LOWE LIPPMANN
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TAX ALERT: ATO FOCUS ON TAXPAYERS WITH INCOME PRODUCING PROPERTIES

Introduction

The ATO is reminding all taxpayers with interests in real property that they will be continuing their focus on a number of common tax errors associated with income producing purposes.

Taxpayers with rental properties are reminded to review the expenses they are entitled to claim as income tax deductions and to understand what records they need to maintain as substantiation. The ATO also advises it will be paying close attention to excessive interest expense claims, claiming costs for initial repairs, and incorrect apportionment of rental income and expenses between owners.

For taxpayers with interests in holiday homes, those currently involved with property developments and the expanding number of taxpayers entering the share-economy (i.e. Airbnb), the ATO has advised that the spotlight is moving their way for the 2016 tax year.

Rental Property Claims

Types of interest expenses which can be claimed as deductions
The ATO reminds taxpayers that interest expenses incurred for a rental property are only deductible when the property is used to produce rental income. The following is a summary of when a taxpayer can and can not claim interest deductions:

You **can** claim the interest charged on the loan used for:	You **cannot** claim interest charged on the loan used for:
• purchase a rental property	• you incur after you start using the rental property for private purposes
• purchase a depreciating asset for the rental property (for example, to purchase an air conditioner for the rental property)	• on the portion of the loan you use for private purposes (for example, money you use to purchase a new car or invest in a super fund)
• repairs to the rental property (for example, roof repairs due to storm damage)	• on a loan you used to buy a new home if you do not use the new home to produce income
• finance renovations on the rental property, which is currently rented out, or which you intend to rent out (for example, to add a deck to the rear of the rental property)	
• purchase land on which to build a rental property	

Apportioning income to your partner or omitting income
The ATO will also be focusing on couples who claim deductions in the name of the other person to reduce tax. For example, where a husband and wife invest in a property 50/50, and then in order to reduce tax, the deductions are claimed in the name of the spouse that can access the largest deduction.

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ATO focus on "initial repairs"
The ATO is concentrating on circumstances where investment properties have repair works done on them shortly after the property is purchased; these are known as "initial repairs". The ATO is more inclined to deem these expenses are "improvements", and should not be claimed as a deduction against income on tax returns, but could be claimed in the future as an addition to the cost base if the property is subsequently sold.

Alternatively, such an expense may be depreciated over the life of the asset under the uniform capital allowance provisions or the capital works provisions. Some taxpayers have been asked by the ATO to provide evidence to support the tax treatment of such initial repairs.

Holiday Homes

The ATO is also targeting holiday home owners that claim properties that are not genuinely available for rent. The key focus by the ATO will be circumstances where holiday home owners are using the property for private use.

If the property is used for private purposes for part of the year, it cannot be claimed. If a taxpayer rents out a holiday home to family or friends, for part of the year and charges them less than market rent, the ATO will also take this into consideration.

Property Developers

The ATO is continuing its focus from recent years on trusts developing and selling properties as part of their normal business. The key focus being circumstances where these developed properties are sold and trusts are incorrectly claiming the 50% CGT general discount. The CGT concession should only be accessed where the trust taxpayer is holding the property on capital account, as they are not in the business of property development and are merely realising a capital asset.

The ATO have indicated they will continue to analyse arrangements with the following characteristics and the trustee claims the 50% CGT discount on the sale of the property:

- clients with experience in either property development or selling property (or experience in the real estate industry) and establish a new trust to acquire property for development and sale;
- circumstances surrounding the arrangement are not consistent with the original purpose of developing the property and holding it as a long term investment; and
- the development is advertised for sale before completion, or is sold soon after completion.

Share Economy Taxpayers

Clearly as advances in technology and data-matching have been enhanced, the ATO has reminded us that its ability to cross-check various claims are increasing every year. The ATO also reminds people engaged in the share economy (i.e. Airbnb) to include income and deductions from these enterprises in their tax returns.

Income people earned through occasionally renting their homes for sharing economy services such as Airbnb are being monitored and the ATO will be data-matching with bank information.

Please do not hesitate to contact your Lowe Lippmann Relationship Partner if you wish to discuss any of these matters further.