Property Speaking

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Welcome to the Winter edition of *Property Speaking*. We hope you find the articles both useful and interesting.

To talk further about any of these topics, or indeed any property matter, please don't hesitate to contact us — our details are on the top right of this page.

Recent property tax changes

Bright-line and interest deductibility

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The changes include extending the bright-line period from five years to 10 years, changing the main home exemption 'test' and removing the ability to deduct mortgage interest from rental income.

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Clarity around fixtures and fittings

Address these before the lease is signed

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For both landlords and tenants negotiating a commercial lease, it is always best to turn your mind to your intentions for any fixtures and fittings attached to the premises; this will help enormously in avoiding costly disputes later on.

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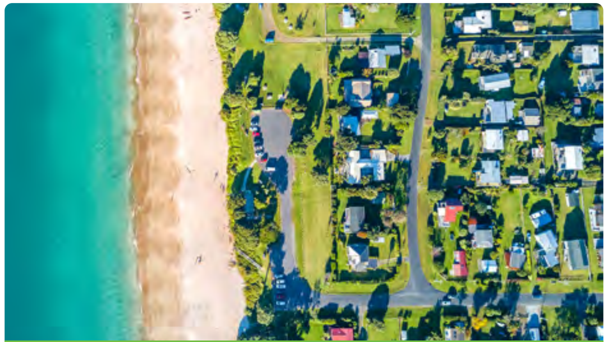

Property briefs

Government housing package: other notable points

The government's recently announced housing package included four major initiatives other than those we have talked about on page 2 **here**.

We give a brief overview of:

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Recent property tax changes

Bright-line and interest deductibility

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Changes to the bright-line regime

The bright-line test was established in 2015 to classify as income the profit made from buying property and selling the same property within a set period. Once captured as income, tax must be paid on that income at your marginal tax rate.

Initially the bright-line period was two years from the date that you acquired the residential property. This was extended to five years from 29 March 2018. From 27 March 2021 onwards, if you purchase residential property and you sell it within 10 years, any profit from that sale will be subject to income tax.

The government has indicated, however, that for new build investment properties, the five-year period still applies, rather than the longer 10-year period.

The government has stated that a new build investment property will be a self-contained dwelling with its own kitchen and bathroom, which has received a code of compliance certificate. The government is consulting with interested parties until 12 July and it is proposed that any agreed measures will apply from 1 October 2021.

Main home exemption

There are, of course, some exemptions to the bright-line test.

If you are selling your main home and you don't have a pattern of buying and selling properties (generally selling your main home two or more times within two years), the sale may not be captured under the bright-line rules.

Previously, if your property was your main home for most of the time that you owned it, the exemption would apply. For example, you buy a property to live in; over a four-year period you spend 18 months working overseas, during which time you let the property out to cover expenses. Under the old rules the property would still be your main home and you wouldn't have to pay bright-line tax on any profit from the sale.

This test has now changed; a property can be your main home for periods of time and not others. The new rule takes into account that you may be called to work in other regions or countries and, in this respect, you are permitted to live somewhere else continuously for up to 12 months. If you live elsewhere for more than 12 months, however, and want to sell your home within the applicable bright-line period (10 years for any older property purchased after 27 March 2021), bright-line tax will apply to the period (over 12 months) you spent living elsewhere.

Using the same example from above, you acquire your property on 1 April 2021 and live in it for six months. On 1 October 2021 you work overseas for 18 months before moving back into your property on 1 April 2023; two years later you decide to sell it.

Inland Revenue will calculate how much the property increased in value and you will need to pay tax for the six months that the property was not your main home.

Interest deductibility

The final change affects interest deductibility. Previously, if you had a mortgage secured against your rental property, you could treat the interest paid as a loss. This could be offset against the income earned by way of rent or sale profit. From 1 October 2021, this will no longer be the case.

Initially the change will only apply to properties purchased after 27 March 2021. Over the next four years, however, the ability to deduct your interest as an expense and offset this against your property income for all properties, including those purchased prior to 27 March 2021, will be phased out completely.

You will be able to claim back 75% of interest paid for the 2022-23 tax year; 50% for the 2023–24 tax year; 25% for the 2024–25 tax year; and from 1 April 2025, you will not be able to treat any interest as a loss.

You should also note that if you borrow money after 27 March 2021 and secure that loan over a property purchased before that date, the interest deductibility rule will be applied as if the property was also purchased after 27 March 2021 and you will not be able to claim back the interest.

These changes make it more important than ever to get legal and accounting advice before you decide to purchase or sell your rental investments.

If you're thinking of a change, or you want more advice on how the changes will affect you, don't hesitate to talk with us. +

Clarity around fixtures and fittings

Address these before the lease is signed

In December 2020, a commercial landlord and their tenant found themselves in the High Court arguing about who was responsible for replacing fixtures and fittings because their lease was silent on the issue.[1] These types of disputes around fixtures and fittings in commercial leases are quite common.

For both landlords and tenants negotiating a commercial lease, it is always best to turn your mind to your intentions for any fixtures and fittings attached to the premises; this will help enormously in avoiding costly disputes later on.

Issues to think about

Which items are the landlord's fixtures and fittings? Will a tenant's fixtures and fittings be added to the premises?
A lease may allow the tenant to make various alterations to the premises to ensure the fit-out meets its business needs. Whether certain fixtures or fittings belong to the landlord or the tenant often affects the rights and responsibilities around those items. It is critical that a clear schedule of landlord's fixtures and fittings (and the condition of those items) is included in the lease.

