Buying and selling residential property

What you need to know about your tax obligations

Inland Revenue
Te Tari Taake

www.ird.govt.nz

This guide will help you to understand whether you should be paying tax when you sell a property and tells you about your responsibilities. It will help you decide whether you need to get more information or professional advice.

This guide is primarily aimed at individuals. Builders, developers, dealers, etc should talk to their tax professional as different rules may apply.

Contents

Do I have to pay tax on property I sell?

It depends on your reason or intention at the time you bought the property.

When deciding whether or not you should pay tax on the profit from the sale of a property, we look at your intention when you bought it.

If you bought the property with the firm intention of selling it when prices rise—to make a gain from the increase in the property's value—the profit is likely to be taxable.

However, if you bought the property to provide a home for your family, any profit from the eventual resale will most likely not be taxable, unless you have a history of regularly buying and selling properties.

A good test is to ask yourself "what were my reasons for buying this property?"

Case study 1

Chris knows Tom is looking for a property in Avondale. Chris has a friend in real estate with a property Chris knows Tom will like. Chris buys the property with the hope of selling it to Tom at a profit.

Chris bought the property with the intention of reselling it and making a gain and must pay tax on any profit he makes.

Case study 2

Bob knows there's a shortage of houses for sale in Green Bay. Bob buys a property in the area. His immediate goal is to build a granny flat on the property and rents both properties to pay off some of the building costs. He later plans to sell both properties at a profit.

Bob bought the property with the intention of improving it and then selling it. His rental income is taxable and he must pay tax on any profit he makes from the sale of the property.

Case study 3

Lance is a university student. He decides to buy one of the properties he's heard advertised on the radio for "...only a $1,000 deposit down". He borrows the $1,000 as he thinks he can sell the property at a bit of a profit before the title is issued, and before he needs to pay the balance.

Any profit Lance makes is taxable as his only intention was to make a profit.

Why is my reason for buying a property important?

If one of your reasons for buying a property is to resell it any profits are taxable.

It's a fact that nearly everyone buying a property will sell it at some stage in the future and most people hope their property will gain in value. However, this alone isn't enough to make any profits taxable.

It's only when one of your specific reasons for buying a property is to resell it that any profit you make from the sale is taxable.

We need to work out your intentions when you bought property so we can decide whether any profits you make on its sale will be taxable.

Normally, living in a house means that any profits on its eventual sale are likely to be non-taxable, unless you have a history of regularly buying and selling properties.

We make all our decisions on a case-by-case basis.

Case study 4

Moana buys a property with the intention of providing a home for herself and her children. When she eventually sells it she hopes to make a gain and leave her children a legacy.

In a year's time she gets a new job and decides to sell the property to move closer to her new job. Property prices have risen, so Moana gains from the sale and can buy a bigger home.

The profit from the sale of Moana's property is not taxable as her intention was always to provide a home for her family.

Case study 5

Sue buys a property with the intention of selling it for a higher price when the time is right. She and her family will live in it in the meantime. Sue has a regular pattern of buying and selling properties while living in them. Six years later, house prices in Sue's area have risen to a level where she could make a good profit on the sale of her property.

The sale of Sue's property is taxable as her intention was always to sell it, and she has a history of regularly buying and selling properties.

In these examples we've assumed that Moana and Sue's stated intentions are genuine and don't change over time.

What if I had more than one reason for buying a property?

You can have more than one reason for buying a property and for selling one.

In principle, we take into account all of your reasons for buying a property.

Case study 6

Joe and Gail buy a second property as a rental. They also hope, in the long term the property could be sold for a profit.

Joe and Gail's reason for buying the property is for rental income—the hope of a higher resale value was not a reason for the purchase. In this case, the rental income and recovery of any depreciation they've claimed against the property is taxable. Any profit from the eventual sale of the property is unlikely to be taxable.

Case study 7

Frances and Bruce buy a second property in the hope that it will quickly gain in value. They decide to rent it out in the meantime.

One of Frances and Bruce's reasons for buying the property is to make a gain from any increase in its value when they sell it, so they must account for the profit in their tax returns.

Case study 8

Bill and Dean buy rundown properties that need minor work to get them into a saleable condition. They aim to make a profit on their sales. They also live in the houses while they work on them and don't own another home.

Although Bill and Dean use each of the houses as a home, their main reason for buying the properties is to resell them at a higher price. They must pay tax on the profits because they have a history of regularly buying and selling properties.

Case study 9

Mark and Jan buy a property as a family home. They are keen on DIY and do a lot of work on the house to make it more comfortable and hope this will increase its eventual resale value. Then Mark gets a job in another city and they sell their home at a substantial gain.

Although Mark and Jan worked on the property they had no real intention of reselling it when they bought it. As a family home, the profit made on the house is not taxable.

Please note that the buyers' intentions in these examples seem quite clear but there may be other factors in each case which we need to consider. For example, if Mark and Jan had bought and sold houses regularly and this one just happened to coincide with a job change, the situation might be different.

What if I change my mind after I buy a property?

This can happen. It's your intention when buying the property that matters. And we do realise that your intentions might change over time.

