



Has your rental property been damaged or destroyed by a natural disaster?

The impacts of a natural disaster may affect the types of expenses you can claim and the income you need to report for your rental property.

The issues you may need to consider include:

- claiming expenses for repairs
- replacement of capital items such as a kitchen or bathroom
- rebuilding costs and capital gains tax (CGT) implications where a property is destroyed
- taxation treatment of insurance compensation payments
- keeping records.

Claiming expenses for repairs

When we say 'repairs', we mean work to make good or remedy defects in, damage to or deterioration of the property, for example:

- replacing part of the guttering or windows damaged in a cyclone
- replacing part of a fence damaged by a bushfire
- replacing the plaster board in a wall damaged by flood inundation
- repairing electrical wiring or machinery damaged by a flood.

Can you claim a deduction while your property is being repaired even though it is unoccupied?

Yes you can claim deductions for a property where it is tenanted or genuinely available for rent. A property may not be able to be rented out at a particular time due to the need for repairs to make it habitable again. A claim for repairs will be an allowable deduction provided:

- your property was rented out immediately prior to the repairs being needed
- the damage being repaired occurred during the rental period.

Example 1

Ben's rental property was tenanted at the time it was severely damaged by a cyclone. Due to the damage, the tenants had to move out to other accommodation. Ben carried out repairs and he then readvertised the property for rent. Even though the property was not available for rent while being repaired, Ben is able to claim his repairs.

Replacing capital items

Can you claim the cost of completely replacing something?

If you have to replace something identifiable as a separate item of capital equipment (such as a complete fence or building, a stove, kitchen cupboards or a refrigerator) you have not carried out a repair. This means you cannot claim the entire replacement cost you incurred in the year you incurred it. However, you may be able to claim the cost, spread over a number of income years, as a **capital works deduction** or a **deduction for decline in value**.

If you have replaced a depreciating asset costing \$300 or less, you may be able claim an **immediate deduction**.

Example 2

Janet has owned and rented out a residential property since 12 January 1983. She replaced the old kitchen fixtures, including the cupboards and appliances. The old cupboards were damaged beyond repair due to water inundation caused by flood.

The kitchen cupboards are separately identifiable capital items with their own function. This means the cost of completely replacing them is a capital cost. Because of this, Janet can only claim a:

- capital works deduction for the construction cost of this work
- deduction for the decline in value of the kitchen appliances.

This is the case regardless of whether or not any of the following apply:

- the new fittings are of a similar size, design and quality as the originals
- the new cupboards are made from a modern equivalent of the material used in the originals
- the layout and design of the new kitchen may be substantially the same as the original.

Can you claim the cost of improvements?

When we say 'improvement' we mean work that:

- provides something new
- generally furthers the income-producing ability or expected life of the property
- generally changes the character of the item you have improved
- goes beyond just restoring the efficient functioning of the property.

You cannot claim a deduction for the total cost of improvements to your rental property in the year you incur them. However, you may be able to claim the cost, spread over a number of income years, as a capital works deduction or a deduction for decline in value.

Example 3

Tim replaced a fibro wall inside his rental property, which was damaged by a flood, with a brick feature wall.

The new wall is an improvement because Tim did more than just restore the efficient function of the wall. This means Tim cannot claim the cost of the new wall as a repair but he can claim the cost as a capital works deduction.

However, had Tim replaced the fibro with a current equivalent such as plasterboard, he could have claimed his costs as a repair. This is because it would have merely restored the efficient function of the wall without changing its character, even though a different material was used.

Can you claim improvements you carry out at the same time as repairs?

If you conduct a project that includes both repairs and improvements to your property, you can only claim a deduction for the cost of your repairs if you can separate the cost of the repairs from the cost of the improvements.

If you hire a builder or other professional to carry out these works for you, we recommend you ask for an itemised invoice to help work out your claim.

Example 4

Lyn's rental property was partially inundated with water due to flood. Lyn noticed damage to the vanity unit in the bathroom when cleaning the floor. Lyn was advised that the vanity unit could be fixed up but needed to be dismantled. Lyn decided to re-tile the bathroom (as the colour was a bit dated) whilst the chipboard in the sides and bottom of the vanity unit was being replaced.

