Indecon Evaluation of Scheme of Allowances for Qualifying Residential Units Associated with Nursing Homes

Final Report

Prepared for

Department of Finance

By

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Executive Summary

Introduction and Background

Indecon International Economic Consultants were appointed in 2006 by the Department of Finance to conduct an independent review of the tax incentive pertaining specifically to Residential Units attached to registered Nursing Homes/Convalescent Facilities. The report presents our assessment of the extent to which the scheme as it pertains to residential units has justified its introduction and the contribution that the relief has made and can make to the wider policy objectives of developing the nursing home and residential care sector. We evaluate the success of the scheme in terms of its economic impact and provide recommendations on policy options for the Government going forward. This report represents a follow-on to the major review undertaken previously by Indecon of property-based tax incentive schemes.

Approach to the Review

Our approach to this study is focused on the evaluation of the contribution the relief available for investment in the construction or refurbishment of residential units attached to private nursing homes has made to its sector through the application of a formal cost-benefit analysis.

We examine the total capital expenditure under the scheme and the associated cost to the Exchequer, and the economic benefits. The study also identifies changes which could be considered to the ongoing operation of the scheme.

Major information deficiencies existed in relation to the operation and extent of usage of the residential unit relief. These deficiencies have been addressed by Indecon as part of this study by utilising a wide range of sources and approaches. This has enabled us to prepare detailed estimates of the costs of the scheme. The estimated costs relate to projects undertaken since the inception of the residential units relief scheme in 2002.

In our estimates of tax costs we take account of the fact that allowances are claimed over time and allowances on capital expenditure incurred will arise only when the allowances are claimed. Future estimates of allowances are therefore included in our estimate and an NPV based on discounted values at 5% per annum is utilised. While there is uncertainty concerning future take-up, this does not, in general, impact on the cost-benefit ratios or on the merits of continuing or ending the incentive.

Terms of Reference

The terms of reference for this study to evaluate the costs and benefits of qualifying residential units attached to private nursing homes has involved the following:

- Assessment of the extent to which the scheme has justified its introduction ;
- Examination of the contribution that the relief has made and can make to the wider policy objectives;

- Estimation of the costs and benefits of the scheme through a formal cost/benefit analysis having regard to guidelines issued by the Department of Finance on this issue;
- The study has also identified what elements/changes/improvements should be considered to the scheme, bearing in mind changes in economic and other circumstances, the need to ensure effectiveness and value for money and the balance within the tax system.

Factors which have been considered in assessing the scheme include:

- The level and type of investment generated;
- The cost to the Exchequer of the tax incentives and gross and net impact on Exchequer revenues;
- The level of private finance leveraged under the scheme;
- The extent of deadweight costs incurred and any displacement effects;
- Employment and other economic effects – both temporary and sustainable;
- Examination of the extent, if any, to which the existing scheme of relief for residential units associated with nursing homes would contribute to the development of an infrastructure of long-term care services for older people.

Note on Residential Units Attached to Registered Nursing Homes

Section 33 of the 2002 Finance Act provided for a scheme of capital allowances for expenditure incurred on the construction or refurbishment of housing units associated with a registered nursing home. These residential units are intended for older people who wish to maintain their independent living status within a sheltered caring environment.

The main conditions of the original scheme were as follows:

- The residential units had to be operated or managed by a registered nursing home and the nursing home will provide back-up medical facilities (including nursing) to the occupants of the units when required, and an onsite caretaker will also be available.
- There had to be a minimum of 20 housing units within the site of the nursing home. The units had to be single storey houses or comprised in a two storey building. The units and any building in which they are comprised were required to be designed and constructed to meet the needs of persons with disabilities, including in particular the needs of persons confined to wheelchairs. Each unit had to contain one or two bedrooms, a kitchen, a living room, bath or shower facilities, toilet facilities and a nurse call system linked to the nursing home.
- The units were only permitted to be leased to those who are certified by a medical doctor to require such accommodation by virtue of old age or infirmity.
- There was a requirement for a day care centre in site, which complies with Health Board requirements (any development cost of providing this centre did not qualify for capital allowances).
- Not less than 20 percent of the residential units had to be made available to the relevant Health Board, and the general rates charged had be discounted by at least 10 per cent in the case of the Health Board tenants.

The original tax relief available was the same as the relief for nursing homes. There was a write off period of 7 years for qualifying expenditure. Capital allowances of 15 percent per year were available for the first 6 years with the balance of 10 percent being written off in year 7. The capital allowance was available for expenditure incurred in the 5 year period commencing with the passing of the Finance Act, 2002.

The Finance Act 2004 provided that, in the future, such units may be comprised in a larger building consisting of one or more storeys where a fire safety certificate in relation to the building is required under Part III of the Building Control Regulations 1997 (S.I. No. 496 of 1997) and, before construction works commence, such certificate is issued by a building control authority. Units which heretofore qualified as single houses are unaffected by this condition. The section also reduced, from 20 to 10, the number of qualifying residential units, associated with a registered nursing home, which are required in order that the scheme of capital allowances may apply in relation to such units. The amendment applied as respects capital expenditure incurred on or after 4th February 2004.

Finance Act 2006 introduced some additional changes to the relief for residential units. The termination date for the relief is moved from March 2007 to 31 July 2008 in line with the new deadlines applicable to the other terminating schemes. Also units that are leased directly to registered nursing homes may qualify for relief provided such units are to be subsequently leased by the registered nursing home to elderly or infirm persons who have the appropriate certificate from a medical practitioner.

The 2006 Finance Act provides that only 75 percent of capital expenditure attributable to the year 2007 and 50 percent of the capital expenditure attributable to the period 1 January 2008 to 31 July 2008 may qualify to relief. Again, expenditure which is proper to the year 2006 can qualify without restriction.

Also, all such buildings that are first used (or first used after refurbishment) on or after 1 February 2007 the 2006 Finance Act increases to 15 years both the current 7-year tax life and 10-year holding period for balancing allowance and balancing change purposes. However, the 7-year write-off period and annual rate of write-off are unchanged.

Review of Capital Allowances for Nursing Home Residential Units

Based on our analysis of nursing home residential units, we believe that the tax incentive has been effective in increasing the level of supply of residential unit spaces over what has been a short time period since the relief for these units was introduced under the 2002 Finance Act. Moreover, our analysis and assessment of demographic trends points to a very strong growth in future demand for such facilities and associated accommodation, particularly over the next 10-20 year period.

Eligible capital investment undertaken on the development of residential units attached to registered private nursing homes which has availed of the tax relief under the scheme is estimated to have totalled €10.7 million between 2004 and 2005. We estimate that future growth in the demand for beds is likely to involve an additional capital investment over the period to 2008 of €39 million, but there is uncertainty re future investment which could be lower or higher than this level.

A summary of the overall costs and benefits arising from historic and projected future capital allowances and related tax relief provided under the incentive scheme for investment in residential units associated with private nursing homes is presented in the table below. We estimate the gross tax cost of this incentive scheme to the Exchequer to be between €13-14 million over the period 2004-2014 (the period over which allowances are claimed in respect of capital expenditures taking place between 2004 and 2008). Taking into account the projected net economic benefits arising from the scheme, which are estimated to amount to approximately €10 million, in addition to indirect tax benefits on foot of these benefits totalling an estimated €5 million, a small overall net benefit is observed through the operation of the scheme. The Indirect Exchequer Tax Revenues and the Net Tax Foregone estimates are adjusted for opportunity cost and deadweight.

Costs and Benefits of Capital Allowances/Tax Reliefs for Investment in Nursing Home Residential Units: Indecon Estimates

Estimate	Scenario 1 - € million	Scenario 2 - € Million
Estimated Capital Expenditure on Projects that have Proceeded – 2004-2005	10.7	10.7
Capital Expenditure on likely Future Projects – 2006-2008	38.8	38.8
Gross Tax Cost of Allowances – 2004-2014	13.0	14.0
Indirect Exchequer Tax Revenues – 2004-2008	5.0	5.0
Economic Benefits – 2004-2008	9.7	9.7
Net Cost of Tax Foregone – 2004-2014	8.04	9.02
Net Overall Benefit – 2004-2014	1.7	0.7

Source: Indecon calculations

Recommendations

Based on our detailed analysis and evaluation of the costs and benefits arising from the operation of the capital allowances/tax relief scheme pertaining to residential units attached to registered private nursing homes, we present Indecon's recommendations designed to inform future policymaking in this area in the table below.

