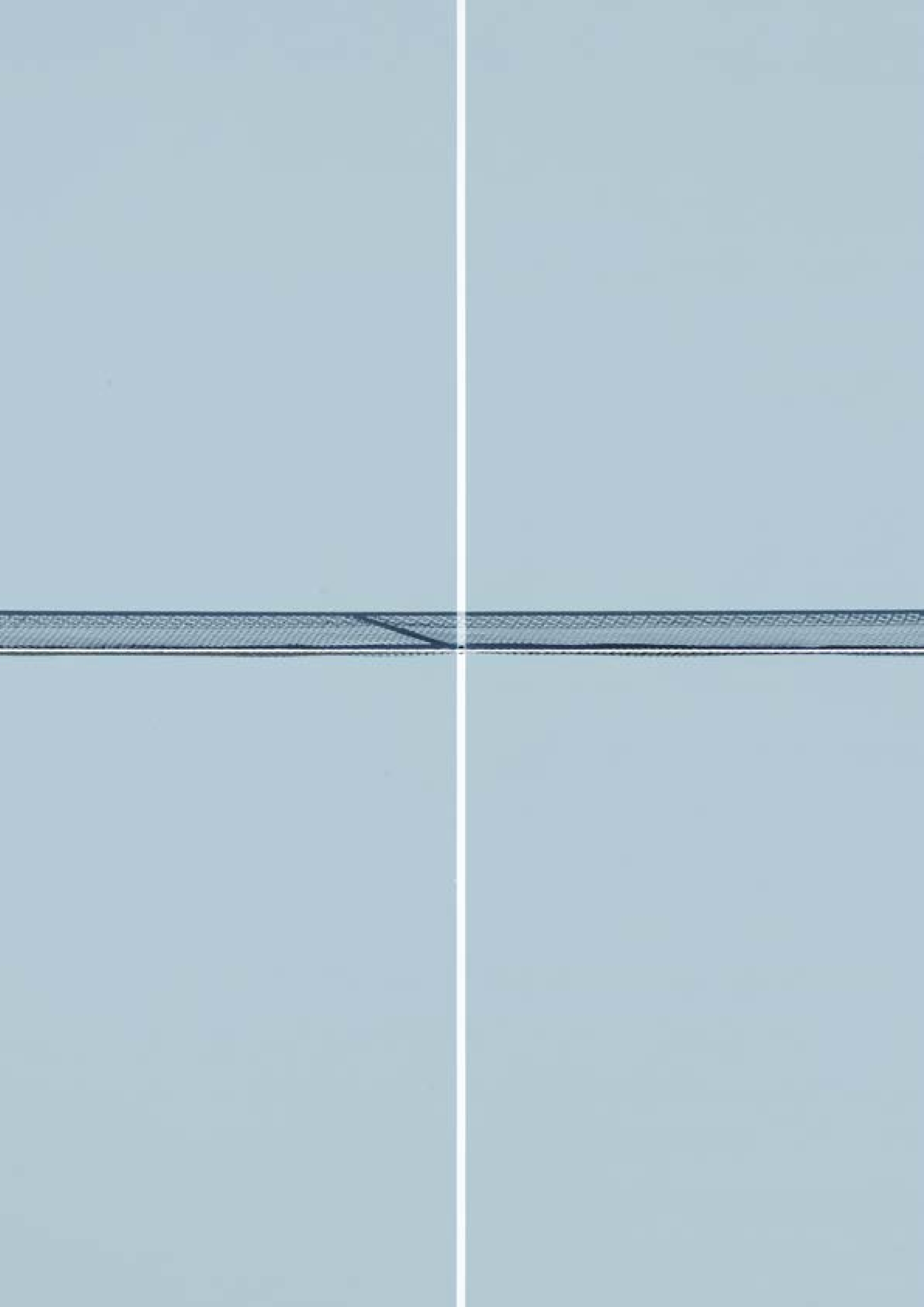
All tenancies that have commenced on or after the 1st of July 2024 (including long-standing tenancies where no changes have been made to the agreement), must comply with the requirements.

To maintain compliance and prevent potential fines, many existing properties in New Zealand will likely require work to meet standards. The ability to claim expenses for healthy homes compliance work depends on the condition of the property and the necessary improvements.