For example, you might buy a property with the intention of selling it later at a higher price, but then you decide you like the area and want to stay there. However, any profit you make when you eventually sell the property would most likely be taxable as your original intention was to make a profit from the sale.

On the other hand, you might buy a family home and then your circumstances change. In this situation it's unlikely that you'll be taxed on any profit you make.

As long as you aren't in the business of trading in or developing property, or constructing buildings, it's your intention at the time you buy the property that counts.

If your reasons for buying a property have changed over time, we strongly recommend you consult a tax advisor so you can work out your tax obligations.

How do you work out what my intention or reason for buying a property was?

We work out your intentions by listening to what you tell us and looking at your actions. We may look at your history in buying and selling properties. For example, have you bought and sold a number of properties over a period of time, or bought and sold properties at regular intervals? We might look at statements you made to a bank manager or advisor when you bought the property, and at any plans made or discussed at the time.

For example:

- What did you arrange and discuss with your bank?
- What did you discuss with your real estate agent/s?
- If you rent out the property, how long have you rented it out for?
- Did you draw up any plans for the property?
- What notes were made on council documents?
- What telephone, power and other utility arrangements did you make?
- What was your actual or planned involvement in the community, eg attendance at schools, membership of clubs etc?
- What were the terms of the financial arrangements?
- Is the property providing you with a living?

The actions you take before and after the purchase can also help us to determine your intent.

In some cases, a buyer's intention will be fairly black and white. However, in other cases there will be grey areas. If you're unsure about whether you should pay tax on a property you've sold, please talk to us or your tax advisor.

We work out your intentions by listening to what you tell us and looking at your actions.

What about my family home?

Whether we consider a property to be your home or not depends on how you use the property. It doesn't depend on what type of property you own.

Case study 10

Mary lives in a property A. She bought it intending to provide a home for her family. She is enrolled at the local gym, is a member of the local video store and her children attend preschool nearby. She knows her property is worth far more than when she bought it, but is happy in the area and has never put the property up for sale.

Mary also owns two other houses (property B and property C) which she purchased to on-sell. These are in different areas from her family home, and in-between tenancies she stays in them for security reasons.

Noisy neighbours move in next door to Mary at property A. She calls noise control a number of times but the noise gets worse and Mary eventually decides to sell her home.

As property A was clearly bought by Mary as her family home any profit she makes would not be taxable. Mary should pay tax on any profit she makes from selling properties B and C.

Case study 11

Ross lives in a property A, which he bought with the intention of reselling it when it increased in value. Ross has a history of regularly buying and selling properties. He has taken out a six-month membership at the local gym, is a member of the local video store, and his children attend preschool in another suburb. He knows his property is worth far more than when he bought it. He likes living in the area but intends to put the property up for sale as soon as the market is right.

Ross also owns two other houses (property B and property C) which were purchased to on-sell. These are in different areas and in-between tenancies he stays in them for security reasons.

The market picks up and Ross decides to sell his home.

Despite the fact Ross lived in property A as his family home, he bought it with the intention of re-sale, and has a history of regularly doing so. He should pay tax on it.

Profits from the sale of your family home are generally not taxable.

Does it matter how long I own a property for?

It's commonly thought that if you hold a property for long enough the profit made isn't taxable. This isn't true—there's no time limit as your intention or reason for buying the property is what counts.

There's no time limit as your intention or reason for buying the property is what counts.

If a property owner or an associate is involved in the business of dealing in land, building and construction work, or in a business or an undertaking involving developing or subdividing land, the time the property has been owned before its sale becomes an important consideration for tax purposes.

If sold within 10 years, a property may be taxable even though it wasn't bought with the intention of resale.

If any of these circumstances relate to you, we strongly recommend you consult a tax advisor so you can work out your tax obligations.

Does this mean I can't shift house when I need to?

No. Lots of factors influence decisions about buying and selling properties.

Changing your job, children changing schools or changes in the neighbourhood are all good reasons for selling a property.

However, if you buy and subsequently sell a number of properties at a profit, giving little or no consideration to the personal inconvenience of shifting, and if there are no outside factors influencing your shift, we may question your reasons for the initial purchases.

What type of tax will I have to pay?

Income tax

As an individual buying and selling property or as a partner in a partnership, each year you'll need to send us an *Individual tax return (IR 3)*, or an *Individual tax return—non-resident (IR 3NR)* if you live overseas.

In this return you'll need to include enough information to show how you worked out the amount of property income you've calculated after deducting expenses.

The profit is added to any other income you've earned to calculate your total taxable income.

You can then work out the tax on your total taxable income. Tax credits, such as PAYE, are deducted from the tax on your total taxable income.

Most people will have a tax year that ends at 31 March each year. Any tax to pay is due by 7 February the following year.

If you don't already send us a tax return each year, please call us on 0800 227 774 and we'll send you a tax return at the end of the year. If you're calling from overseas, please call us on 64 4 978 0779.

Provisional tax

As a buyer and seller of properties it's likely your tax to pay will be more than $2,500, so you'll have to pay provisional tax.

Provisional tax is not a separate tax—it's another way of paying your tax as you earn your income. You usually pay three instalments of provisional tax throughout the year to cover your expected end-of-year income tax.

