

Ask the experts

Our panel of experts gives advice on a capital gains tax issue, starting out as a new investor and getting into the New Zealand market



Capital gains tax

Q I bought my first property in February 2007 – a two-bedroom unit in Greensborough, Victoria – for \$206,000. I did extensive renovations for \$14,000, lived there until August 2008 and am now renting it to a friend for \$250 per week. I owe just under \$130,000 as I have been paying it off as fast as I can.

Can you please advise me about my capital gains tax (CGT) liabilities? I have heard that as long as I don't buy another principal place of residence I don't have to pay CGT for the next six years. I would like to buy another property as an investment only and wish to understand more about my CGT liability.

A You can choose to treat the unit in Greensborough as your main residence and be entitled to six years of CGT exemption for this property. However, from the beginning of the seventh year, if you do not move back into the property and live there for a time, CGT will apply when you sell the property. At the beginning of the seventh year the market value of your property at that time will be the new cost base and will influence the sale price and capital proceeds should you decide

to sell then. But, if you move back in to the Greensborough property and live there for a while at the beginning of the seventh year, you are then entitled to another six-year exemption. However, you need to be mindful that

The experts



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Mary O'Brien
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if you also own the property you are currently living in cannot be your main residence, and will be subject to CGT when it is sold.

You can purchase subsequent investment properties but for tax purposes you are only legally allowed to have one main residence at any time. Hence, any subsequent investment properties that you purchase will be subject to CGT upon sale.

As with any investment strategy, we recommend that you seek professional advice before taking any action.

– Michael Quinn

Starting out

Q I would like to start out as a property investor. I don't have any assets but I don't have many liabilities either. My gross salary is \$47,925 plus super and I pay \$560 rent per month. I would like my investment property to hit my pocket as quietly as possible. I'm not sure whether to buy a house or unit or which state to choose. I have come across different suburbs while reading investing magazines but I'm not sure who to go to or trust. Your help and time is much appreciated!

A The first issue you have is one of a deposit. You have not stated if you have one or not, and this would be required.

I have assessed that, with your current commitment to rent and assuming that you have no dependents, you would probably be able to borrow around \$170,000.

Assuming the bank would need you to contribute around 10% plus costs (including lender's mortgage insurance at this level of borrowing), then you would be in the market to buy a property valued at, say \$180,000.

In this case, you would need to have \$18,000 as a deposit and a further \$7,000 for costs, which totals \$25,000.

If we assume you have the capacity to save this deposit, the next issue is buying a property in today's market which does not hit your pocket at all.

While rents are on the move and we are already seeing rental yields of around 7% in some areas, there is still a bit of a shortfall between the potential income and expenses, because rates are so high.

Having said that, if you are prepared for this, and if you buy property in an area where you have identified an abundance of growth drivers, I would guess that this shortfall will be short lived, as rental yields of any property you buy in the coming two years will experience pressure and grow even if the value of the property does not.

As for strategy, I want you to go into this knowing that you don't have much choice. Buying to sell quickly for a profit will not be possible in almost any area, as the economy has ground to a halt and values do not have capacity to boom over the next few years. This means it may be between three and five years before you can even see equity upon which to leverage further, unless you are a great saver and can plunge a lot of extra money into debt repayment.

Having said that, I believe that low socio-economic areas that have low rental vacancy rates, are close to a major city and have good transport will be areas that are most likely to at least grow a little. Don't expect the big booms though, and be prepared to be patient. At least buying now will put you in the box seat for the next boom.

– Margaret Lomas

Buying in New Zealand

Q A friend purchased a property on New Zealand's South Island two years ago and it's returning a positive cash flow and has increased in value by 40%. Is it still possible to get these kinds of deals in New Zealand? How can I find the best areas to invest in? I don't know where to begin to research – any help would be appreciated.

A First, get yourself a pre-approval with a New Zealand bank's letterhead by an accredited New Zealand mortgage broker with a variety of banks/lenders. Secondly, work out what you can afford and which location and search the web (websites are listed below).

Thirdly, pick your area by looking at:

- Occupancy statistics in each main town in each province (rural areas have increased their vacancy rates) and in areas like Queenstown, outer suburbs of Auckland and Wellington
- Median rent statistics which will reflect rental yields (rent to purchase price). Compare existing rent to statistics and obtain rental assessment from real estate agent
- An area/suburb/street online valuation which should show comparable sales
- Market statistics of suburbs to see how the suburbs are changing
- Climatic conditions of the house (sun, wind, flood area, main road or rail noise)
- Suburban area (no problems of crime and good school zone)

The New Zealand market has softened this year, following the worldwide trend. It's impossible to advise on the South Island overall because median-priced quality lifestyle areas like Nelson and Queenstown have been two of the five most expensive areas of New Zealand for years, while the West Coast and Southland areas, which were dormant for many years, have increased dramatically recently.

There may be opportunities due to fire sales, mortgagees wanting to sell very quickly, marriage breakups, Kiwis going overseas, and renovator projects going wrong or over budget. Other circumstances include subdividing a block of land and constructing townhouses or a house on the back, or purchasing and adding capital value and/or rental income through renovations.

Websites to use include:

- www.reinz.co.nz (Real Estate Institute of New Zealand for median sales, rent, market statistics for area)
- www.minhousing.govt.nz/market-rent (government department where all rental bonds are kept for minimum suburban rent)
- www.qv.co.nz/onlinereports/propertyvaluemap.htm (showing all statistics for New Zealand)
- www.qv.co.nz (helps you in so many ways and allows you to order your own valuations)

– Mary O'Brien

Got a property question you need answered? E-mail your questions to editor@yipmag.com.au