Tax deductibility for residential rental property expenses is relatively straightforward, with the property's condition at the time of acquisition setting the benchmark. Any subsequent expenditure to restore the property to that condition is considered a legitimate tax-deductible expense. However, expenses for improving the property beyond its original condition are non-deductible as they are considered capital improvements.

For example, if an existing moisture barrier has rotten away and is no longer effective and had to be reinstated in order to pass compliance on the moisture and drainage category of healthy homes requirements, this would be classed as a repair and considered as a claimable expense. Conversely, if there was never a moisture barrier at the existing property and one was installed in order to bring the property up to standard, this would be considered an improvement and not a claimable expense as it is not considered a "repair."

If you are unsure whether the improvement made would be considered a repair, an upgrade or a new install, we recommend that you speak to your property manager and a chartered accountant.



Bright-line property rules

Including exemptions

If you sell a residential property you've owned for less than a certain period, called the bright-line period, you may be required to pay income tax on the capital gains since purchase.

The specific length of the bright-line period varies depending on when the property was acquired.

It's important to note that while the cost of acquiring the property is a legitimate tax-deductible expense, any spending on improving the property beyond its original condition other than repairs is classified as capital improvements and is therefore non-deductible.

The bright-line property rule applies to residential rental properties acquired on or after specific dates. If you sell a property on or after 1 July 2024 the bright-line property rule will apply if the property is sold within 2 years of buying it.

If you sell a property before 1 July 2024 the current bright-line periods still apply.

- If you bought the property between 29 March 2018 and 26 March 2021, the bright-line property rule applies if you sell the property within 5 years of buying it.
- If you bought the property on or after 27 March 2021, the bright-line property rule applies if you sell the property within 5 years for qualifying new builds or within 10 years for other residential property.

Your Properli Adviser can assist you to understand how this may apply to you.

Bright-line exemptions

1. **If the property is your main home and the main home exclusion applies.** Your main home is the property where you live for most of the time. If you have more than 1 property it is the one you have the greatest connection to. You cannot have more than 1 main home. The criteria for the main home exclusion will apply as follows.

– use more than 50% of the property's area as your main home

– use the property as your main home for more than 50% of the time you owned it.

The main home exclusion does not apply when you:

– have a regular pattern of either buying and selling or building and selling your main home (even if you or your family live in the property before it is sold)

– have used the main home exclusion twice or more over the 2-year period immediately before you sold your main home.

Residential properties held in trust may use the main home exclusion if the property was the main home of a beneficiary of the trust, and:

– the principal settlor does not have a main home; or

– it is the main home of the principal settlor of the trust that is being sold.

2. **Inherited property**

However, if any part of the property is acquired other than by inheritance, it may be subject to the bright-line rule when it is sold.

3. **Business premises**

4. **Farmland**

It is important to understand that the bright-line rule does not supersede existing property tax rules. Investors may still be required to pay taxes on property profits, even if the bright-line rule is not applicable.

Interest deductibility

A phased approach is being implemented regarding mortgage interest deductibility for rental properties.

- Landlords will be able to claim a **60% deduction** on their interest expenses for the **2023/24 Financial Year**
- Landlords will be able to claim **80% deduction** on their interest expenses from **1 April 2024**
- Landlords will be entitled to claim **100%** of their interest expenses as a deduction from **1 April 2025**

Interest deductibility now applies to existing and new build homes.

Tax

Claimable expenses and expenses you can’t claim

Claimable expenses

Interest

Please see Interest Deductibility section above.

Property Management Fees

When you engage a property manager to look after your tenancies or manage your property yourself but engage with a property manager for select services, you can claim 100% of the expenses you incur for these services. These expenses may include tenant selection, consulting, or inspection-only services, which are offered by Properli, our property management arm to private landlords. Additionally, you can claim 100% of the fees or commission paid to property managers who are managing the tenancy on your behalf.

At Properli, our property managers will give you a monthly and yearly statement outlining the expenses and income you have received throughout the period. This will significantly simplify the process your accountant will undertake in determining and completing your yearly tax returns.