The new chipboard for the vanity unit is considered a repair as it does no more than just restore the function of the vanity unit. The re-tiling is not a repair. Lyn would need to know the cost of each component of the work so she could claim her repair and her capital works deductions correctly.

Repairs to depreciable items

A repair to depreciable items is an allowable deduction. The replacement of the depreciable items with new depreciable items is not a repair.

Example 5

Caitlin's rental property was partially inundated with water due to flood. Caitlin needed to replace the carpet in the lounge room and one of the bedrooms. Caitlin decided to replace the carpet throughout the property.

If Caitlin had just repaired the damaged carpet she would have been allowed a deduction for the repair. As the whole carpet was replaced, Caitlin may be able to claim a deduction for the adjustable value of the carpet that was disposed of and a deduction for the decline in value of the new carpet.

Where a property is destroyed

Can you claim the cost of rebuilding your rental property destroyed by a cyclone?

The costs of rebuilding a rental property are not immediately deductible.

If your rental property was destroyed by a natural disaster, any costs to rebuild are capital and not immediately deductible.

However, you may be able to claim a deduction for the rebuilding costs of your property over a forty-year period. This is called a capital works deduction.

What are the CGT implications where a rental property is destroyed?

If a CGT asset you own is lost or destroyed, the CGT event happens when you first receive compensation for the loss or destruction. If you do not receive any compensation, the CGT event happens when the loss is discovered or the destruction occurred. A capital gain may be able to be deferred - see [Guide to capital gains tax](#).

Example 6

Laurie owned a rental property that was destroyed by cyclone in February 2011. He received a payment under an insurance policy in April 2011. The CGT event happened in April 2011.

Example 7

Marie owned a rental property that was damaged by flood in January 2011. Her local council deemed this property uninhabitable. She received a payment under an insurance policy in September 2011. The CGT event happened in September 2011.

Example 8

Christine owned a rental property that was damaged by flood in January 2011. Her local council deemed this property uninhabitable in May 2011. The property was demolished in October 2011. She did not receive any compensation. The CGT event is January 2011.

What are the capital works implications where a rental property is destroyed?

If you have been claiming a capital works deduction for a rental property, you can claim a deduction for the remaining amount of construction expenditure that has not yet been deducted, less any compensation you receive or are entitled to receive. This applies even if the destruction or demolition is voluntary.

You can claim the deduction in the income year in which the destruction occurs.

The deduction is reduced if the capital works are used in an income year only partly for the purpose of producing assessable income.

Insurance payments

What is the taxation treatment of insurance compensation payments?

If you receive income other than rent for your rental property (for example, an insurance payout for lost rent), you must include this amount as income on your tax return.

If the insurance payment is for a loss of a depreciating asset, then you need to work out the balancing adjustment amount and include it in your tax return.

If the insurance payment is for the loss of a CGT asset, then you need to work out your capital gain or loss and include it in your tax return, unless you are eligible to defer the capital gain. A capital loss must be offset against a capital gain. If you have been claiming a capital works deduction for the asset, then see 'What are the capital works implications where a rental property is destroyed?' above.

What records do you need to keep?

You need to keep proper records in order to make a claim, even if you use a tax agent to prepare your tax return or you do it yourself. You must keep records of:

- the rental income you receive and the deductible expenses you pay - keep these records for five years from 31 October or, if you lodge later, for five years from the date your tax return is lodged
- your ownership of the property and all costs of purchasing or acquiring it and selling or disposal of it - keep these records for five years from the date you sell or dispose of your rental property.



As capital gains tax may apply if you sell your rental property, we recommend you keep records of every transaction over the period of ownership of the property. This would include contracts of purchase and sale, and conveyance and loan documentation.

Keeping these records will help you work out your capital gain or loss correctly and ensure you do not pay more tax than you need to.



For information about easy ways to keep your records, visit [Capital gains tax essentials](#) and read 'Acquiring CGT assets and keeping records' in the [Introduction to capital gains tax](#).

More information

For more information about rental property expenses you can claim, visit www.ato.gov.au/rental

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