Indecon Recommendations re Capital Allowances/Tax Relief Scheme for Residential Units Associated with Registered Private Nursing Homes	
1.	The Residential Units Nursing Home Scheme should be extended for a period with allowances of 50% of capital expenditure if allowances are claimed at personal tax rate and 75% of capital if expenditure claimed at corporate tax rates.
2.	A formal assessment of the continued relevance of the scheme and the costs and benefits should be undertaken after a period. This should be co-ordinated with the previously recommended 3-year review of the nursing homes scheme.
3.	Eligibility for residential unit nursing homes should be conditional on investors/promoters obtaining a certification of the scheme by a relevant statutory body such as HSE/HIQA/SSI to ensure that they are fit for purpose and are associated with a nursing home registered by HSE/HIQA/SSI
4.	As part of certification by HSE/HIQA/SSI, promoters/investors should provide full profile details of capital costs which will be claimed, and whether the investors are corporate entities or individuals. An annual report to HSE/HIQA/SSI indicating occupancy levels disaggregated by those with and without disabilities should be provided. The profile detail forms should be forwarded by HSE/HIQA/SSI to the Department of Health and Children, and copied to the Department of Finance.
5.	The existing restriction on prohibiting owner/occupancies should continue to apply.
6.	The current condition re medical certification should be strictly enforced. In other words, eligibility for tax allowances should be strictly dependent on all occupancies of the residential units having a medical certificate indicating they require such accommodation.
7.	Immediate family relatives and immediate in-laws of purchasers should not be entitled to occupancy of units.
8.	The existing restriction on the availability of 20% of units for those eligible for a rent subsidy at 90% of costs of other units should continue to apply. This restriction should not apply where capital allowances are claimed at corporate tax rates, where corporate entities own the totality of units.
9.	The strict enforcement of the condition that the selection of occupants should remain with a registered nursing home should continue and this requirement should be made explicit in future legislation.
10.	The claw back period for allowances if the property is used for purposes other than nursing homes residential units should be extended to 20 years for both personal sector and corporate sector investors.

Source: Indecon

1 Introduction and Background

Indecon International Economic Consultants were appointed by the Department of Finance to conduct an independent review of the tax incentive pertaining specifically to Residential Units attached to registered Nursing Homes/Convalescent Facilities.

1.1 Background to Review

This report represents a follow-on to the major review undertaken by Indecon in 2005 of property based tax incentive schemes. The report presents our assessment of the extent to which the scheme as it pertains to residential units has justified its introduction and the contribution that the relief has made and can make to the wider policy objectives of developing the nursing home and residential care sector. We evaluate the success of the scheme in terms of its economic impact and provide recommendations on policy options for the Government going forward. We outline our approach to the review in more detail later in this section.

1.2 Overview of Methodological Approach

Our approach to this study involves a rigorous evaluation, through the application of a formal cost-benefit analysis, of the contribution the relief available for investment in the construction or refurbishment of residential units attached to private nursing homes has made to its sector. We also implicitly consider whether the scheme has served its purpose.

Indecon believes that if it is deemed that continuation of the scheme is justified it may also be useful to consider other potential modifications to the scheme to reduce deadweight or Exchequer costs.

The study also identifies changes which could be considered to the ongoing operation of the scheme, bearing in mind changes in economic and other circumstances, the need to ensure effectiveness and value for money and the balance within the tax system.

Our approach involved five main areas of focus as presented in Figure 1.1.

Figure 1.1: Main Areas of Focus

Quantification of Level of Activity, Investment and Exchequer Costs

Evaluation of Gross Economic Costs and Benefits

Adjustments for Deadweight, Displacement and Opportunity Costs

Analysis of Distribution of Benefits

Assessment of Alternatives and/or Refinements to Scheme

Survey of Private Nursing Homes

As part of this update review, in addition to examining numerous sources of information, a limited survey of registered private nursing homes was undertaken with the objective of seeking information on a number of issues pertinent to the review. The survey, *inter alia*, sought information on:

- Classification of facilities in relation to dependence levels among residents;
- Year of construction of residential units;
- Extent of usage of capital allowances/tax relief scheme for in investment in residential units;
- Level of eligible capital expenditures on construction of residential units;
- Profile of persons utilising capital allowances/tax relief scheme, i.e. personal sector or corporate sector;
- Details re number of residential unit beds available and utilised;
- Details re average weekly costs of residential unit places;
- Views on impact of capital allowances/tax relief scheme on cost of places;

- Views on impact of capital allowances/tax relief scheme on site prices, construction costs, investment in projects, financial returns to promoters and property prices;
- Views on extent of likely impacts *in absence of* allowances/tax relief scheme;
- Views on effectiveness of scheme in increasing supply and reducing costs of residential unit places.

Case study

We have also undertaken a case study, where we set out an example of a development, including the features of the development in terms of the cost of purchase of units, the numbers of units, the characteristics of these units and the level of services provided.

Assessment of investor perspective

A related issue concerns the operation of the incentive scheme for investment in a residential unit development from the perspective of the investor and we consider this aspect in detail in the form of an assessment of potential returns under a number of hypothetical investment scenarios. In particular, we model the impact of our recommendations for the scheme on potential future returns to prospective investors in residential unit developments.

1.3 Overview Discussion of Concepts Underpinning Review

The fact that a sector is economically important, or that nursing home residential units may be important in addressing the needs of the elderly or infirm, does not necessarily justify the operation of tax incentive schemes. Neither does the case where the economic benefits exceed the economic costs of an investment. The justification for tax incentives should be based on the identification of market failure.

(The potential ranges of market failure are discussed below and include estimates which could, *inter alia*, include a shift in demands from the Exchequer and other potential benefits of the incentives.) We also discuss the concepts of deadweight, displacement opportunity costs and multiplier effects, which we use in our evaluation in subsequent sections of this report.

1.3.1 Market Failure

The concept of 'market failure' is the appropriate economic justification for Government intervention in various markets. It occurs when markets are not optimally efficient.

Perfectly competitive markets display the following characteristics:

- Buyers and sellers have perfect information;
- There are no barriers to entry and;
- Firms are price-takers.

When a market is perfectly competitive, the price will be equal to marginal cost ('allocative efficiency') and production will occur at minimum average cost ('productive efficiency'). There will be no excess profits and the market will function optimally for consumers by delivering the highest possible output at economic cost.

In practice, however, markets are not always perfectly competitive and may not, therefore, be characterised by these factors. 'Market failure' occurs when one or more of the assumptions outlined above do not hold or where economic externalities exist. The existence of such cases means that non-optimal outcomes occur and markets do not function at optimal efficiently. The existence of market failure serves as a basis for why governments and other institutions (such as regulators) should intervene in some markets. Their role is to identify and address the sources of market failure and take appropriate corrective action to help the market function effectively.

The main sources of market failure encountered in practice are as follows:

- Asymmetric information;
- Unaligned incentives;
- Externalities;
- Public goods;
- Merit goods;
- Market power.

Asymmetric information occurs in markets where one party (buyers or sellers) has more information than the other party. A potential adverse consequence of asymmetric information is that too much low quality output or too little high quality output may be produced.

Unaligned incentives may be related to asymmetric information insofar as the interests of buyers and sellers, and other parties, such as, for example, regulators, are out of line with each other. This may result in too few of the good or service being produced, in the absence of Government intervention. A related issue could apply in case of residential nursing home units arising from Government support for people using nursing home resident units which have the impact of significantly expanding demand for such units. In such a scenario this could result in an increase in prices for users unless sufficient supply measures are taken. The current tax incentives with some modifications could assist in expanding supply.

An **externality** arises when the costs or benefits of a good or service are not fully reflected in the market price of the good or service. A positive externality occurs when the marginal private benefit of the good or service is less than the marginal social benefit. In the absence of Government intervention or regulation, this particular kind of market failure may result in too little of the good or service being produced relative to the socially optimal level.

A **public good** is one that can be consumed by everybody in a society, regardless of whether they pay for them or not. Most goods and services are 'private goods' – we have to pay for them and one person's consumption may limit another's consumption of the good or service. On the other hand, 'public goods' are non-rivalrous (i.e. one person consuming them does not necessarily stop another person's consumption) and non-excludable (i.e. it is not possible to prevent non-payers from consuming them). The combination of these two characteristics makes it difficult for producers to charge for these goods, so their markets are usually characterised by Government provision.

Merit goods are very similar to public goods – they satisfy the two properties of non-rival and non-excludable but not fully. They are goods with positive externalities that governments believe the consumer undervalues due to imperfect information.

Market power refers to the ability of buyers or sellers to exert influence over price or quantity in a market. Market power depends on the number of parties on each side of the market. If a market has few buyers, but many sellers, the buyers tend to have relatively more market power than sellers. The converse occurs if there are many buyers, but relatively few sellers. If a single seller controls the market on the supply side, the market is a monopoly. If a single buyer controls the market, we have monopoly. Most markets are subject to some degree of power by their participants and most market power occurs on the supply side – monopoly or oligopoly (a few suppliers or firms). Barriers to entry are a principal cause of market power on the supply side. These prevent new (potentially more efficient) firms from entering the market and mean that incumbent firms with market power can continue to price at above cost in the long run without fear of losing market share to new rivals.

1.3.2 Deadweight

Deadweight refers to the extent to which the benefits of a tax incentive or subsidy are reduced or eliminated. In the case of this study, deadweight of the tax incentive relates to the extent to which investments benefiting from the tax relief under the scheme would have occurred in the absence of the incentive. If investment would have proceeded in the absence of the tax incentive, then the tax revenue foregone through the tax relief extended under the scheme represents an unnecessary cost to the Exchequer. We carefully considered this issue in the case of nursing home residential units in the light of Government demand side measures in relation to nursing home costs. While this requires careful monitoring over time our analysis suggests that the incentives have the potential to accelerate supply.

1.3.3 Displacement

This refers to the extent to which Government involvement in a particular sector may lead to other negative side effects that result in a reduction in overall benefits. For example, incentives to one project could result in business being displaced from an existing operator. In cases where supply is in balance with demand or where there is supply, government incentives for additional investment could impact negatively on existing providers. While this is a very real issue for many property based tax incentives, it may be less significant for residential nursing home units providing the conditions are strictly enforced and measures are taken to remove other potential difficulties.