Body corporate fees, fixed water costs, travel associated with property management and valuation fees may also be claimable, but you are advised to engage with a chartered accountant to ensure you are claiming the correct expenses.

Rates & Insurance

The total cost of insuring your rental property can be claimed back as an expense, along with council rates payable through the ownership of the residence.

Maintenance & Repairs

Any costs for repairs or general maintenance can be claimed back. If you opt to undertake the work yourself are only able to claim the materials used, not for your time. Keep in mind, repairs (to return to original condition) can be claimed but improvements cannot. Examples of the differences can be found above in the Healthy Homes section. Plastering and painting damage caused by tenants would be considered to be repairs but removing that wall and extending the property would not.

If you're uncertain regarding the classification of work done on your property as repairs or maintenance, we recommend consulting with a chartered accountant. The distinction between repairs and improvements can sometimes be challenging to navigate but seeking professional advice will help ensure accuracy and peace of mind.

Legal Costs

If your total legal fees for a given year amount to $10,000 or less, you can claim a deduction for the legal expenses incurred in the purchase of a rental property. Additionally, if you are engaged in the business of providing residential rental accommodation, you may also claim legal fees related to the sale of a rental property from your portfolio. It is advised to consult with your chartered accountant to ensure that you meet the criteria to be considered 'in the business'.

Accountant Fees

Fees charged to you by an accountant for advice, management of your accounts and statements and preparation for filing of tax returns can all be claimed. Although, costs involved in the initial set-up of your rental property cannot be claimed.

Depreciation

It's important to note that depreciation cannot be claimed on the property's land or buildings. Depreciation on capital expenses is deductible. As this topic is multifaceted, we recommend seeking advice from a chartered accountant for further information.

Expenses you cannot claim

Certain expenses that do not directly relate to your rental property cannot be claimed. Particularly, capital or private expenses can't be deducted. Capital expenses refer to the costs associated with the acquisition or enhancement of a capital asset. Such expenses include the purchase cost of the property as well as any improvements made to it. On the other hand, private expenses encompass purchases or payments made for personal benefit rather than for the purpose of generating rental income.

If the property is not rented out for the entire year, occupied by tenants, isn't available for rent at any point during the year, or only accessible for rent during a portion of the year, then you are not eligible to claim the ongoing costs for the entire year, including rates, insurance, and interest.

In summary, you cannot deduct the purchase price of a residential investment property, any principal portion of mortgage repayments and costs relating to improvements to the property that increase the property value.

Initial Costs

As touched on above, any costs incurred through selection of the property, including valuation costs or reports on the condition of the property prior to purchasing it. These cannot be claimed.

GST

Goods & Services Tax is not applicable to residential rent. Therefore, rental income should not be included in your GST returns. This differs from commercial rental such as AirBnB.

Home office expenses

If you are legitimately using a portion of your home to run a business, you may be able to claim some of your personal expenditure as a home office expense. This is determined through a calculation based on the percentage of your home that is utilised for these purposes.

You begin by working out the sum of personal expenditure on your personal home, e.g. mortgage interest or rent plus rates, insurance and other expenses. Calculate the square meterage of your home and from that, the square meterage of space used as a home office within it. Divide the square meter size of the home office by the total floor area size. This is the proportion of your home expenses that can be claimed and offset against the rental income you receive.

Alternatively, you can use a method called the Square Metre Rate Option. This method utilises an annual rate established by the IRD, reflecting the average utility costs per square metre for typical New Zealand households. The rate is then applied to the floor area of your home office.

Please note that the square metre rate does not cover mortgage interest, rates, or rent for the residence. However, you can still claim a portion of these expenses based on the percentage of floor area used. It is crucial to ensure that you are utilising the designated space for its intended purpose.

How we can help

Properli are Financial and Property Investment Advisers that enable you to unlock the potential of property ownership and investment to secure a better financial future. We tailor our services to your individual goals, considering your situation, experience, and long-term objectives. Our network of external professionals ensure we can cover all bases required to ease the process of property investment.

Our strategies and recommendations are supported by thorough research and data from REINZ, economists and industry experts. We welcome your questions and thoroughly analyse opportunities to manage risks and maximize potential gains.

Ready to invest in property?

Get in touch with us today.

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Click here to book a time slot now