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IOOF TechConnect fact sheet

Investment property – Centrelink implications

The great Australian dream has always been to own your own home and for some, an investment property. It is important to understand how income from real estate investments, including net income or losses from rental property can impact Centrelink entitlements. This fact sheet answers some common questions regarding Centrelink’s treatment of investment property.

How does Centrelink determine the value of the property?

In most cases, the client’s own assessment of their assets, including real estate, is accepted. Where an assessor has some doubt or needs clarification, documents confirming ownership of the property, exact location or the type of real estate (e.g. vacant land or residential block) may be requested.

If a client provides funds for a building extension, renovations or construction of a granny flat on the same land, a copy of the building contract should be available to verify the construction cost is similar to the estimate provided by the client.

Can Centrelink reduce the asset value by any loans on the investment property?

Generally, the value of an asset is reduced by the amount of any outstanding charge or encumbrance over the asset. The exceptions to the rule are if the charge or encumbrance:

- is for the benefit of a person other than the client or their partner, or
- is secured against an asset which is disregarded.

Case Study 1:
Matthew's son borrows money for his business, secured against an investment property owned by Matthew. The charge or encumbrance against the investment property is for the benefit of a person other than the income support recipient or their partner (in this case the customer's son benefits). Therefore, the value of the investment property cannot be reduced by the amount of the charge.

If a client has an unsecured loan and provides evidence that the loan was specifically obtained to purchase the asset, the outstanding amount of the loan can be deducted from the value of the asset.

If a client has a charge or encumbrance secured against more than one asset, for instance where it is secured against both an asset that is disregarded and an assessable asset, the amount of the outstanding charge or encumbrance is shared between the assets in proportion to the asset values.
Case Study 2:
A client has a charge of $100,000 secured against both their farm and principal home. The value of the farm is $180,000 and the value of the principal home is $60,000. The gross value of the farm and principal home combined is $240,000. Calculating the proportion attributable to the farm – ($100,000 X $180,000)/$240,000=$75,000. This means the net asset value of the farm is $105,000 ($180,000 minus $75,000).

For the income test does Centrelink look at current rent received and expenses or the last tax return lodged?

Generally, the last tax return is used. If a tax return is not available, deduction amounts will need to be estimated. This means that Centrelink will accept most of the allowable deduction relating to property investments (with some exemptions such as depreciation).

For social security purposes, if the net income is a negative amount, the income for social security purposes would be zero. Losses from one property cannot offset against income from another property.

Where a tax return is not available, in some exceptional cases, such as when a property is newly rented, the estimate process outlined in the table below could be used. As soon as the next tax return is available, the estimate method should be discontinued in favour of figures derived from the tax return.

<table>
<thead>
<tr>
<th>Step</th>
<th>Description</th>
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<tr>
<td>1</td>
<td>Deduct one third from the gross amount of rent received (this takes into account land tax, rates, insurance, repairs etc).</td>
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<tr>
<td>2</td>
<td>Deduct any mortgage interest payments from this amount.</td>
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There are some exceptions however. For instance, if a person provides evidence that expenses are more than one third of the gross amount of rent received, (eg if extensive repairs were required to make the property habitable), then the actual amount could be deducted, instead of one third of gross rent. Structural alterations or improvements to the property are not allowed as a deduction.

For the income test, does Centrelink reduce the net rent through any depreciation deductions?

The following deductions are allowed for tax purposes but not allowed for social security purposes:

- capital depreciation
- special building write off
- construction costs and
- borrowing costs, eg loan establishment fees.

What does the question on the Real Estate Form ‘Has the property been your principal home for 20 years or more continuously?’ relate to?

This relates to properties greater than 2 hectares (on one title), such as farms, when people wish to have their whole property exempt from the asset test (under the principal home exemption). This asset test exemption may apply in some situations, such as, if the person is receiving the age pension and have held their home/land continuously for at least 20 years.

For further information

The fast fact finder has been designed to assist you with all of your technical questions. For help please go to www.fastfactfinder.com.au. Should you be unable to find exactly what you are looking for, please contact your local Business Development Manager.

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