Tax Strategy Group

Property Taxation

Introduction

1. This paper deals with the taxation of property as part of the overall fiscal treatment of property, rather than just within the context of Budget 2010. The paper concentrates on the taxation of property recommended by the Commission on Taxation, including the practicality of introducing a tax on property and its inter-relationship with Stamp Duty. Other property-related taxes such as Capital Gains Tax and Capital Acquisitions Tax are covered in an associated paper on Capital Taxation (TSG 09/06). As quasi-property taxes such as local authority commercial rates and development levies do not fall under the remit of the TSG, they are not discussed.

Background

2. There are arguments both for, and against, the introduction of a property tax in Ireland. Those in favour would include the fact that Ireland is the only OECD member without an annual property tax and that a generous tax regime for owner-occupied housing through the provision of tax relief on rent and mortgage interest payments, combined with other exemptions, distorts housing decisions. Finally, annual property taxation in itself is less economically distortionary than taxes on labour or capital. Arguments against the introduction of a property tax include the fact that any liability will have to be paid from individuals' after tax income, the necessary infrastructure for the operation of the tax (such as up-to-date valuations) are not in place and that Ireland has a long and troubled history with property taxation (see RPT, below).

Residential Property Tax (RPT)

3. Over the period 1983-97, Ireland had an annual property tax through the Residential Property Tax (RPT). Once the market value of a residential property exceed a given limit (increased yearly in accordance with the New House Price Index), that value was subject to a RPT rate of 1.5% provided that the owner's income exceeded a certain level.

4. The nature of the RPT, particularly the income and house valuation exemptions, meant that in practice it was based on an extremely narrow tax base which led to relatively insignificant revenue yields, high administrative costs and a perception of it as a predominantly urban-based and, more specifically, a 'Dublin tax'.

5. Over the fourteen years of its existence, the level of assessments never exceeded 20,000 taxpayers, apart from 1994 when a flat rate was introduced (as opposed to a proportion of valuation). In 1996, which was its final full year of operation, there were 21,500 assessments representing less than 2% of all households.

6. In the last two full years of operation (1995 and 1996), RPT raised an average of €16.5 million per annum; by contrast, over the same period the estimated yield from residential Stamp Duty was an average of €134 million per annum.

Recent development - €200 annual charge on non-principal private residences

7. The Local Government (Charges) Act 2009 introduced a €200 annual charge on non-principal private residences (rental, holiday and vacant properties) with the revenue provided to the local authorities where the property is located. New, but unsold properties, are excluded from the charge in addition to a number of other exemptions, namely: local authority and social housing, persons moving home, "granny flats" and mobile homes used for holidays.

Domestic rates

8. The current commercial rate structure was mirrored by the existence of rates on domestic properties until their abolition in 1978. As with commercial rates, this system was based on two main elements:

   (i) Rateable valuation (tax base) of a property, determined by the Commissioner of Valuation and based on net annual letting value of a property; and
   (ii) Annual rate on valuation (tax rate), determined by the Local Authority as part of its budgeting process

Programme for Government 2007 – 2012

9. Property tax is not mentioned in the Programme for Government 2007 – 2012. Stamp Duty is covered in the Programme under the commitment to "*implement a series of measures to help young people and families both to buy their first home and to meet their mortgage repayments. Specifically, we will: Legislate immediately to abolish stamp duty for all first- time buyers and make this change retrospective for all deeds presented for stamping to the Revenue Commissioners on or after 30th April 2007*".

10. Finance (No 2) Act 2007 abolished stamp duty on residential property for all owner-occupying first time buyers in respect of all legal instruments executed on or after 31 March 2007. This exemption applies to all second-hand houses and new houses less than $125m^2$. Further reforms were undertaken in the Finance Act 2008 and Finance (No. 2) Act 2008, which are detailed below.

Commission on Taxation

11. If a property tax is to be considered, the Commission on Taxation provides a potential starting point. A significant proportion (Part 6) of the Report of the Commission on Taxation deals with the taxation of property, the relevant recommendations of which are summarised in Appendix A.

