

Ask the experts

From property clubs and buying off the plan to depreciation, our experts have got all your questions answered

Q A friend of ours is talking about property investment through an investment club – which apparently builds or sources properties, and provides the finance and ongoing management of properties. I'm curious about this and wonder whether these clubs are genuine and how safe they are.

A As Australia presently has no regulation in the property investment industry, there are many schemes and strategies that have popped up, which could breach a law, if there was one. Hopefully, this situation will soon change, with the PIAA (Property Investment Association

of Australia) leading the push for nationwide regulation to protect all property investors. Until this happens, investors must be wary of any group selling property that uses clever marketing strategies such as these.

Investment clubs have begun to spring up around the country, using a carefully cultivated approach that trades on the Aussie need to congregate and be 'mates'. On the surface, these clubs appear to be a group of your peers, working voluntarily for the good of all members to provide education and guidance to allow for successful wealth creation. In some cases, however, this is just a cover for an intricate network of seasoned con artists, who use the club as a front for their own moneymaking ventures, and a fence to sell overpriced and overvalued real estate to the unsuspecting public.

Typically, the marketing material advertises freedom, friendship and financial success through group support. Help is reportedly available, free of charge, any time you need it. There are usually group meetings where fellow investors help each other. And in all fairness, in some of these clubs many of the members offering this support are in fact genuine in their concern – they themselves are unaware of the dishonest network of money-hungry opportunists who lurk in the shadows.

In fact, money is made for the stakeholders (not the investors, or 'members') through a comprehensive commission structure, usually involving 6% added to the purchase price. Although this might seem palatable, evidence has suggested to me that a lot of these properties already have a substantial amount of developer profit built into the price before the 6% is added.

I have known of investors who have had properties that they bought via these clubs independently valued, at which point they have discovered

that they were worth at least 20% less than what was actually paid for them – suggesting that the real profit for the club owners is vast and undisclosed.

Investors needing to exit early, or wanting to leverage against equity into more property, during times of stabilised property values, found themselves with an asset worth considerably less than what is owing on it.

While these clubs may seem 'free' and independent, I caution you to question the impartiality of any wealth creation group that charges a 'commission' on the sale of the properties it recommends. Don't be taken in by the welcome grin. They are not what they seem, their advice is subjective and they profit from every purchase you make, both through profit on the sale and commissions way above acceptable levels.

Q I'm interested in buying property off the plan, but I've heard horror stories about investors who have lost money during the construction phase. Do you think off-the-plan properties make a good investment?

A Buying off the plan is when the house or apartment has not been built yet, or is currently under construction. In my investing career, I have purchased several properties off the plan that have been very successful each time. While there are many benefits to following this buying strategy, there are some risks too.

Benefits

- Lower or alternative deposits – meaning you can use a lower cash deposit, a bank guarantee or a deposit bond
- Maximum tax advantages
- Stamp duty savings in some states
- Redesign possibilities
- Long settlement, which allows potential for capital growth

- If settlement is longer than 12 months, then often a revaluation at the current market price can allow 100% finance.
- Opportunity to on sell the property prior to settlement

Risks

- Project may not proceed at all
- The finished product may not be what you expected
- Expected capital growth may not eventuate, or may fall
- Developer may go into liquidation, which stalls the project and ties up your deposit

To protect myself from a developer going into liquidation, I never authorise a developer to use my deposit for the construction. I prefer to have the deposit sitting in the solicitor's trust account; this way, I have more chance of getting it back should things go wrong.

Also, as an investor I always have my solicitor review the contract. However, I have found that sometimes he/she can miss things, so as a rule I generally review my own contracts in addition to the solicitor doing so.

The items that I may expect to see as part of the contract for purchasing off the plan include floor plans, building plans, site plans and electrical plans.

Also, a detailed outline of fixtures and fittings – including the standard of quality – should be included. Some areas to watch out for are:

- Kitchen cupboard construction
- Exhaust fans in kitchen and bathrooms
- Heating and cooling
- Floor coverings – type and quality
- Wall finishes – type and quality
- Window dressings
- Garage door – remote or manual
- Letter box
- Clothes line
- Appliances (white or stainless steel) model, standard or its equivalent
- Fly screens
- Security doors
- Lighting and electrical layouts
- Extent of garden beds and lawns

I once had an experience whereby a contract for an off-the-plan property I purchased in NSW had a list of inclusions that included a dishwasher,

under-sink water filter and power points in the kitchen.

Being from Melbourne, I flew up to Sydney for the final inspection before settlement, and we noticed that these items were missing, but I didn't have the contract with me to confirm. When I raised this with the builder at the time, he refused to correct any of the above, claiming they were not part of the contract.

Upon returning home I double checked the contract, which stipulated that these items were included. Therefore, the builder was legally obliged to provide these.

My lesson here was to always take the contract with me during final inspection prior to settlement, and to double check that all the inclusions are actually in the property.

Q I own two apartments as investment properties. They are in the same block, which was constructed in 1989. Is it worthwhile getting a depreciation schedule done for these properties? They've never been renovated, but I'm planning on redoing the kitchen and bathroom in the next few years – so would I be better off waiting to get a depreciation schedule done post-renovation?

A In this scenario, you can claim both against Division 43 (building allowance) and you can also claim against Division 40 (plant items).

The building allowance covers the actual construction cost of the building, and is depreciated at a rate of 2.5% per year for 40 years. So even if your property is already 19 years old, you still have a further 21 years of building allowance deductions available to you.

Had the apartments been built prior to 18 July 1985, the building allowance would not have been available.

Plant items include such things as carpets, drapes, stoves, heaters and hot water services. These items are depreciated according to their effective life, which is often between six and 15 years.

In answering this question, we make the assumption these apartments have been owned by you for a number



of years. The depreciation schedules of existing property can be used immediately, and may be used to verify up to four years of depreciation if it has not been claimed up until now.

If this is the case, it is definitely worthwhile having the depreciation schedules done now, particularly in light of the fact that renovations are intended.

When the renovations are completed, all new items can be adjusted to reflect the costs of additional works. Costs for new works, and in particular new plant items such as stoves and ovens (new kitchen), can be claimed from the time of installation. This way, you can claim the old and the new.

At the time of completion, a revision to the schedule can be made for a small tax-deductible fee, based on expenditure of the renovations. Make sure you keep all receipts!

A tip for bathroom and kitchen renovations: vinyl flooring is considered a plant item and thus is depreciable, whereas tiles are not depreciable. ■

Got a property question you need answered? E-mail your questions to editor@yipmag.com.au

The experts



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