



# Granny flats: Beware of the CGT consequences

Granny flats are becoming more of a common feature of the urban environment. No doubt this is due to the ongoing and unremitting nature of the housing affordability crisis, and the relaxing of regulations about where and how they can be built.

And they do seem to offer a very viable solution to the problem – at least in the short term.

However, if you are thinking of constructing one, or already have one in place, you need to be aware of all the tax implications – and they can be very significant.

Firstly, if you rent it at commercial or arm's length rates, then not only will you be assessable on the rent (albeit being able to claim a portion of the deductions), but you will lose a part of the capital gains tax (CGT) exemption on your home. This is because you are using your home to produce income.

But in most cases, this partial CGT liability should be taxed concessionally by giving you a market value cost (at the time you first rent it) from which to calculate the gain (or loss).

Furthermore, the CGT 50% discount (or whatever is in place after the May Budget) should, in most cases, be available to reduce the amount of your assessable income.

However, where you do not rent your granny flat at commercial rates (including where the occupants may only pay their share of outgoings, such as electricity and rates) then you will not lose any CGT exemption on the home.

This will typically be the case where your granny flat is occupied by a relative, such as an adult child – or by a granny (and/or granddad), themselves!

It should also be noted that it is becoming common for the owner of the home (young adult children) to come to some sort of agreement with a parent or parents, whereby the parent/s agree to pay the price for building the granny flat in exchange for the “right to occupy” for a number of years. Likewise, such agreements may bring to an end a right to occupy.

The making of an agreement whereby “granny-flat” rights are created in another party (or bought to an end) can technically have immediate CGT consequences – despite the fact that it is made in relation to the CGT-exempt home and among family members.

However, the CGT rules provide that this will not be the case where the person acquiring the granny flat right has reached pensionable age (or has a relevant disability) and the arrangement is in writing and is not of a “commercial” nature.

These and other granny flat arrangements require good professional advice – particularly in terms of determining if such an agreement is “commercial”.

**i** So, if you currently own a granny flat or you are thinking of constructing one for any purpose, it is important to come and speak to us – especially in terms of preserving the CGT exemption on your home (or at least maximising it). 💰

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