

# NRAS: \$100,000 tax-free cash for property investors



**In our November issue, we looked at the basics of investing in NRAS properties. This month, Flynn De Freitas examines this new and exciting class of cash flow positive properties and finds out if the marketing claims are true**

**T**ax free money for your next investment property? Is it possible? How about \$100,000 over the next ten years?

There's nothing like a financial crisis to encourage governments to give away bucket loads of cash, and Australia is no different. First it was the \$900 stimulus cheque and then the First Home Owners Grant boost. Now the federal government is unveiling the most generous cash handout – a \$100,000 tax-free cash give away!

Called the National Rental Affordability Scheme (NRAS), property investors can now receive annual, tax-free incentives courtesy of the government. Sound too good to be true? How much is it worth in 2010? A cool \$8,672!

Well of course there are conditions but they are pretty mild, and over

10,500 properties across Australia now qualify for NRAS incentives.

Before we look in detail into NRAS, let's first examine why the federal government is offering such unprecedented incentives.

## Government's aim with NRAS

The federal government announced in July 2008 that it would allocate \$623m to build 50,000 new dwellings as part of its affordable housing initiative.

Recognising the severity of Australia's housing shortage and the vital role investors play in providing new rental properties, the federal government decided to 'go hard and go early' with a generous, long-term scheme that would incentivise investors to provide rental properties at 20–25% below market rentals. The federal government wanted to provide

affordable rental accommodation for two broad classes of renters.

First, the so called 'critical infrastructure workers' such as teachers, nurses, fire fighters and police who had been priced out by rents in many areas they worked.

Second, the low income/welfare recipients who were being pushed further and further away from capital and regional centres due to rising rents.

Developers and not-for-profit organisations were invited to apply to round one of NRAS in July 2008, round two in December 2008 and the current round three.

Like all free money exercises, a stampede has occurred with more than 30,000 applications received in the first two rounds. After numerous delays, over 10,500 NRAS properties have been approved, with construction for these well underway.

The federal government has primarily intended to target developers, 'institutional' investors and not-for-profits/charities with the NRAS incentives to ensure better compliance and save on administration and red tape costs. However, the

door is open for individual property investors to benefit as well.

## The largest investor incentives in history

While Australian investors enjoy the benefits of negative gearing (ie, offsetting property losses against other income) and depreciation, these pale at an individual investor level in comparison to the government's NRAS incentives.

Investors holding NRAS qualifying properties are entitled to 10 years of annual 'tax free' incentives, starting at \$8,672 in 2010.

For investors with a marginal tax rate of 30%, this equates to \$12,388 in pre-tax dollars (ie, \$238/week rental top up). It's even better for investors on the top marginal tax rate of 47%, with NRAS equating to \$16,362 in pre-tax dollars (\$315/week).

Each year, the incentive increases according to the rental component of official inflation. With rentals increasing at their highest rate in 20 years, this means that the annual NRAS incentive increase for 2010 will be 8.4%.

In total, an NRAS investor will receive a total of approximately \$104,000 in tax-free incentives over 10 years. While incentives are calculated on a national basis, increases in rents are calculated based on the growth rate of market rents in the capital city of the state the property is located.

Not surprisingly, these incentives come with certain obligations to ensure they meet the government's stated goals of providing Australians with more affordable rental properties.

**Table 1: Overview of NRAS**

Investor perspective	Government aims
New property only	<ul style="list-style-type: none"> <li>• Stimulate economy through construction of new housing</li> <li>• Increase supply of rental properties to reduce pressure on rentals</li> </ul>
Rents discounted 20–25% off market rental	<ul style="list-style-type: none"> <li>• Provide 'critical infrastructure workers' (eg, teachers, nurses, police) with affordable rental properties</li> <li>• Provide more 'affordable' housing for welfare recipients</li> </ul>
10-year commitment to NRAS	<ul style="list-style-type: none"> <li>• Long-term program to provide affordable housing</li> </ul>
\$8,672 'tax free' annual incentive payment	<ul style="list-style-type: none"> <li>• Large incentive to attract sufficient number of investors to build 50,000 properties</li> </ul>
Annual payment increase at same rate as national rentals	<ul style="list-style-type: none"> <li>• Ensure investors not disadvantaged by rising market rentals over time</li> </ul>
Cumulative incentives likely to exceed \$100,000 over 10 years	

... a stampede has occurred with more than 30,000 applications received in the first two rounds... over 10,500 NRAS properties have been approved ...