1.3.4 Opportunity Cost

The opportunity cost of any expenditure or investment refers to the cost of the opportunity foregone (i.e. the benefits that could be received from the alternative expenditure or investment). In the context of the nursing home residential unit incentives, the opportunity cost of the investment under the incentive will be the value foregone from investors using their money to invest in a different sector of the economy, or of simply spending the money on consumption. In a near full employment economy such as currently exists in Ireland the opportunity costs of resources is very high.

1.3.5 Multiplier Effect

The multiplier effect relates to the impact of indirect and second and subsequent round impacts arising out of the initial capital or current expenditure. The multiplier is concerned with how national income changes as a result of a change in an injection in a given area of the economy, the construction sector in the case of this study. The size of any multiplier effect is determined by the extent of 'leakages' from an economy, such as imports and taxation. Of course multipliers simply measure the linkages between different sectors and the existence of indirect benefits for other sectors arising from an investment does not provide any justification for government incentives.

1.4 Structure of Report

The remainder of this report is structured as follows: in Section 2 we present a description of the current incentive scheme for investment in residential units, including the operational rules governing the scheme. In addition, we also discuss the issue of the interaction of the incentive scheme with other, demand-side measures supporting participation in the residential care sector. In Section 3 we review activity and recent developments in the sector, including in relation to the supply of residential units and the extent of recent construction activity, and the cost of facility places. We also consider the likely developments in relation to the demand for nursing home residential units in the future and the implications of this for the consideration of policy options going forward. Finally, we present a case study example of a scheme of residential units. Section 4 focuses on the evaluation of the impact of the incentive scheme and sets out our evaluation of the costs to the Exchequer against the economic benefits of the scheme. Finally, Section 5 sets out our overall conclusions and recommendations for the scheme going forward. In this section, we also assess the implications of these recommendations for prospective investors.

1.5 Acknowledgements

Indecon would like to acknowledge the valuable inputs and assistance provided by the Department of Finance, the Revenue Commissioners and the Department of Health and Children. Thanks are also due to Irish Nursing Homes Organisation and to the HSE. Thanks are also due to a number of local authorities who provided updated data on planning applications, and to participants in the sector who responded to our survey of nursing homes.

The usual disclaimer applies and the views and analysis in this report are exclusively those of Indecon.

2 Description of Tax Incentive and Other Sectoral Support Measures

2.1 Background to Tax Incentive Scheme

Section 33 of the 2002 Finance Act provided for a scheme of capital allowances for expenditure incurred on the construction or refurbishment of housing units associated with a registered nursing home. These residential units are intended for older people who wish to maintain their independent living status within a sheltered caring environment.

2.2 Qualifying Conditions of Scheme

The main conditions of the original scheme introduced in 2002 were as follows:

- The residential units had to be operated or managed by a registered nursing home and the nursing home will provide back-up medical facilities (including nursing) to the occupants of the units when required, and an onsite caretaker will also be available.
- There was a requirement for a minimum of 20 housing units within the site of the nursing home. The units had to be single storey houses or comprised in a two storey building. The units and any building in which they are comprised had to be designed and constructed to meet the needs of persons with disabilities, including in particular the needs of persons confined to wheelchairs. Each unit was required to contain one or two bedrooms, a kitchen, a living room, bath or shower facilities, toilet facilities and a nurse call system linked to the nursing home.
- The units were only permitted to be leased to those who were certified by a medical doctor to require such accommodation by virtue of old age or infirmity.
- There was a requirement for a day care centre in site, which complied with Health Board requirements (any development cost of providing this centre did not qualify for capital allowances).
- Not less than 20 percent of the residential units had to be made available to the relevant Health Board, and the general rates charged had to be discounted by at least 10 per cent in the case of the Health Board tenants.

2.2.1 Capital allowances and write-off period

The original tax relief introduced in 2002 was the same as the existing relief for nursing homes. This involved a write-off period of 7 years for qualifying expenditure. Capital allowances at a rate of 15 percent per year were available for the first 6 years with the balance of 10 percent being written off in year 7. The capital allowances were made available for expenditure incurred in the 5 year period commencing with the passing of the Finance Act, 2002 (i.e. 25 March 2002).

2.3 Recent Amendments and Adjustments

Since the introduction of the relief for residential units attached to private nursing homes under the 2002 Finance Act a number of amendments and adjustments have been introduced, which are described below.

Finance Act 2004

The Finance Act 2004 provided that, in the future, such units may be comprised in a larger building consisting of one or more storeys where a fire safety certificate in relation to the building is required under Part III of the Building Control Regulations 1997 (S.I. No. 496 of 1997) and, before construction works commence, such certificate is issued by a building control authority. Units which heretofore qualified as single houses are unaffected by this condition. The section also reduced, from 20 to 10, the number of qualifying residential units, associated with a registered nursing home, which are required in order that the scheme of capital allowances may apply in relation to such units. The amendment applied as respects capital expenditure incurred on or after 4th February 2004.

Finance Act 2006

Most recently, the 2006 Finance Act introduced some changes to the relief for residential units. The termination date for the relief is moved from March 2007 to 31 July 2008, in line with the new deadlines applicable to the other terminating schemes. Also units that are leased directly to registered nursing homes may qualify for relief provided such units are to be subsequently leased by the registered nursing home to elderly or infirm persons who have the appropriate certificate from a medical practitioner.

In addition, the 2006 Finance Act provides that 75 percent of capital expenditure attributable to the year 2007 and 50 percent of the capital expenditure attributable to the period 1 January 2008 to 31 July 2008 may qualify to relief. Again, expenditure which is proper to the year 2006 can qualify without restriction.

Also, all such buildings that are first used (or first used after refurbishment) on or after 1 February 2007 the 2006 Finance Act increases to 15 years both the current 7-year tax life and 10-year holding period for balancing allowance and balancing change purposes. However, the 7-year write-off period and annual rate of write-off are unchanged.

2.4 Other Sectoral Support Measures – Demand-side Measures

An issue in the assessment of the impact of the incentive scheme for investment in residential units concerns the interaction of the scheme, which is a supply-side measure, with demand-side mechanisms which are also in existence and designed to support access to residential places for persons in need of such care. Two measures, in particular, are indirectly relevant to this issue, namely:

- The Private Nursing Homes Subvention scheme;
- The recently-announced *A Fair Deal* scheme.

We briefly describe each of the above demand-side supports below. We understand, however, that the Fair Deal scheme will not apply to nursing home residential units.

2.4.1 Private Nursing Homes Subvention scheme

Residents of registered private nursing/convalescent homes in Ireland may get a subvention from the Health Service Executive (HSE) if they are dependent and if they pass a means test. The objective of the subvention is to assist in defraying the costs of nursing home care. While the scheme is not designed to meet the full costs of care, in certain circumstances the HSE (where it has 'contracted beds' in private nursing homes) may pay the full cost of a private nursing home bed.

The means test for availing of the subvention factors in a resident's income and may also take account a person's assets, including principal residence. There are also maximum rates of subvention related to the level of dependency of the prospective resident.

The current levels of subvention under the scheme were reviewed in 2005/2006.

2.4.2 'A Fair Deal'

The Government recently announced a new system of nursing home care, called 'A Fair Deal on Nursing Home Care', which is expected to begin in January 2008. This new regime would effectively replace the existing Private Nursing Homes Subvention scheme. Five steps have been identified from the perspective of prospective residents of private nursing homes, namely:

1. An assessment of care needs
2. An assessment of means
3. Agreement re share of contribution towards costs of care
4. Selection of appropriate nursing home
5. Agreement re State's share of contribution agreed.

While the proposed operational approach to the new scheme is complex, an important issue within the context of this evaluation of the scheme of capital allowances/tax relief for investment in residential units associated to private nursing homes concerns the potential implications for future policy arising from the interaction of the two schemes. The main issue in this context concerns the impact of continued supports on the demand for nursing home places and the indirect impact this may have on the demand for nursing home residential units. In particular, in an environment where demand supports are likely to increase in the wider sector, we believe there is a strong argument for continuing to provide supply-side incentives towards further investment in capacity and that the current tax incentive scheme could have an important role to play in this context.

3 Review of Activity in Residential Units Sector

In this section we undertake a detailed review of recent activity in the private nursing home residential units sector. We begin by assessing the recent developments in the supply of such facilities, particularly since the introduction of the capital allowances scheme in 2002. We then consider developments in relation to occupancy rates, the cost of facility places, and the extent of construction activity. Following our review of developments to-date, we then consider the likely developments in relation to the demand for nursing home residential units in the future and the implications of this for the consideration of policy options going forward. Finally, we present a case study example of a scheme of residential units.

3.1 Supply of Facilities

3.1.1 Number of facilities and bed places

Owing to the fact that residential units associated with or on the same site as registered nursing homes are not subject to separate registration and/or inspection regimes, the number of such units is not subject to ongoing tracking or measurement by any of the State agencies.

In this evaluation we have drawn from a wide range of sources including the survey work undertaken by the Irish Nursing Homes Organisation (INHO) during 2005 and, most recently, in 2006. This survey was undertaken by Horwath Bastow Charlton and covered all registered private nursing homes in the State, of which there were 431 in 2005 and 432 in 2006. The number of respondents to the 2006 survey was 143, of which 18 respondents stated that they had independent residential units on-site.

The estimated overall number of nursing homes having associated residential units is indicated in Table 3.1. It is estimated that in 2005 a total of 46 registered private nursing homes within the State has associated residential units, while the number of nursing homes with residential units in 2006 is estimated at 54. This would suggest that extensive development has taken place in the sector in recent years.