12. In overall terms, the Report recommends, as part of a "new configuration of taxation of property in Ireland", the introduction of "an annual property tax on all residential housing units" with a number of exceptions, including local authority and social housing (Recommendation 6.2).

13. The Commission considers, "as a matter of general principle", that all property should be subject to recurrent (annual) taxation, either through the local government rates system (commercial property) or an annual tax on residential property, with the development of an annual property tax (APT) on residences a key part of broadening the overall tax base.

Context of the Commission's recommendations on a property tax

14. It is clear from the Report that the Commission's recommendation for an annual tax on residential property was not designed to be considered in isolation. Instead, it has to be considered in the context of its related recommendations on the discontinuation of Stamp Duty on purchases of principal private residences (6.3), its continuance for investors of residential units (6.4), and a number of related proposals, including a tax on zoned development land with a windfall tax on profits from development land ('betterment') - see Appendix A for full details.

15. This link between the various recommendations is reflected in the narrative surrounding the rationale for, and feasibility of, introducing a recurrent tax on residential property which the Commission regards as a fundamental element to a restructured system of property taxation. The Commission inextricably linked the introduction of a new annual property tax with the attainment of the other developments such as discontinuation of Stamp Duty on purchases of principal private residences. It has been noted by commentators that the combined impact of the recommendation for a property tax, with the proposal to discontinue Stamp Duty for most residences, may have the potential to create market uncertainty, as has happened in the past, which could impact on the recovery of the private housing market.

Rationale for the development of an annual property tax

16. The over-riding rationale for a recurrent tax on immovable property is twofold. Firstly, the taxation of property through a recurring annual tax is less economically distortionary than the imposition of tax on either income or capital. This is supported by economic literature and recent OECD analysis. Secondly, an annual property tax provides a reliable and sustainable source of revenue for the Exchequer. Stamp Duty on property transactions, which is dependent on transaction levels and values, is particularly subject to fluctuations, especially in times of buoyant property prices and markets which occurred over the 2003-07 period. Capital Gains Tax and Capital Acquisitions Tax, which are covered in an associated paper on Capital Taxation (TSG 09/06), are also subject to fluctuations closely related to asset values and the level of transactions in the property market.

17. The fluctuation of Stamp Duty yields can be readily seen in the following Table:

Year	Residential	Commercial	Total	Charge: €/% (Y-on-Y)
2009*	84	100	184	-€452m (-71 %) **
2008	445	600	1,045	-€1,336m (-56%)
2007	1,018	1,363	2,381	-€528m (-18%)
2006	1,311	1,678	2,909	+€908m (-45%)
2005	945	1,056	2,001	+€540m (+37%)
2004	752	709	1,461	+€386m (+36%)
2003	528	547	1,075	+€409m (+61%)
2002	349	317	666	-€5m (-0.8%)
2001	265	406	671	-€3m (-0.5%)
2000	282	392	674	+€123m (22.3%)
1999	263	288	551	-

* Out-turn to end-June, provisional figures

** In respect of H1 2008 versus H1 2009

18. The nature of Stamp Duty, especially as it relates to residential property, makes it difficult to forecast and renders it extremely vulnerable to changing conditions in the property market. Appendix B sets out the current rates of Stamp Duty for residential and non-residential property, while Appendix C details existing reliefs and exemptions.

Potential impact of an annual property tax on economic activity

19. The OECD has highlighted that annual taxes on land and buildings have a relatively small adverse impact on economic performance because of the following factors:

(i) lack of a direct effect on labour, either supply or demand;
(ii) with a stable tax base, there is a predictable tax yield; and
(iii) Using an immobile tax base is less likely to distort economic behaviour.