## NRAS qualifying criteria

NRAS incentives are available only on select properties that meet its qualifying criteria, being:

- New property (including off-the-plan) only
- Rented to 'approved tenants' at 20–25% below market rentals (for the region)
- Managed by an 'approved manager', which is required to select tenants, set rents and manage the property
- The property is rented in NRAS for 10 years (except in certain circumstances)

The government intends to issue 50,000 NRAS licenses (10,500 issued to date) for properties that meet these criteria – meaning there will be a finite number of properties that investors can obtain NRAS incentives.

## Buying an NRAS property

While the federal government initially intended that NRAS properties be owned by large institutional investors (eg, corporate super funds), developers and not-for-profits/charities, there are ways in which individual investors can purchase an NRAS property.

The process involves the little known concept of 'non-entity joint venture partner'. This effectively means an individual investor enters into a joint venture with an institutional investor, charity or developer that qualifies for NRAS (JV Partner). Once a JV Partner applies and is granted an NRAS licence for a particular property, it can then sell this property to an investor. The investor purchases the property and then generally enters into two agreements. Firstly, a head lease with the JV Partner (who holds the licence) and, secondly, a management agreement with the approved manager. The

**Table 2: Forecast NRAS incentives**

Year	Incentive	Annual percentage increase
Year 1	\$8,672	8.4%
Year 2	\$9,019	4.0%
Year 3	\$9,380	4.0%
Year 4	\$9,755	4.0%
Year 5	\$10,145	4.0%
Year 6	\$10,551	4.0%
Year 7	\$10,973	4.0%
Year 8	\$11,412	4.0%
Year 9	\$11,868	4.0%
Year 10	\$12,343	4.0%
<b>Total</b>	<b>\$104,117</b>	

### 1. Aztec Developments

Aztec Developments (Qld) Pty Ltd is a family-based business experienced in the development of quality investment properties in areas of high growth.

"All NRAS properties are high quality homes, in desirable areas, designed to provide affordable housing for middle Australian families on good incomes but unable to acquire deposits or to afford a mortgage payment needed for a home ownership," says Jenny Hall of Aztec Developments.

"Rising rents and lower than average vacancy rates for rental properties particularly in the Caboolture Statistical Division means that tenants are finding it harder to find suitable affordable rental housing. The jump in sales prices of houses and townhouses in the area over the past few years have also meant that fewer people are able to enter the housing market and instead need to continue to rent rather than buy their own home. Therefore, affordable rental housing in the area will provide much needed relief for low to moderate income earners. Investors earning as low as \$50,000 a year can invest in NRAS properties and could earn a positive income of \$63 in the first year," she says.

For more information, please call (07) 5491 2717 or visit [www.aztecdevelopments.com.au](http://www.aztecdevelopments.com.au)

### 2. Awesome1 Investment Properties (A1IP)

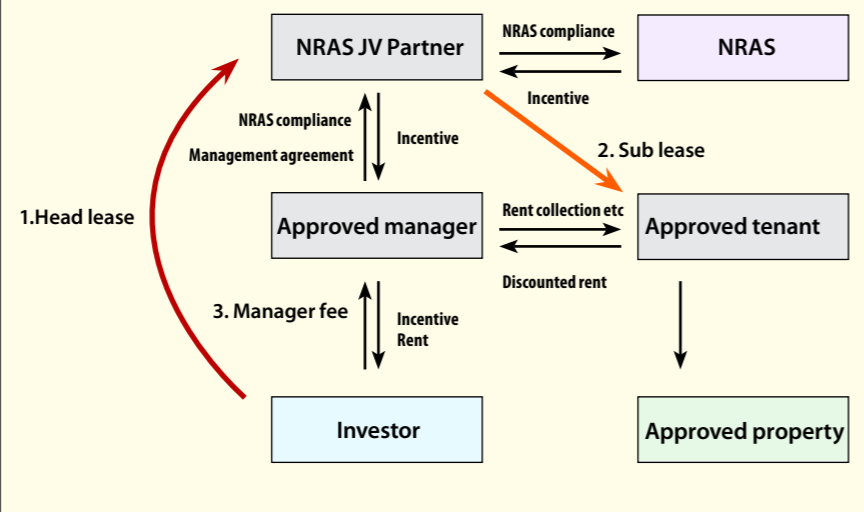
The Queensland-based property investment group specialises in sourcing NRAS properties in Queensland, NSW and Victoria.