Table 3.1: Estimated Number of Nursing Homes with Residential Units

Details	2005	2006
Estimated Total No. of Nursing Homes with associated Residential Units	46	54

Source: Indecon workings based on annual surveys undertaken by Irish Nursing Homes Organisation

The estimated number of residential units associated with these nursing homes is identified in the table below. Based on the evidence, it is estimated that some 964 nursing home residential units existed in 2006, indicating a substantial increase on the level of 792 units in 2004.

Table 3.2: Estimated Number of Residential Units

Details	2005	2006
Estimated Total No. of Residential Units	792	964

Source: Indecon workings based on annual surveys undertaken by Irish Nursing Homes Organisation

The number of bed places within the nursing homes residential units sector is estimated in the table below. We estimate that some 1,465 bed places were in existence in the sector in 206, up from 1,086 in 2005 and indicating a growth of almost 35% in one year alone in the supply of beds in the sector.

Table 3.3: Estimated Number of Residential Unit Bed Places

Details	2005	2006
Estimated Total No. of Beds in Residential Units	1,086	1,465

Source: Indecon workings based on annual surveys undertaken by Irish Nursing Homes Organisation

The analysis of the overall numbers of nursing home residential units and associated bed spaces would indicate that growth in the sector has been very strong in recent years.

3.1.2 Geographic location of facilities

The table below provides an indication of the geographic location of nursing home residential units. Based on the responses to the INHO annual survey in 2006, it can be seen that the largest concentrations of residential units associated with private nursing homes are located in the South Western, Southern, East Coast and North Eastern HSE regions.

Table 3.4: Geographic Location of Residential Units by HSE Area –2006*

Area	2006 - % of Total Residential Units
East Coast Area	17.2
Midland Area	5.0
Mid Western Area	6.9
North Eastern area	13.8
Northern	9.7
North Western	-
South Eastern	-
South Western	24.8
Southern	16.6
Western	6.0
Total	**100.0**

Source: Irish Nursing Homes Organisation, Survey of Registered Private Nursing Homes, 2006
* 2006 figures based on 18 respondents stating they had independent living/sheltered accommodation units on-site, with a total of 319 units.

A further indication of the location of bed places within these residential units is provided by the figures in the next table, which again confirm that the largest numbers of residential unit beds are located in the South Western, Southern, East Coast and North Eastern HSE regions.

Table 3.5: Number of Beds Associated with Residential Units by HSE Area – 2005 and 2006*

Area	2006 - % of Total Beds in Residential Units
East Coast Area	20.4
Midland Area	4.9
Mid Western Area	2.5
North Eastern area	12.8
Northern	6.6
North Western	-
South Eastern	-
South Western	30.7
Southern	17.5
Western	4.5
Total	100.0

Source: Irish Nursing Homes Organisation, Survey of Registered Private Nursing Homes, 2006
* 2006 figures based on 18 respondents stating they had independent living/sheltered accommodation units on-site, with a total of 319 units. 2005 figures based on 11 respondents stating they had independent living/sheltered accommodation units on-site, with a total of 191 units.

3.1.3 Size of Residential Units

An indication of the typical size of residential unit developments associated with registered private nursing homes is provided by the figures in the table below. Based on the survey evidence for 2006, it can be seen that the largest proportion (over 60%) of residential units fall within the 60+-bed category, which account for over 68% of the estimated total number of beds.

Table 3.6: Size Category Breakdown of Nursing Home Residential Units in 2006

Size	% of Residential Units	% of Beds in Residential Units
1 (1-25 beds)	-	-
2 (26-39 beds)	10.0	7.4
3 (40-59 beds)	29.5	24.1
4 (60 plus beds)	60.5	68.5

Source: Irish Nursing Homes Organisation, Survey of Registered Private Nursing Homes, 2006

3.2 Dependency Levels among Residents

Residential units are intended for medically certified people who wish to maintain their independent living status within a sheltered caring environment. In this context, residents are likely to differ from those in nursing homes in terms of their dependency levels. To establish this, we used new data from the survey undertaken by Indecon as part of this study. As detailed results were obtained from 6 nursing home respondents stating that they had associated residential units, caution must be exercised in interpreting the results but in the absence of any on-going monitoring of these units, the results represent a valuable indication on this issue. An indication of the typical dependency levels of residents living in residential units associated with nursing homes is provided by the figures in the table below. The Low Dependence classification refers to facilities which provide basic services for residents, while the High Dependence classification refers to facilities which provide more specialised services in terms of personal and medical care. Indecon's survey of private nursing homes indicates that among nursing homes surveyed having associated residential units some 43% cater for low dependence residents while 57% house high dependence residents. An issue arises concerning the low dependence residents of whether the units are primarily retirement homes and this highlights the merits of ensuring enforcement of medical certificates.

Table 3.7: Classification of Private Nursing Homes with Associated Residential Units— "High Dependence"/ "Low Dependence" Facilities

Classification	% of Residential Unit Facilities
Low Dependence	42.9
High Dependence	57.1
Total	**100**

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

3.3 Occupancy Rates

One indication of the take-up and demand for residential units is the occupancy rate of these units. The figures presented in the table below, based on the INHO's recent survey, point to a wide variation across regions in average occupancy rates for residential units associated with private nursing homes. Overall, the evidence suggests an average occupancy rate across the State within these facilities of over 70% in 2006. There may, however, be timing issues involved as some units are recently built.

Table 3.8: Average Occupancy Levels within Nursing Homes with Associated Residential Units by HSE Region

Area	Average Occupancy - %
East Coast Area	98%
Midland Area	-
Mid Western Area	100%
North Eastern area	10%
Northern	83%
North Western	-
South Eastern	-
South Western	87%
Southern	47%
Western	-
Total	**71.5%**

Source: Irish Nursing Homes Organisation, Survey of Registered Private Nursing Homes, 2006
"-" = Insignificant

3.4 Level of Construction Activity

The table below provides an indication of the year of construction of nursing home residential units based on Indecon's survey of private nursing homes. According to the survey evidence, the majority (over 57%) of residential units attached to private nursing homes were constructed following the introduction of the capital allowances/tax relief scheme in 2002.

Table 3.9: Year of Construction of Residential Units Associated with Private Nursing Homes

Year	% of Responses
Pre-2002	42.9
2002 onwards	57.1

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland, 2006

Planning Activity

The extent of construction activity in the nursing homes residential units sector can be seen from the data presented in the table below on the numbers of planning applications and approvals for such schemes over the period since 2000. The figures collated from the local authorities indicate that there has been a steady increase in applications for residential unit developments from 4 in 2000 to 24 in 2004, with an associated increase in approvals from 2 to 12 over the same period. This increased supply since 2002 in particular is likely to have been stimulated by the availability of tax incentives for these schemes.

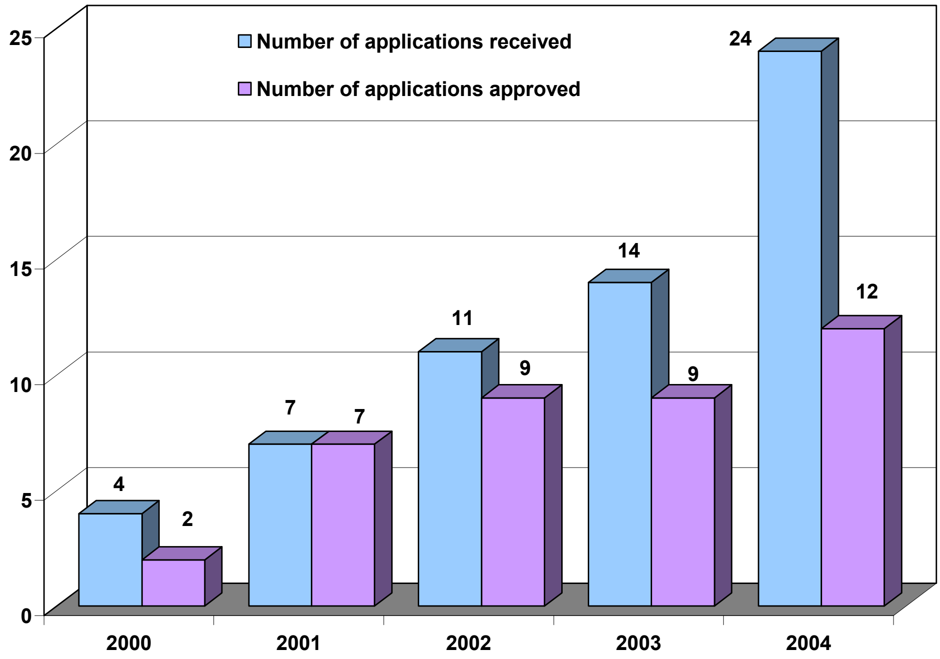
Table 3.10: Details of Planning Applications - Total Number of Applications: Associated Residential Units, 2000-2004

Detail	2000	2001	2002	2003	2004
Number of applications received	4	7	11	14	24
Number of applications approved	2	7	9	9	12
Number of applications awaiting decision	0	0	1	1	7

Source: Indecon Confidential Survey of Local Authorities.

A graphical illustration of the number of planning applications submitted and the number of applications approved for nursing home residential unit schemes is presented in the figure below. This highlights the strong growth in activity in this area, particularly since the introduction of the capital allowances in 2002.