For more detailed information read our booklet *Provisional tax (IR 289)*.

If more than one person is involved in buying and selling property

If you're in a partnership of two or more people, you'll need to get an IRD number by completing an *IRD number application—non-individual (IR 596)* form. The partnership will only need to keep one set of accounts to record its income and expenses and file an IR 7 tax return each year.

This return will show how the income was calculated and the amount of each partner's share.

Where a couple (such as a husband and wife, civil union or de facto) is involved in buying and selling property, you don't need a partnership IRD number or IR 7. Each partner includes a copy of the accounts in their individual tax returns.

Goods and services tax (GST)

Goods and services tax (GST) is a tax on the supply of most goods and services in New Zealand. GST can apply to people who buy and sell property/ies. You must register for GST if your annual turnover in the previous 12 months was more than $40,000 (or is likely to be in the next 12 months). Turnover is the total value of taxable supplies made for all your taxable activities, excluding GST.

Case study 12

Tony regularly buys rundown houses with the intention of renovating them in his spare time and selling at a profit. He also owns his own family home.

Tony is clearly involved in a taxable activity with taxable supplies exceeding $40,000 so he must register for GST and account for GST inputs and outputs.

If your property dealings fall within the guidelines for GST registration you must register. For detailed information read our booklets *GST—do you need to register? (IR 365)* and *GST Guide (IR 375)*.

Putting your tax affairs right

You have an obligation to assess your own tax liability and pay the tax you owe. To do this you'll need to know your basic tax obligations.

You must:

- correctly calculate the amount of tax you have to pay (unless you don't have to file a return)
- when required, deduct or withhold the correct amount of tax from payments or receipts
- pay tax on time
- keep all necessary information (including books and records) and maintain all necessary accounts or balances
- disclose all information Inland Revenue requires in a timely and useful way
- cooperate with Inland Revenue as required by the Inland Revenue Acts
- correctly respond to a personal tax summary, if you receive one
- advise Inland Revenue if you should have received a personal tax summary but have not yet received one
- comply with other specific tax obligations.

An example of not meeting your obligations is entering false information in a tax return or knowingly not showing all your income.

If you tell us about your tax situation, any penalties will be much lighter than if you wait for us to find out.

If you've made a mistake or filed an incorrect tax return, it's best to tell us about it before we find out some other way.

Voluntary disclosures

A voluntary disclosure is when you tell us what's wrong with your tax return/s before we find out some other way.

If you think you should have paid tax on the sale of a property but didn't, you should consider making a voluntary disclosure. Penalties are significantly reduced if you come forward before we contact you. This applies to all disclosures, not just property ones.

Anyone can make a voluntary disclosure at any time:

- by completing a *Voluntary disclosure (IR 281P)* form
- by calling us
- by letter, fax or email
- by visiting one of our offices
- during an interview.

For more information about voluntary disclosures please read *Putting your tax returns right (IR 280).*

Useful information

www.ird.govt.nz

Visit our website for services and information. Go to:

Get it done online to file returns, register for services and access account information

Work it out to calculate tax, entitlements, repayments and due dates and to convert overseas income to New Zealand currency.

How to get our forms and guides

You can view copies of all our forms and guides mentioned in this booklet by going to **www.ird.govt.nz** and selecting "Forms and guides" or you can order copies by calling INFOexpress.

INFOexpress

INFOexpress is our automated phone service. You can order stationery (forms and guides) and request personal tax summaries.

Remember to have your IRD number handy when you call.

You can call INFOexpress on **0800 257 773** for copies of our forms and guides between 6 am and 12 midnight, seven days a week.

How to contact us

We're available from 8 am to 8 pm Monday to Friday and 9 am to 1 pm Saturday on the following numbers. Remember to have your IRD number handy.

Income tax and general enquiries
0800 227 774

Overdue tax and returns
0800 227 771

Call recording

As part of our commitment to providing the best possible service to our customers, we record all phone calls answered in, and made by, our permanent call centres. For further information about our call recording policy and how you can access your recorded information, please go to **www.ird.govt.nz** or call us on 0800 227 773 or 0800 377 774 (if you or your partner are in business).

Privacy

Meeting your tax obligations involves giving accurate information to Inland Revenue. We ask you for information so we can assess your liabilities and entitlements under the Acts we administer.

You must, by law, give us this information. Penalties may apply if you do not.

We may exchange information about you with the Ministry of Social Development, Ministry of Justice, Department of Labour, Ministry of Education, New Zealand Customs Service, Accident Compensation Corporation or their contracted agencies. Information may be provided to overseas countries with which New Zealand has an information supply agreement. Inland Revenue also has an agreement to supply information to Statistics New Zealand for statistical purposes only.

You may ask to see the personal information we hold about you by calling us on 0800 377 774. Unless we have a lawful reason for withholding the information, we will show it to you and correct any errors.

Property means...

land (including a bare section), buildings and rights or options, eg for "off the plan" properties. Please note that the ownership structure of the property doesn't matter. Whether it's owned by an individual, by a trust or by a loss attributing qualifying company—the rules are still the same.