CEO, Laura Castelli says that A1IP found that they preferred NRAS properties in the eastern states rather than Western Australia, given these properties are substantially cheaper.

"As the NRAS incentive is the same regardless of the price of the property, from a cash flow perspective, it's better to buy a cheaper property over a more expensive one. For example, the annual after tax, cash flow difference between a \$360,000 property and

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**Chart 1: Example investment structure for individual NRAS investor**



It is important that the whole process is correctly set up, so that you (as the investor) can 'tax free' receive the incentive

manager is responsible for selecting all tenants, managing the property, setting rents, and ensuring compliance with NRAS requirements and paper work.

The federal government then pays 75% of the NRAS incentive to the JV Partner, who then passes it on to the manager, who in turn passes it to the investor. Investors apply directly to the state government for the remaining 25% of the incentive (see Chart 1).

It is important that the whole process is correctly set up, so that you (as the investor) can 'tax free' receive the incentive. JV Partners will have applied to the Australian Taxation Office for a 'private binding ruling', which investors should ask for and have their accountant check before purchasing an NRAS property. There are also other JV Partner arrangements that do not operate under a head lease structure but are similar in effect. Again, a private binding ruling should be requested and shown to your accountant.

#### Too good to be true?

Sounds good but let's look at a couple of real life examples:

**19 Joyce Street, Burpengary, Qld,** is a group of townhouses offered for sale by NRAS specialist, Aztec Developments. Located 30 minutes to the Sunshine Coast and Brisbane, the three-bedroom townhouses are due to be completed in June 2010.

Assuming a loan of 90% LVR, lenders mortgage insurance of 1.5%, interest rate of 6% and tax rate of 30%, 19 Joyce Street is \$3,531 after tax, cash flow positive in 2010 (see Table 3).

**199 Norris Road, Bracken Ridge, Qld,** is a group of townhouses that have been offered for sale by NRAS investment specialist, Awesome1 Investment Properties. Situated 19km from the Brisbane CBD, some of these 34 three-bedroom townhouses are expected to be granted NRAS licences in round three with joint venture partner, Queensland Affordable Housing Consortium.

Assuming a LVR of 90% on the purchase price of \$360,000, interest rate of 6.00% and investor marginal tax rate of 30% (31.5% after Medicare Levy), Norris Road is \$2,428 after

# NRAS APPROVED HOMES IN BURPENARY POSITIVELY GEARED PROPERTY

## RECEIVE \$100,000 TAX FREE OVER TEN YEARS FROM THE GOVERNMENT\*



- ✓ High growth area
- ✓ 30 mins to Brisbane CBD
- ✓ Buy direct from the developer
- ✓ 3 bedroom, 2½ bathroom townhouses
- ✓ \$325,000 - Only 4 left!



**AZTEC TERRACES**  
19 Joyce Street,  
Burpengary, QLD

Aztec Terraces is located at 19 Joyce Street, Burpengary approximately 30 minutes drive to the Sunshine Coast and Brisbane. The townhouses are only minutes walk to the shops including Coles, Woolworths, Aldi, the new Burpengary police station, library, post office, community centre, sports grounds, medical centre, schools and public transport.

Based on the developer's calculations, the property will provide a surplus of \$63 per week (on an income of \$50,000) or \$81 per week (on an income of \$100,000), based on borrowing the full purchase price of \$325,000, stamp duty, legals, mortgage fees, solicitor fees, transfer costs and loan costs, as well as allowing for the yearly payments of council rates, body corporate fees, rental expenses, NRAS management fee. Return is based on an interest rate for the loan of 5.74%.

To take advantage of this great investment, contact us on: **07 5491 2717**

Or email [contactus@aztecdevelopments.com.au](mailto:contactus@aztecdevelopments.com.au)  
[www.aztecdevelopments.com.au](http://www.aztecdevelopments.com.au)

\*Sale price \$325,000 divided by rent plus NRAS incentive factored up plus tax and depreciation benefits. Aztec Developments (Qld) Pty Ltd is not a Licensed Financial Planner and this information is only a guide to assist in making an informed decision, however professional advice should be sought at all times.