Figure 3.1: Details of Planning Applications - Total Number of Applications: Residential Units Associated with Nursing Homes - 2000-2004



Source: Indecon Confidential Survey of Local Authorities.

A further indication of the potential future pipeline of supply in relation to residential units can be seen from the estimates we have developed based on the evidence compiled through the 2006 survey of private nursing homes undertaken by the INHO. In particular, the table below presents our estimates of the overall number of nursing homes planning to develop associated residential units, and the number of units and beds involved. We estimate based on the INHO findings that some 57 private nursing homes are planning to build independent residential units, involving over 800 units and over 1,000 beds.

Table 3.11: Estimated Number of Private Nursing Homes Planning to Construct Associated Residential Units and Numbers of Units and Beds Involved

Plans/Details	No.
Estimated total nursing homes planning units	57
Estimated total units planned	807
Estimated total beds planned	1,069

Source: Irish Nursing Homes Organisation, Survey of Registered Private Nursing Homes, 2006

3.4.1 Nature and Extent of Care Provided

The table below summarises the findings from Indecon's survey of private nursing homes in relation to the nature of services provided within residential units associated with these nursing homes. A majority (53.6%) of respondents specified Medical Care as being the main service available to residents within these facilities, while 28.6% of respondents cited nursing care and 17.9% highlighted the operation of day care centres attached to the associated nursing homes.

Table 3.12: Nature of Services Provided by Residential Units

Services	% of Responding Providing Service
Day Care Centre	17.9
Nursing Care	28.6
Medical Care	53.6

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

The table below presents the findings from Indecon's survey of nursing homes in relation to the extent of care provided to residents within associated residential units, as measured by the average number of hours per day provided by staff members.

Table 3.13: Extent of Care Being Provided in Private Nursing Home Residential Units - Average Number of Hours per Day provided by Staff Members

Hours per Day	% of Respondents
0-1 hours	40
1-2 hours	20
2-3 hours	20
2-4 hours	20
Greater than 4 hours per day	0

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

The largest proportion of respondents, 40%, indicated that the typical extent of care provided to residents within residential unit facilities is up to 1 hour per day. A further 20% of respondents indicated that the extent of care varies between 1-2 hours per day, while 20% indicated that their extent of care is 2-3 hours per day, and the final 20% of respondents indicated that the extent of care is 2-4 hours per day. It is notable that no respondents to our survey indicated that the typical extent of care provided by nursing home staff to residents in associated residential unit facilities is above 4 hours per day.

The nature and extent of care provided to residents within residential units constitutes an important issue within the context of ensuring that the marketing and operation of these facilities is in accordance with the objectives of supporting the development of such facilities for medically certified persons. This aspect is one that we believe should be addressed through the operation of adequate registration, inspection and monitoring systems.

3.5 Assessment of Future Demand for Residential Units

An issue in evaluating the merits of a particular investment scheme such as the tax relief for residential units associated with registered nursing homes concerns the likely evolution of demand for the product/service which investment in the sector is designed to support.

Age profile of residents in private nursing homes and related accommodation

In relation to residential units, a key driver of demand for such accommodation is the number of persons in the older age brackets, which, as indicated by the survey evidence presented in the table below, constitute the primary users of private nursing homes and related accommodation service in the State. In particular, it can be seen that almost 95% of residents are aged 65 and over.

Table 3.14: Age Profile of Residents in Private Nursing Homes and Related Accommodation*

Age Group	Under 40	40-64	65-69	70-74	75-79	80-84	85-89	90-94	95+
% of Residents	0.5	4.9	3.6	7.5	13.8	25.4	26.0	14.1	4.2

Source: Irish Nursing Homes Organisation, Annual Survey of Registered Private Nursing Homes

* Based on survey of all 431 registered private nursing homes in 2005.

While the demand for residential units associated with nursing homes will be subject to a range of economic and social factors, including the demand for semi-independent as opposed to high dependence accommodation, the figures above highlight the importance of demographic trends involving the 65+ age group within the context of assessing the prospective demand for living spaces within residential units associated with private nursing homes. We would, however, expect that the age profile of occupants of nursing home residential units would be younger than that for nursing homes.

Projections for older age population groups

In this section we look at the projected increase in the size of the population aged 55 years and over in Ireland, and how this might affect the requirement for beds in residential units linked to nursing homes.

The size of the population in Ireland aged 55 years and older is projected, under the CSO's M1F2 scenario, to slightly more than double over the next 30 years. Much of the growth in this age cohort is expected to come in those aged 65 years and older. The CSO expects the size of this particular group to almost treble from 465,000 to over 1,100,000 between 2006 and 2036 (Table 3.15).

Table 3.15: Population Projections by Age Group - 55+ year Age Groups - 2006-2036 - M1F2 Growth Scenario - '000 Persons

Age Group	2006	2011	2016	2021	2026	2031	2036
55-64	409.5	468.9	516.1	570.9	625.0	691.9	780.2
65-74	262.7	307.8	377.6	435.5	483.6	539.5	594.9
75-84	155.9	168.2	189.9	231.1	291.8	344.0	391.9
85+	46.9	55.1	63.6	74.7	90.7	118.8	158.5
Total Persons Aged 55+	**875.0**	**1,000.0**	**1,147.2**	**1,312.2**	**1,491.1**	**1,694.2**	**1,925.5**
Total Persons Aged 65+	**465.5**	**531.1**	**631.1**	**741.3**	**866.1**	**1,002.3**	**1,145.3**

Source: CSO, Population Projections

The size of the elderly population will grow as a proportion of the population as well as in absolute numbers. Currently, 21% of the population is aged 55 years and older, and 11% are aged 65 years and older. As shown in Table 3.16, these percentages are expected to grow steadily over the next 30 years, reaching 34% and 20%, respectively, under the M1F2 scenario. The M1F2 and M2F1 scenarios constitute mid-range scenarios from a wider range of scenarios, based on a series of assumptions regarding migration and fertility.

Table 3.16: Population Projections by Age Group - 55+ year Age Groups - 2006-2036 - M1F2 Growth Scenario - % of Total Population

Age Group	2006	2011	2016	2021	2026	2031	2036
55-64	9.8	10.5	10.7	11.3	11.8	12.6	13.8
65-74	6.3	6.9	7.9	8.6	9.1	9.8	10.5
75-84	3.7	3.7	3.9	4.6	5.5	6.3	6.9
85+	1.1	1.2	1.3	1.5	1.7	2.2	2.8
Total Persons Aged 55+	**21.0**	**22.3**	**23.9**	**25.9**	**28.1**	**30.8**	**34.0**
Total Persons Aged 65+	**11.2**	**11.8**	**13.1**	**14.6**	**16.3**	**18.3**	**20.2**

Source: CSO, Population Projections

The forecasts under the CSO's M2F1 growth scenario are very similar to, though slightly lower than, those under the M1F2 scenario. Table 3.17 below presents the projected numbers of persons aged 55+ and aged 65+ under the M2F1 scenario. Under this scenario, the number of persons aged 55+ in the State is projected to reach almost 1.14 million by 2016 and 1.46 million by 2026, while the population aged 65+ is forecast to expand to almost 627,000 by 2016 and to 853,000 persons by 2026.

Table 3.17: Population Projections by Age Group - 55+ year Age Groups - 2006-2036 – M2F1 Growth Scenario - '000 Persons

Age Group	2006	2011	2016	2021	2026	2031	2036
55-64	409.5	467.2	510.7	561.4	610.0	668.2	740.7
65-74	262.7	306.8	374.3	429.8	475.0	527.7	578.4
75-84	155.9	168.0	189.0	229.1	288.3	338.5	384.2
85+	46.9	55.1	63.5	74.3	90.1	117.7	156.4
Total Persons Aged 55+	**875.0**	**997.1**	**1,137.5**	**1,294.6**	**1,463.4**	**1,652.1**	**1,859.7**
Total Persons Aged 65+	**465.5**	**529.9**	**626.8**	**733.2**	**853.4**	**983.9**	**1,119.0**

Source: CSO, Population Projections

The table below presents the figures above in percentage terms relative to the population as a whole, highlighting the projected increase in the relative importance of the 65+ age group, particularly over the next 10 years.