Who is responsible for maintaining and repairing the fixtures and fittings?
Under some leases, the landlord's fixtures and fittings are defined as being part of the premises. This means that the tenant's obligations around maintenance and repair of the premises include the maintenance and repair of fixtures and fittings. However, this is not always the case and you should make sure that the lease otherwise addresses who holds these obligations.

Who is responsible for replacing broken or worn out fixtures and fittings?
In the *Ventura* case, the lease was silent about who was responsible for replacing fixtures and fittings during the lease. The High Court determined that, on the wording of the lease, Ventura could decide whether to replace any fixtures and fittings if required for its business and either remove or allow its landlord to purchase these items at the end of its lease.

If it is intended that either the tenant or landlord must replace any fixtures and fittings where necessary, this should be clearly expressed in the lease.

What happens with the tenant's fixtures at the end of the lease?
Ordinarily, fixtures are considered to be part of the building, and ownership will pass to the landlord at the end of the lease (subject to any requirements that the tenant reinstate the premises to their original condition).

However, if a lease does not specify otherwise, the default rules in section 266 of the Property Law Act 2007 allow a tenant to remove their trade, ornamental or agricultural fixtures at the end of the lease. These fixtures can be removed before, or a reasonable time after, the end of the lease as long as there is minimal removal damage and the tenant repairs (or compensates the landlord for) that damage.

Commercial landlords should make sure their leases provide specific direction on a tenant's fixtures if, for example:

1. The removal of the fixtures and repair of any damage must occur before the end of the lease or within a set timeframe following the end of the lease to avoid, for example, the landlord being unable to re-let the premises while the reinstatement is still ongoing, or
2. The tenant is required to leave certain fixtures in place and transfer ownership to the landlord at the end of the lease.

Lease assignment

When a tenant assigns the lease, a new tenant may want to change which of the previous tenant's fixtures they will need to remove at the end of the lease. If this is not done, you may be able to require the new tenant to meet the cost of removing all tenants' fixtures and fittings – even those installed by the previous tenant. Before agreeing to reduce the new tenant's responsibilities, you will need to consider carefully how you want the premises to be left at the end of the lease and who should bear the cost of removing any unwanted fixtures and fittings.

Replacing an expired lease

When replacing an expired lease, both landlords and tenants should ensure that the records of the tenant's fixtures are up-to-date and included in the new lease. Otherwise, there could be a dispute about whether those fixtures became the landlord's property at the end of the expired lease.

Take care

The points in this article are just some of the matters to consider around fixtures and fittings in a commercial lease. If you are entering into a commercial lease, we can advise you in more detail and tailor your lease's terms to match your intentions for the fixtures and fittings in the property. +

1 *Ventura Ltd v Robinson* [2021] NZHC 932.

Property briefs

Government housing package: other notable points

The big ticket items of the government's recent housing package included the extension to the bright-line test as well as landlords no longer being able to offset their tax with interest paid on their rentals. We have covered these two items here.

There are, however, a number of other features of the package that may make it easier for New Zealanders trying to get onto the property ladder and to help increase the housing supply.

Increases to income and price thresholds for First Home Grant

Since 1 April 2021, more New Zealanders can qualify for government assistance to buy their first home. Income thresholds for singles applying for the First Home Grant have increased from $85,000 pa to $95,000 pa as well as an increase for a couple's combined income from $130,000 pa to $150,000 pa.

Similarly, the price thresholds for both new homes and existing homes in many areas of the country have also been increased. With the rapid rise in house prices leaving the scheme's original house price caps desperately out of kilter from the real-time housing market, first home buyers have suffered. Some had to rely on parents for additional funding or others have been completely priced out of their local housing market where prices had risen well above the threshold for government assistance.

The increases vary between regions and differ depending on whether you are looking to buy a new or existing home. There is a full list of the changes to the house price thresholds in your region here. With more people now being eligible to apply for the First Home Grant to subsidise the purchase of their first home, we hope that more Kiwis will get the assistance they need to help get them on the property ladder.

Housing Acceleration Fund

Property developers will also get a helping hand from the government's housing package. A $3.8 billion boost to development has been announced and will subsidise the cost of providing services and infrastructure to 'build-ready' land. In subsidising these significant upfront costs which often slow housing development, the government hopes to increase the supply of a range of affordable, public and mixed housing.

The Housing Acceleration Fund is available to a range of key stakeholders in both the private and public sector but it will rely on local government playing its part in opening up suitable land to allow more housing development projects to take place. Developers involved in housing development should speak to their local council first for more information about whether they are eligible for assistance from the fund or for what stages of housing development the fund is available.

Kāinga Ora Land Acquisition

The government continues to support affordable housing by lending Kāinga Ora an additional $2 billion to assist with land acquisition for social housing development projects. The increased capital is expected to see the rate of acquisition of land increase which, along with the funding boost for development of public and mixed housing, aims to increase the supply of housing across the country.

Apprenticeship Boost

Finally, the apprenticeship subsidy scheme (Apprenticeship Boost) is extended for a further four months. Employers taking on apprentices can access a $1,000 per week wage subsidy for first year apprentices and $500 for second year. This extension will help ensure that enough skilled tradespeople are trained to take advantage of the government's plans to increase housing supply by not only enabling a greater workforce to achieve the government's affordable housing goals, but also by providing private developers with a sufficient pool of skilled workers to draw on to keep up with housing demand.

Whether you are a first home buyer trying to find your feet in the property market, a property developer looking for a financial boost to kick-start your latest housing development project or an employer with apprentices, the government's housing package will help address the supply issues affecting the housing market and will give a financial leg-up for those working to increase supply. +

The next edition of *Property Speaking* will be published in **early Summer.**

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