**HURRY, ONLY 4 UNITS LEFT!**





**Table 3: NRAS example – 19 Joyce Street Burpengary Investment cash flow analysis**

Purchase price	Traditional \$325,000	NRAS \$325,000	Difference
Stamp duty and legals	(\$11,500)	(\$11,500)	
LMI (1.5% of purchase price)	(\$4,875)	(\$4,875)	
Deposit (10%)	(\$32,500)	(\$32,500)	
<b>Cash required</b>	<b>(\$48,875)</b>	<b>(\$48,875)</b>	<b>0</b>
Rent (\$320/week market)	\$16,640	\$13,312	<b>(\$3,328)</b>
Vacancy (2 weeks)	(\$640)	(\$512)	
Interest (6.00%)	(\$17,550)	(\$17,550)	
Management fee	(\$1,408)	(\$1,760)	
Joint venture fee		(\$1,000)	
Expenses (ex-depreciation)	(\$4,450)	(\$4,450)	
<b>Pre-tax cash flow</b>	<b>(\$7,408)</b>	<b>(\$11,960)</b>	<b>(\$4,552)</b>
Tax benefit (30% marginal tax rate)	\$5,386	\$6,819	
NRAS		\$8,672	
<b>Post-tax cash flow</b>	<b>(\$2,022)</b>	<b>\$3,531</b>	<b>\$5,554</b>
Gross rental yield	5.1%	4.1%	
Gross NRAS yield	0.0%	2.7%	
<b>Total gross yield</b>	<b>5.1%</b>	<b>6.8%</b>	<b>1.6%</b>
Expenses	(7.4%)	(7.8%)	
Tax benefit	1.7%	2.1%	
<b>Net yield</b>	<b>(0.6%)</b>	<b>1.1%</b>	<b>1.7%</b>
Weekly rent	\$320	\$256	
Tax benefit	\$104	\$131	
Weekly NRAS		\$167	
<b>Effective weekly rental</b>	<b>\$424</b>	<b>\$554</b>	<b>\$130</b>
<b>Yield on cash required</b>	<b>(4.1%)</b>	<b>7.2%</b>	<b>11.4%</b>

Disclaimer: Aztec Developments (Qld) Pty Ltd is not a licenced financial planner and this information is only a guide to assist in making an informed decision, however professional advice should be sought at all times.

tax, and cash flow positive in year one (see Table 4). This equates to a pre-tax gross yield (ie, rent + NRAS divided by purchase price) of 6.5% and a post-tax, net yield (ie, cash after all expenses divided by purchase price) of 0.7%.

On the key investor metric of 'cash on cash' return (ie, post-tax, net yield divided by total cash needed for purchase), the returns are 5.2% – equivalent to putting the \$42,000 in funds required to buy the property in the bank and it earning 5.2%.

While this mightn't sound too exciting at first glance, the beauty about NRAS properties are that they are generally located in traditional, higher capital growth but negative geared areas rather than the standard positive cash flow areas (eg, mining towns, inner city apartments, etc). Consequently, investors are likely to enjoy solid capital growth over the ten years of the investment.

The fact that the federal government has selected NRAS properties out of thousands of applications also means that it is likely to be located in a 'higher' demand area.

#### Investment considerations

Investors need to consider NRAS properties as long-term investments, as they need to be held in NRAS for 10 years. Some JV Partners make it hard for some properties to be removed from NRAS, which may lead to legal wrangling.

However, there are circumstances in which investors can effectively leave NRAS. Firstly, they can sell to another investor who agrees to retain the property in NRAS, which allows capital gains to be crystallised.

Secondly, should the JV Partner be able to find another property suitable for the NRAS licence then they can apply to transfer the licence to the other property.

This then enables an investor to remove their property from NRAS or sell to an owner-occupier (and potentially capture higher capital gains). In all other cases, investors can generally exit NRAS but will either lose the current year's incentives or only be able to pro rata claim the incentive according to the number of days the property was in NRAS that year.