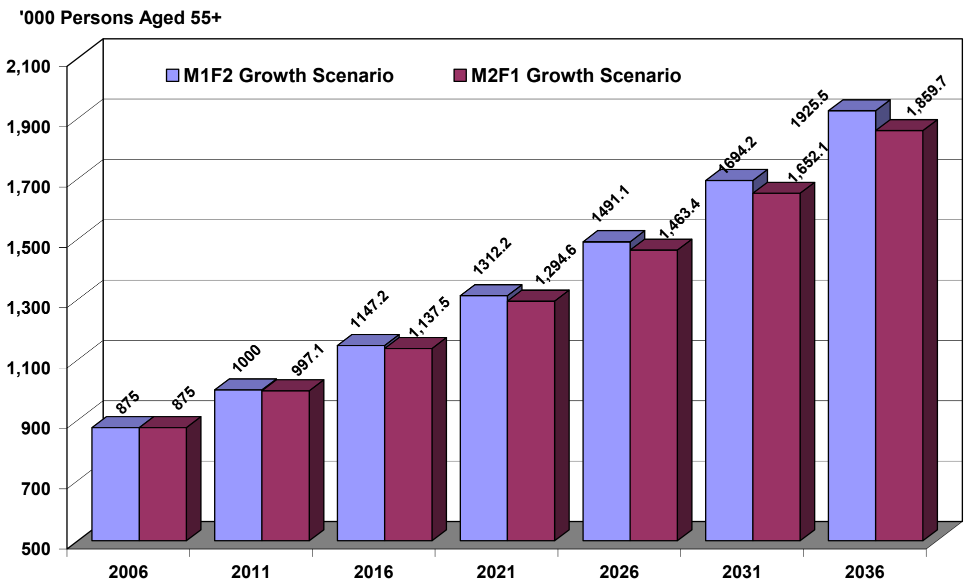
Table 3.18: Population Projections by Age Group - 55+ year Age Groups - 2006-2036 – M2F1 Growth Scenario - % of Total Population

Age Group	2006	2011	2016	2021	2026	2031	2036
55-64	9.8	10.5	10.9	11.5	12.2	13.0	14.1
65-74	6.3	6.9	8.0	8.8	9.5	10.3	11.0
75-84	3.7	3.8	4.0	4.7	5.7	6.6	7.3
85+	1.1	1.2	1.4	1.5	1.8	2.3	3.0
Total Persons Aged 55+	**21.0**	**22.4**	**24.3**	**26.6**	**29.2**	**32.1**	**35.4**
Total Persons Aged 65+	**11.2**	**11.9**	**13.4**	**15.1**	**17.0**	**19.1**	**21.3**

Source: CSO, Population Projections

The figure below compares the CSO's two scenarios for population growth among the 55+ age group. This highlights the expected strong growth in this age group going forward.

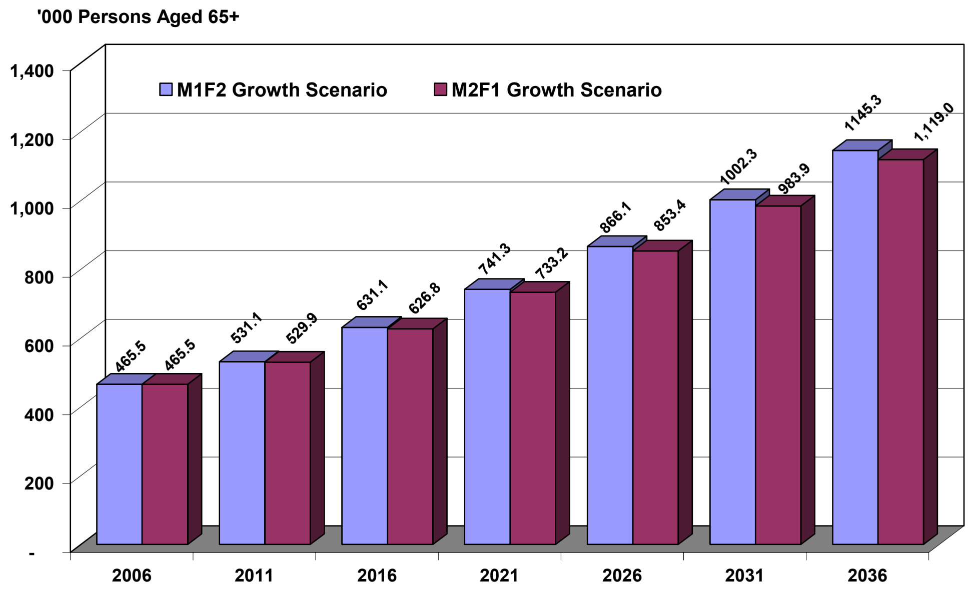
Figure 3.2: Projected Population Aged 55+ - Comparison of Growth Scenarios



Source: CSO, Population Projections

The figure below presents a graphical comparison of the CSO's scenarios for population growth among the critical 65+ age group which constitute the principal resident group within the nursing homes and related accommodation sector.

Figure 3.3: Projected Population Aged 65+ - Comparison of Growth Scenarios



Source: CSO, Population Projections

Projections for Demand for Residential Unit Beds

We now combine the population projections described above with our estimate of current number of beds per person aged over 55 and 65 years, respectively, to yield a series of projections for the likely future demand for residential unit beds. In Table 3.1 we used INHO-based survey evidence to estimate that the total number of beds in residential units per 1,000 people aged 55+ years and aged 65+, at 1.7 per 1,000 persons aged 55+ and 3.1 beds per 1,000 people aged 65+ respectively.

In modelling the future demand for residential unit beds, we assume the following:

- A constant ratio of the number of beds relative to the populations aged 55+ and 65+ over the projection period;
- Population growth among the 55+ and 65+ age groups in line with the CSO's M1F2 and M2F1 scenarios, presented above.

Our projections for the demand for nursing home residential unit bed spaces based on the CSO's M1F2 projections for the older age population are shown in Table 3.19. We estimate that the required growth in residential unit beds for those aged 55 years and older will be fairly stable, but at a high rate of about 14% per year. However, for those aged 65 years and older, the required growth will need to be stronger between 2011 and 2026 (over 18% between 2011 and 2016) than in the latter period towards 2036.

Table 3.19: Scenarios for Projected Demand for Nursing Home Residential Unit Beds - 2006-2036 - Scenario 1: Estimated Number of Residential Units Based on M1F2 Projection for Population Growth

Scenario Details	2006	2011	2016	2021	2026	2031	2036
Estimated Total No. of Beds in Residential Units:							
Based on Projected Population Aged 55+	1,465	1,666	1,912	2,187	2,485	2,823	3,209
% Growth		*13.7*	*14.7*	*14.4*	*13.6*	*13.6*	*13.7*
Based on Projected Population Aged 65+	1,465	1,654	1,965	2,308	2,697	3,121	3,566
% Growth		*12.9*	*18.8*	*17.5*	*16.8*	*15.7*	*14.3*

Source: Indecon workings based on annual surveys undertaken by Irish Nursing Homes Organisation and CSO, Population and Migration Estimates, April 2006

The projections for the demand for residential unit bed spaces based on the M2F1 scenario for population growth among the older age groups are marginally different from those under the M1F2 scenario and are shown in Table 3.20. Since the projection under M2F1 is a slightly more conservative forecast for population growth, so the expected number of beds required is lower too. There remains however the pressing rise in the requirement over the next 20 years than was estimated from the M1F2 scenario.

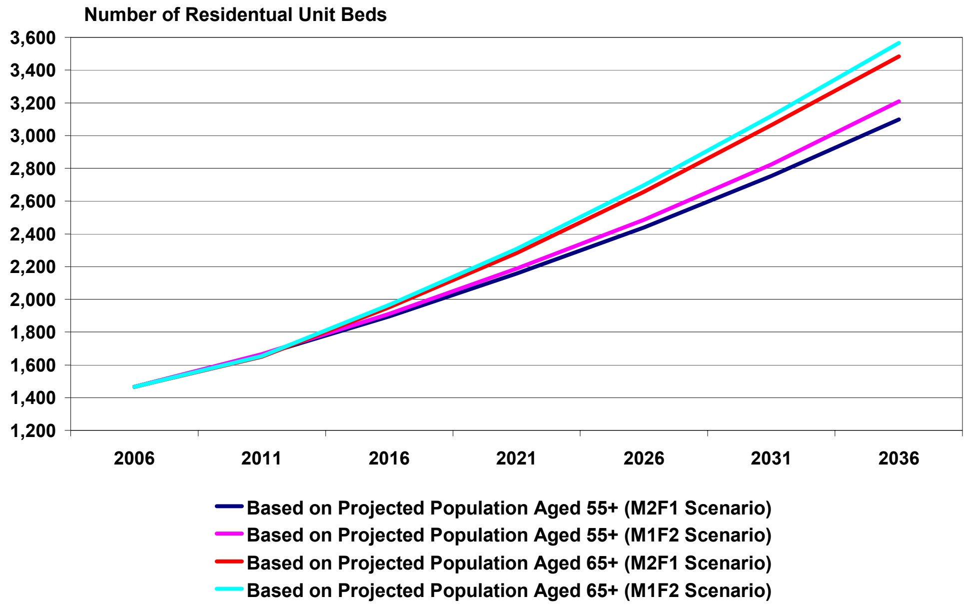
Table 3.20: Scenarios for Projected Demand for Nursing Home Residential Unit Beds - 2006-2036 - Scenario 1: Estimated Number of Residential Units Based on M2F1 Projection for Population Growth

Scenario Details	2006	2011	2016	2021	2026	2031	2036
Estimated Total No. of Beds in Residential Units:							
Based on Projected Population Aged 55+	1,465	1,662	1,896	2,157	2,439	2,753	3,099
% Growth		*13.4*	*14.1*	*13.8*	*13.0*	*12.9*	*12.6*
Based on Projected Population Aged 65+	1,465	1,650	1,951	2,283	2,657	3,063	3,484
% Growth		*12.6*	*18.3*	*17.0*	*16.4*	*15.3*	*13.7*

Source: Indecon workings based on annual surveys undertaken by Irish Nursing Homes Organisation and CSO, Population and Migration Estimates, April 2006

The forecast numbers of residential beds required, according to the projected increases in the size of the two population cohorts and for each of the two CSO growth scenarios, are compared in graphical form in Figure 3.4 overleaf. This chart illustrates how the requirement for residential unit beds is likely to increase sharply over the next 30 years.