Possible features of an Annual Property Tax

20. A number of features to a proposed annual property tax can be identified, many of which have also been recognised by the Commission on Taxation:

- Frequency - annual tax, but payable in a flexible (via the PAYE system or online) manner spread over frequent intervals over the year;
- Coverage – cover as many residential properties as possible, including vacant properties and rented properties, but excluding local authority and social housing;
- Exemptions – based on ability to pay with exemptions for persons on low incomes, including deferred payment until disposal of the property in the case of the elderly on low incomes;
- Persons Liable - owners of the property would be liable and not tenants in the case of rented properties;
- Assessment – either self-assessment (property owner) or direct assessment (Revenue, Local Authority or specialised agency: public or private);
- Basis of taxation - tax payable is established by reference to either the market value of a property or its floor space or an amalgamation of both;
- Information – requirement for a comprehensive database of properties covering valuations and floor space, including details of ownership and sale prices is critical for an effective property tax;
- Rate - a low rate of tax which can be either proportionate, progressive or flat; and
- Equity - general perception amongst taxpayers that the tax is equitable with assessment based on measurable criteria.

21. Features of this nature occur in property tax regimes in other OECD and EU States. A common characteristic of regimes in other jurisdictions is transparency and certainty. Taxpayers are aware of how the tax is computed and there is a shared sense of equity, through its coverage of as many properties and taxpayers as possible. There is also certainty based on comprehensive, up-to-date, and accessible property databases, which enable taxpayers to be generally aware of their tax liability.

22. Another common feature of the regimes in other jurisdictions is the use of the property tax as a source of revenue for Local Authorities, either directly (assessed and collected) or through hypothecation where there is collection by a national tax administration service.

However, the Local Authorities in such jurisdictions are structured differently and generally have wider operational remits than in Ireland.

Possible yield from a property tax

23. The Commission on Taxation provided illustrative examples of the likely yields from suggested rates of 0.25% and 0.30% which would be applied proportionately to self-assessed (i.e. by a property owner) market values of properties using eight proposed valuation bands for values ranging from €0 to above €1.5m covering 1.934 million houses – Appendix D. House price data was used for 2004 while data for 2009 was used for the number of houses; the use of 2004 data equates to prevailing estimates of current property values. For each proposed valuation band, a mid-point was used to calculate the estimate yield.

24. On this basis, the Commission suggested a tentative projected gross yield of €1.231bn for the 0.25% rate and €1.476bn for the 0.30% which equates to approximately €492m for each 0.1% rate of tax.

25. However, when waivers for low-income households and other exclusions are included, these gross projections fall by €305m from €1.231bn to €926m in the case of the 0.25% rate and by €364m from €1.476bn to €1,112bn. These projected net yields equate to approximately €370m for each 0.1% rate of tax.

26. It should be noted that the estimated annual charge per property ranged from €188 for houses valued below €150,000 using a 0.25% rate to €3,750 for houses in the €1m - €1.5m valuation band using the 0.30% rate; in both cases, houses valued in excess of €1.5m the rates would apply to the actual valuation of the property in question.

Other issues in relation to the development of a tax on property

27. A number of issues can be identified in regard to the possible introduction of a property tax; these are particularly relevant in the context of the Commission on Taxation's recommendation on this matter. The most important issue relates to the interplay of the proposed annual tax on property with Stamp Duty and the timing of introducing such a tax. These can be summarised as:

    (a) the replacement of residential Stamp Duty by a tax on property;
    (b) continuance of residential Stamp Duty in conjunction with a tax on property;
    (c) the position of investors in residential property; and
    (d) The treatment of zoned development land.

    The relationship of a property tax with the existing €200 annual charge on non-principal private residences is also relevant.

28. As previously discussed, a key element underpinning the Commission's consideration of an annual property tax is its inextricable linkage with the abolition of residential Stamp Duty for owner occupiers. The introduction of an annual property tax would require transitional arrangements for a limited period.

    Taxation of zoned land

29. The taxation of zoned development land is a complex issue and one which is very much related to the establishment of NAMA and how it deals with the extensive land banks of zoned, but undeveloped land in locations through the State.

€200 charge on non-principal private residences

30. As previously noted, an annual €200 annual charge on non-principal private residences (rental, holiday and vacant properties) was introduced earlier this year with the revenue provided to the local authorities where the property is located. The Commission's recommendation to replace this charge by a property tax is justified by the potential for confusion and double-charging.