## NRAS specialists

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\$460,000 property is about \$2,000."

"That said, NRAS is a 10-year scheme and for a little extra, investors can buy into a higher growth area that will deliver better capital growth over the long run."

"This is why we source properties from \$320,000 to around about \$420,000, so that investors can make their own choices."

Interested investors can view A1IP's extensive list of NRAS properties on their website, [www.awesome1investmentproperties.com.au](http://www.awesome1investmentproperties.com.au)

### 3. Surat Basin Homes

Surat Basin Homes is a local building company located in Chinchilla and currently offers NRAS stock priced from \$344,000 for a 3-bedroom house to \$609,000 for 2 x 3-bedroom villas.

"Investing in NRAS properties is no different to any other investment. You still need to consider if the fundamentals for the investment is good without NRAS. Ask yourself, would you buy in that location if NRAS was not available? To be more specific, is there good population growth in the area to ensure tight supply so you'll get good capital growth on your investment, and are the rental returns good enough for you now? If the answer is yes then NRAS will be the icing on the cake and you'll have a great investment," says Colin West, sales director of Surat Basin Homes.

"Don't fall into the trap that you must buy a NRAS property without worrying about the location; although most NRAS properties should be good, you still need to research the area for the best results."

With over \$100bn of proposed major resource development in the Surat Basin bringing in thousands of workers to the area, the rental prices and house values are set to soar.

"We understand that supply of houses will be very tight, therefore the average wage earner won't be able to afford to live here unless there's some sort of assistance like NRAS," says West.

To view Surat Basin's NRAS offering, go to [www.suratbasinhomes.com.au](http://www.suratbasinhomes.com.au)



**Table 4: NRAS example – 199 Norris Road, Bracken Ridge, QLD**

Purchase price	Traditional \$360,000	NRAS 360,000	Difference
Stamp duty and legals (off the plan)	\$5,000	\$5,000	
LMI (1.5% of purchase price)	\$5,400	\$5,400	
Deposit (10%)	\$36,000	\$36,000	
<b>Cash required</b>	<b>\$46,400</b>		<b>0</b>
Rent (\$380/week market)	\$19,760	\$14,820	(\$4,940)
Vacancy (2 weeks)	(\$760)	(\$570)	
Interest (6.00%)	(\$19,440)	(19,440)	
Joint venture fee (\$12/week)		-\$660	
Management fee	(\$1,672)	(\$2,090)	
Expenses (ex-depreciation)	(\$5,450)	(\$5,450)	
<b>Pre-tax cash flow</b>	<b>(\$7,562)</b>		<b>(\$5,828)</b>
Tax benefit* (30% marginal tax rate)	\$5,311	\$7,146	
NRAS incentive		\$8,672	
<b>Post-tax cash flow</b>	<b>(\$2,251)</b>	<b>\$2,428</b>	<b>\$4,680</b>
Gross rental yield	5.5%	4.1%	
Gross NRAS yield	0.0%	2.4%	
<b>Total gross yield</b>	<b>5.5%</b>	<b>6.5%</b>	<b>1.0%</b>
Expenses	(7.6%)	(7.8%)	
Tax benefit	1.5%	2.0%	
<b>Net yield</b>	<b>(0.6%)</b>	<b>0.7%</b>	<b>1.3%</b>
Weekly rent	\$380	\$285	
Tax benefit	\$102	\$137	
Weekly NRAS		\$167	
<b>Effective weekly rental</b>	<b>\$482</b>	<b>\$589</b>	<b>\$107</b>
<b>Yield on cash required</b>	<b>(4.9%)</b>	<b>5.2%</b>	<b>10.1%</b>

\* Tax benefit includes 1.5% medicare levy, year one \$8,017 depreciation and \$1,240 in loan costs written off

Finally, as mentioned previously, investors should ensure that their accountant checks the JV Partner's private binding ruling to make sure that there are no complications with receiving the NRAS incentive tax-free. 📌

Flynn De Freitas is Principal of Omega Investments, a boutique property research company specialising in positive cash flow properties such as those in NRAS and in mining towns. Utilising his training and experience as a former management

consultant and investment banker, he provides research and assistance to property investors and investment groups. For more information, please visit [www.omegainvestments.com.au](http://www.omegainvestments.com.au).

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