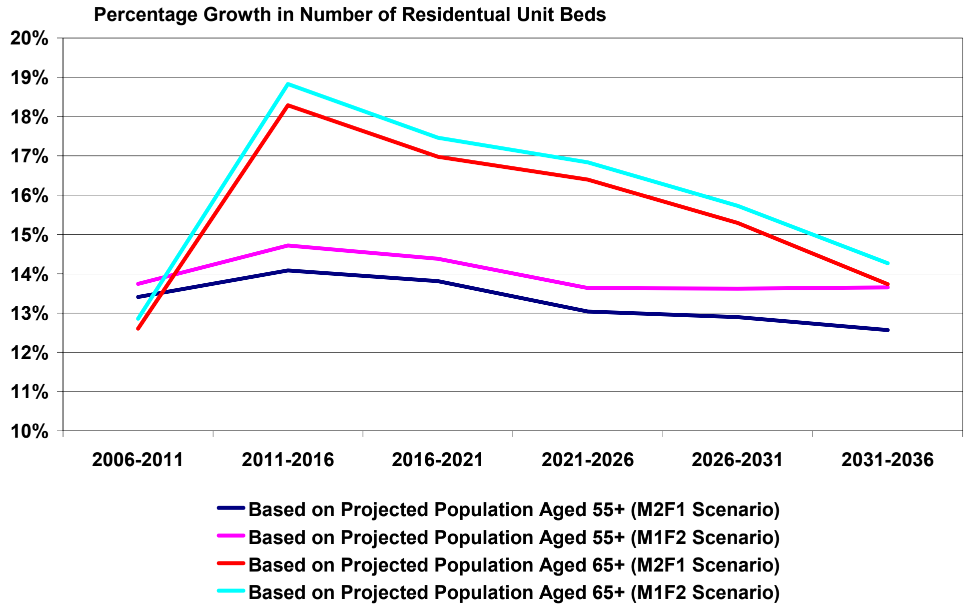
Figure 3.4: Projected Population Aged 55+ and 65+ - Comparison of Growth Scenarios



Source: Indecon workings based on annual surveys undertaken by Irish Nursing Homes Organisation and CSO, Population and Migration Estimates, April 2006

Moreover, the demand for residential unit bed spaces may be especially urgent in the short to medium term, reflecting the anticipated strong growth in the over 65 population age group over the next 10 years. In particular, as highlighted in Figure 3.2 overleaf, the percentage increase in beds required will be around 17% every five years between 2011 and 2026.

Figure 3.5: Projected Population Aged 55+ and 65+ - Comparison of Growth Scenarios



Source: Indecon workings based on annual surveys undertaken by Irish Nursing Homes Organisation and CSO, Population and Migration Estimates, April 2006

Implications of projected growth in demand

This high required growth rate of prospective demand for beds, particularly in the short to medium term, implies potential support for continuing the provision of incentives towards investment through the tax relief scheme.

However, it will be important to consider this within the context of the overall economic appraisal of the current tax relief scheme for nursing home residential units and also within the context of demand-side measures supporting the wider nursing home sector, including the current private nursing home patient subvention scheme and the recently announced 'A Fair Deal'.

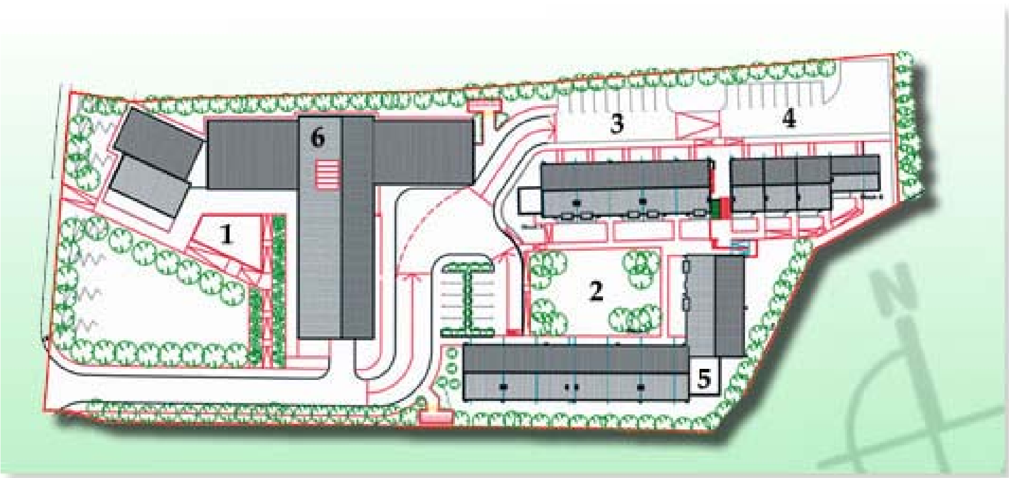
3.6 Case Study Example

Before examining the detailed aspects of the impacts and the appraisal of the costs and benefits of the scheme, it is instructive to consider a case study example of residential unit development associated with a private nursing home which benefits from the capital allowances/tax relief scheme. In this case study we set out an example of a development, including the features of the development in terms of the cost of purchase of units, the numbers of units, the characteristics of these units and the level of services provided. A related issue concerns the operation of the incentive scheme for investment in a residential unit development from the perspective of the investor and we consider this aspect in detail in Section 5.

3.6.1 Residential Unit Development Example – Costs and Features

The figure below presents a site map of a scheme of residential units adjacent to an existing nursing home.

Figure 3.6: Case Study Example of Residential Unit Development - Summary Details and Features - Site map



Source: Indecon research

The figure below presents a summary description of the case study development and it can be seen that the development has a total of 41 units offering a range of facilities and services. The current price range for purchase of the units is between €355,000 and €385,000, with a guaranteed annual rental income in year 1 of €8,000.

Figure 3.7: Case Study Example of Residential Unit Development - Summary Details and Features

Location: Cork
Number of Residential Units in Development: 41
Management Company: Yes
Adjacent Nursing Home: Yes
Available Medical Services to Residential Units: Yes, Doctor on Call and nursing care services
Specification of Units:
Block A: Ground Floor - 1-Bed Unit/Apartment
Block A: First - 2-Bed Unit/Apartment
Block A: Second Floor - 1-Bed Unit/Apartment
Block B: Ground Floor - 1-Bed Unit/Apartment
Block B: First Floor - 2-Bed Unit/Apartment
Block C: Ground Floor - 2-Bed Unit/Apartment
Block C: First Floor - 1-Bed Unit/Apartment

1-Bed Apartment: Bedroom, Kitchen, Dining and Living Areas, Bathroom, Utility and Balcony

Features, Facilities and Recreation:

- 1&2 Bed Homes with Balconies
- 10 Year Structural Guarantee
- Located within the Community
- Fully Furnished and Accessible
- Specialised Beds and Accessible Bathrooms
- Electric Heating
- Caretaker
- Lifts
- Local Supermarket Delivery Service
- Putting Green on Site
- Bowling Green on Site
- Car Parking
- Landscaped Grounds with pond
- Security.

Price of Units: 1-bed Unit - €355,000
2-Bed Units - €385,000

Estimated Rental Income: Guaranteed rental income in Year 1 of €8000

Source: Indecon research

4 Evaluation of Impacts of Tax Incentive

In this section we focus on the detailed evaluation of the costs to the Exchequer and the economic benefits arising through the operation of the capital allowances/tax reliefs available in relation to expenditures on the development of residential units associated with private nursing homes. We begin by examining the level of utilisation of the incentive scheme.

4.1 Level of Incentive Utilisation

Revenue Commissioners data on tax returns

As part of his ongoing review of tax incentive schemes, the Minister for Finance introduced from 2004 a new requirement whereby individuals utilising a tax incentive scheme must complete a new section in their annual tax return form which details the nature of tax incentives utilised and the amounts claimed under these reliefs during the tax year.

During this study, Indecon have consulted with the Revenue Commissioners, who kindly provided the consultancy team with summary data concerning the numbers of claimants and the overall amounts claimed under the residential units relief scheme during 2004 and 2005. The table below summarises the numbers of claimants and amounts claimed in these periods. For reference purposes we also include details in relation to the relief claimed in relation to nursing homes.

Table 4.1: Private Nursing Homes Residential Units Capital Allowances/Tax Relief Scheme - Details of Numbers of Claimants and Amounts Claimed - 2004 and 2005

Claimants/Amounts Claimed	No. of Claimants		€ Million	
	2004*	2005	2004*	2005
Residential Units associated with Nursing Homes	11	46	0.3	1.9
Nursing Homes	287	431	16.6	26.4

Source: Revenue Commissioners
* 2004 figures elate to relief claimed for 'Housing for the Elderly and Infirm'

According to the Revenue figures[1], a total of 46 claimants filed claims for tax relief under the residential unit scheme totalling €1.9 million during 2005. This compares with 11 claimants and €0.3 million in allowances claimed during 2004.

These figures highlight the accelerating level of activity in the residential units sector and it should be noted that given the lead-in time required to bring such developments to completion, and the relatively short time since the incentive scheme was introduced in 2002, further strong growth in activity and the level of claims is likely to become evident from 2006 onwards.

Indecon survey evidence

The table below presents the evidence from Indecon's survey research on residential units associate with private nursing homes in relation to the extent to which the development of these units has entailed the utilisation of the capital allowances/tax relief scheme introduced in 2002. It is notable that all the nursing home respondents to our survey who stated that they had associated residential unit facilities had availed of the tax incentive scheme.

