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... When Advice Matters ...

Landlords Beware: Key issues for property investors

Are you relying on negative gearing?

There has been a lot of negative conversation about negative gearing lately. But, if you are currently negative gearing your investment property, should you be concerned?

Negative gearing is when you claim more in deductions than you earn for an income producing asset that you have purchased using debt. It is not limited to property, you can for example negatively gear shares, but property is the dominant negatively geared asset claimed by Australians.

The latest Taxation Statistics show that we claimed $22.5 bn in rental interest deductions in 2012-13 against gross rental income of $36.6 bn. While these statistics are not as bad as previous years because of the low cost of borrowing ($1.6 bn less than 2011-12), it's more than the total Defence budget in 2013-14 at $22.1 bn.

The use of these property deductions does not vary widely across income ranges - that is, it's not just those on the highest income bracket using negative gearing. The highest proportional losses were experienced by those with incomes (net of the rental loss) between $55,001 and $80,000, where deductions exceeded rental income by more than 28%. Negative gearing makes owning an investment property accessible to those who potentially would not invest for the long term gain in property value alone.

The Reserve Bank has stated that the 'hot' property market, particularly in Sydney, is because "Investor demand continues to drive housing and mortgage markets, with low interest rates and strong competition among lenders translating into robust growth in investor lending."

In NSW, lending to investors now accounts for almost half of the value of all housing loan approvals. Demand drives price.

The tax policy experts we canvassed generally held the view that negative gearing distorts the market and - in combination with the CGT discount - provides considerable and unnecessary tax advantages to those who least need them.

To quote one, "[Negative gearing] is a uniquely Australian phenomenon (no other country is so generous) and I would abolish it (and the CGT discount) immediately (and not be so generous as to grandfather existing owners). The suggestion that its (temporary) abolition in the early 1990s led to an increase in rent was based on spurious and incomplete evidence. More relevant research has subsequently debunked the suggestion that the spike that happened in Sydney house prices had little to do with the abolition and a lot more to do with other, unrelated market forces."

At present, the Government and property investors want to keep negative gearing. It's a lonely policy position.

The Government Tax White Paper is due out later this year and may provide a better indication of any potential risk for investment property owners. But, negative gearing is not something to bank on as a long term strategy. It's just a question of which Government will have the support to remove it.

Quote of the month

"He who is not courageous enough to take risks will accomplish nothing in life."
Muhammad Ali

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