Other issues relating to a property tax

31. There are also a range of purely practical issues that would need to be resolved. For example:

- *Extent of the tax base*- balance between maximum coverage and exemptions for, e.g., local authority and social housing.
- *Persons liable to pay the tax* – possible exemptions for elderly/those on low incomes.
- *Valuation of properties* – need for an up-to-date national property valuation register.
- *Assessment methods for the tax* – direct assessment (Revenue or other State Agency) versus self-assessment by owner but subject to Revenue audit.
- *Assessable values* – value of the property versus floor area or land/site value
- *Type of tax rate*- flat, progressive or proportionate.
- *Administration of the tax and use of its revenue* – administered as a national tax for the Exchequer with or without hypothecation versus administered by local authorities as a source of funding for them.

Exemptions for previously paid Stamp Duty and cases of negative equity

32. Specific issues can be identified in regard to: persons who have previously paid Stamp Duty on their properties; persons with mortgages; and home owners experiencing negative equity.

33. The Commission on Taxation considered this matter and felt that, as a transitional arrangement, a time-bound exemption from property tax be available to persons who paid Stamp Duty on a principal private residence or a certain period in advance of the introduction of the tax; it suggested that the exemption would be for seven years from the date when the Duty was paid.

Stamp Duty

34. Stamp Duty is levied on the value of property covered by property transactions (conveyances), rather than on the actual properties themselves. It was initially introduced in the early nineteenth century as a means of monitoring the level of land transactions.

35. Appendix B sets out the current rates of Stamp Duty for residential and non-residential property, while Appendix C details existing reliefs and exemptions. In recent years, there have been substantial changes to the residential Stamp Duty regime which have primarily related to policy goals such as: making homes more affordable for first-time buyers; encouraging investors in residential properties; and, to a lesser extent, maintaining activity levels in a faltering property market. Simplification of the regime was also an important concern.

36. The most significant of the changes include:

- 2000 - Introduction of preferential treatment for first-time buyers and a new single rate for investors of new residential property.
- 2001 - Investors charged at normal residential stamp duty rates.
- 2003 - Additional rates (7%, 8% and 9%) for non-residential property.
- 2004 - Stamp duty rates and thresholds for first-time buyers further reduced.
- 2007 - Abolition of stamp duty for first-time buyers. New intermediary relief
- 2008 - Radical reform of the stamp duty regime for residential property with two rates replacing five rates, coupled with a reduction in the claw-back period for first-time buyers renting out property, and a reduction in top rate for commercial property from 9% to 6%.
- 2009 - New scheme for stamp duty relief on exchanges of residential properties.

37. At this stage, and as a result of recent reforms, the only owner occupiers liable to residential Stamp Duty are non first-time purchasers of second-hand homes valued over €127,000 or new homes with an area above 125m^2 (1,346ft^2). Investors are liable for residential properties valued over €127,000 as are all purchasers of commercial property (including sites) valued in excess of €10,000.

38. Stamp Duty has an important role within the overall property market because it can impact on persons trading-up and trading-down from existing properties by acting as a determinant on the price paid by a buyer and the price received by a seller. In effect, it reduces the efficiency of the housing market through interference in the trading cycle whereby older houses are ‘recycled’ to new market entrants.

39. However, Stamp Duty has declined in importance as a factor in the current housing market because it now only applies to a segment of purchasers: non first-time buyers buying second-hand homes. It does not apply to most new houses or to first-time buyers of second-hand homes. In addition, the recent decline in house prices has resulted in a fall in the nominal amounts of Stamp Duty being paid.

40. The Tax Strategy Group may wish to discuss.

Capital and Savings Taxation Policy
September, 2009

Appendix a **Recommendations of the Commission on Taxation relating to the taxation of property – 7th September, 2009**

6.1	The provision of an up-to-date valuation base for all property and land in Ireland should be addressed as a priority issue.
6.2	Provide for an annual property tax on all residential housing units with the broad exceptions of local authority and social housing units and some other limited exceptions set out in section 4.2 of Part 6.
6.3	Stamp duty for purchasers of principal private residences should be zero-rated.
6.4	Stamp duty should continue to apply to investor purchasers of residential housing units. The rate should be competitive having regard to the transaction tax rates and thresholds that apply across the EU.
6.6	A recurrent property tax on land zoned for development should be introduced.
8.73*	Stamp duty relief for transfers of land to young trained farmers should continue.
8.74*	The stamp duty exemption relating to the sale or transfer of EU Single Farm Payment Entitlements should be continued.
8.111*	Consanguinity relief within the stamp duty code should continue.
11.11	The proposed annual property tax system should be established and operated as a national property tax system for a short initial period: • Its revenues should then be hypothecated for local government financing as soon as is feasible – once the tax has become established, and • By no later than the next local elections (June 2014), rate-setting powers should be devolved to local government subject to the considerations set out at section 5.3 of Part 11.

* Relates to the provision of a relief from Stamp Duty

Appendix B Stamp Duty Rates: Residential and Non-Residential Property

Stamp Duty Rates for New Residential Properties*

Condition	Owner-Occupiers	Investors/non-occupying purchasers
Under 125 m^2 (1,346ft^2)	Exempt	Standard rates (i.e. second-hand rates in Table below) charged on full property value (ex-VAT) – regardless of size
Over 125 m^2 (1,346ft^2)	Standard rates (i.e. second-hand rates in Table below) charged on site value or 25% property value (ex-VAT)	

***** First-time owner-occupying purchasers are exempt from residential Stamp Duty

Stamp Duty Rates for Second-Hand Residential Properties*

Aggregate Consideration exceeds €127,000*	Rate for instruments executed on or after 5 November 2007
First €125,000	Nil
Next €875,000	7%
Excess over €1,000,000	9%

***** First-time owner-occupying purchasers are exempt from residential Stamp Duty

Non-Residential Stamp Duty Rates

Aggregate Consideration	Rate of Duty
Up to €10,000	Exempt
€10,001 to €20,000	1%
€20,001 to €30,000	2%
€30,001 to €40,000	3%
€40,001 to €70,000	4%
€70,001 to €80,000	5%
Over €80,000	6%

Appendix C Reliefs/Exemptions from Stamp Duty on property

First- time buyers

All first- time owner- occupying purchasers of new and second- hand houses are exempt from Stamp Duty.

Newly constructed homes

Any purchase of a new house/apartment below 125 m^2 in size is exempt from Stamp Duty. For new properties above this threshold, the normal residential rates (7% or 9%, depending on value) are charged on site value or 25% of the property value (ex-VAT).

Minimum valuation threshold

Properties valued below €127,000 are completely exempt from residential Stamp Duty with a corresponding threshold of €10,000 for non- residential property. For residential properties, the first €125,000 of any transaction valued in excess of €127,000 is subject to a 'nil' rate with the residual balance subject to the prevailing rates of 7% (next €875,000) and 9% (excess over €1,000,000).

Young Trained Farmers

There is an exemption for qualified young trained farmers receiving farmland. Farmers aged below 35 who have a specific agricultural qualification may apply for this relief. Budget 2009 extended this scheme for a further four years until 31st December 2012.

Farm Consolidation Relief

Farm consolidation relief allows a farmer to claim relief where he or she sells farm land and purchases farm land, in order to consolidate his or her holding, where both the sale and purchase of farm land occur within 18 months of each other. Budget 2009 extended this scheme for a further 2 years until 30th June 2011.

Site to Child

The transfer of a site from a parent to a child is exempt if the purpose of the transfer is for the construction of the child's principal private residence and the market value of the site does not exceed €500,000, formerly €254,000. The size of the site qualifying for relief is restricted to 1 acre.

Consanguinity Relief

A property transfer between certain blood relatives qualifies for Consanguinity Relief which reduces the rate of Stamp Duty to one-half of the rate which would otherwise apply. This relief applies to the residential and non-residential regimes.

Resting in Contract, Licensing, etc

A number of provisions were introduced by the 2007 Finance Act (Section 110) to address the avoidance of Stamp Duty in the acquisition of land for development. Commencement of these provisions was initially deferred until the property market improved. Following the renewal of the provisions in Section 85 Finance (No 2) Act 2008, the provisions will commence once consultation with interested parties on a number of complex inter-related issues has concluded.

Appendix D **Illustrative valuation bands explored by the Commission on Taxation for a proposed property tax based on possible 0.25% and 0.30% rates**