Table 4.2: Proportion of Nursing Homes with Residential Units that have Utilised Tax Incentive Scheme over Past 5 years

Usage of Tax Incentive	% of Respondents
Nursing Homes with Residential Units that have availed of tax incentive over past 5 years	100%

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

[1] The Revenue Commissioners have stated that the interpretation of these figures should be treated with some degree of caution arising form the concern that the 2004 tax return form may not have been interpreted and completed correctly in respect of the section dealing with tax reliefs. In this respect, the figures presented for 2004 may underestimate the true level of activity taking place in the sector.

4.2 Impact of Tax Incentive

4.2.1 Impact on Supply of Facility Places

The table below summarises the evidence from Indecon's survey of nursing homes with residential unit facilities in relation to the views of proprietors on the effectiveness of the tax incentive scheme for residential units in increasing the supply of facility places. It is notable that 100% of respondents were of the view that the capital allowances/tax reliefs have been effective in boosting the supply of residential unit places. While practitioner views on such issues do not in themselves represent sufficient evidence to derive an overall conclusion, the views are consistent with empirical evidence on the significant expansion in supply post the introduction of the allowances.

Table 4.3: Views of Private Nursing Homes with Residential Units on Effectiveness of Property-based Tax Incentive Scheme in Increasing Supply of Facility Places

Level of Effectiveness	% of Respondent Facilities that have Availed of Tax Incentive
Effective	100
Neither effective nor ineffective	0.0
Ineffective	0.0
Total	**100%**

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

4.2.2 Impact on the Cost of Facility Places

An issue within the context of the evaluation of the costs and benefits of the tax incentive scheme for residential units concerns the impact on supply and prices facing consumers or prospective residents of these developments. The table below presents the Indecon survey evidence in relation to the movement in the average cost of residential unit places since 2000. Respondents to Indecon's survey stated that in 2000, the weekly average cost of residential unit places was €400, while in 2006 the average weekly cost was €440.80. This represents a 10.2% increase in the weekly average cost over this period.

Table 4.4: Average Cost of Residential Unit Places - 2000 and 2006 - € per Week

	2000	2006	*Growth Rate (%)*
Average cost of residential unit places per week - €	400	440.8	*10.2%*

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

The table below presents the findings from Indecon's survey on the views of nursing homes with residential units on the overall effectiveness of the tax incentive scheme in reducing the cost of residential unit places. The research indicates that some 50% of respondents who have availed of the incentive scheme are of the view that the scheme has been effective in reducing the cost of residential unit places, while 50% were of the view that the scheme has been neither effective nor ineffective in reducing the cost of residential unit places. In the context of forecasts of significant future demand, the need to ensure that supply is forthcoming is critical in terms of preventing a rapid escalation in prices.

Table 4.5: Views of Private Nursing Homes with Residential Units on Effectiveness of Property-based Tax Incentive Scheme in Reducing the Cost of Residential Unit Places

Level of Effectiveness	% of Respondents Facilities that have Availed of Tax Incentive
Effective	50.0
Neither effective nor ineffective	50.0
Ineffective	0.0
Total	**100%**

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

In our view, significant weight should be given to ensuring supply is sufficient to keep pace with demand in the sector as, in the absence of sufficient supply, prices for residential unit places could increase dramatically, acting against measures to enhance affordability.

4.2.3 Impact on Site Prices

The views of nursing homes in relation to the impact on site prices of the tax incentive scheme for investment in associated residential units are profiled in the table below. Overall, 13.3% of respondents held the belief that the scheme has ultimately resulted in higher site prices.

Table 4.6: Views of Private Nursing Homes with Residential Units on Impacts of Property-based Tax Incentive Scheme – Proportion of Respondents believing that the Scheme has Resulted in Higher Site Prices

	% of Survey Respondents Believing Impact to be a Result of the Tax Incentive
Respondent Group	**Facilities that have Availed of Tax Incentive**
Private Nursing Homes with Residential Units	13.3

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

4.2.4 Impact on Construction Costs

Evidence in relation to the impact of the tax incentive scheme for investment in residential units on construction costs is provided by the survey findings in the next table, which indicate that 13.3% of nursing home respondents to Indecon's survey were of the view that the incentive scheme has resulted in higher construction costs.

Table 4.7: Views of Private Nursing Homes with Residential Units on Impacts of Property-based Tax Incentive Scheme – Proportion of Respondents believing that the Scheme has Resulted in Increased Construction Costs

Respondent Group	% of Survey Respondents Believing Impact to be a Result of the Tax Incentive Facilities that have Availed of Tax Incentive
Private Nursing Homes with Residential Units	13.3

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

4.2.5 Impact on Financial Returns to Promoters

While being an important factor impacting on incentives, the extent to which the tax reliefs available for investment in residential units result purely in higher financial returns for promoters may be seen as a negative side effect of this type of scheme, if the scheme does not ultimately meet the objectives of boosting the supply and reducing the costs of such facilities. Among nursing homes, 13.3% of respondents to our survey were of the view that the tax relief scheme has resulted in higher returns to promoters.

Table 4.8: Views of Private Nursing Homes with Residential Units on Impacts of Property-based Tax Incentive Scheme – Proportion of Respondents believing that the Scheme has Resulted in Increased Financial Return to Promoters

Respondent Group	% of Survey Respondents Believing Impact to be a Result of the Tax Incentive Facilities that have Availed of Tax Incentive
Private Nursing Homes with Residential Units	13.3

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

4.2.6 Impact on Property Prices

Another potential side effect of the tax incentive scheme for investment in residential units associated with private nursing homes would be where increased activity gives rise to higher property prices rather than an increase in the supply of such facilities and associated beds. Indecon's survey research with the nursing homes sector suggests that there may be significant property price inflation in this sector, although whether this relates solely to the impact of the incentive scheme or to general property market price inflation is difficult to identify.

Table 4.9: Views of Private Nursing Homes with Residential Units on Impacts of Property-based Tax Incentive Scheme – Proportion of Respondents believing that the Scheme has Resulted in Higher Property Prices Compared to Non-Tax Incentivised Properties

Respondent Group	% of Survey Respondents Believing Impact to be a Result of the Tax Incentive
	Facilities that have Availed of Tax Incentive
Private Nursing Homes with Residential Units	26.7

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

4.2.7 Displacement, Deadweight and Opportunity Cost

The evaluation of the overall effectiveness and net cost of a tax incentive scheme such as that available in respect of investment in residential units associated with private nursing homes must address the issue of extent of activity would have occurred in the absence of the scheme. This relates to the issue of *economic deadweight*, which refers to the extent to which an activity would have proceeded anyway in the absence of incentives provided through a tax relief scheme or other support mechanism. Where deadweight is judged to be high, this would suggest that a high proportion of projects are likely to have gone ahead within a similar timeframe, even in the absence of the incentive scheme. This suggests that un-necessary public resources may be expended on areas exhibiting high levels of deadweight. Moreover, these resources have an *opportunity cost*, in that they may have been employed to better effect and have achieved higher returns on alternative projects or policy objectives.

As part of our research with the private nursing homes sector, we sought the views of facilities on the likelihood that some or all projects would have preceded in the absence of the tax incentive scheme for investment in residential units. It is notable that the vast majority (75%) of respondents were of the view that some projects would not have proceeded in the absence of the incentive scheme.

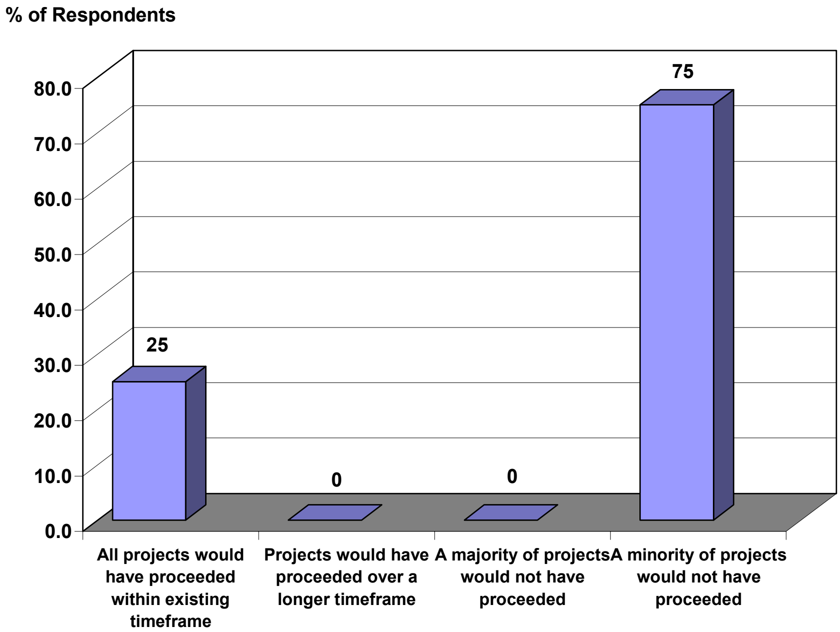
Table 4.10: Views of Private Nursing Homes with Residential Units on the Likelihood that Capital Investment in Residential Units would have Proceeded in Absence of Property-based Tax Incentive Scheme

View	% of Survey Respondents Facilities that have Availed of Tax Incentive
All projects would have proceeded within existing timeframe	25.0
Projects would have proceeded over a longer timeframe	0.0
A majority of projects would not have proceeded	0.0
A minority of projects would not have proceeded	75.0
Total	**100%**

Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

The views summarised in the above table are also expressed graphically in Figure 4.1 below, highlighting the belief among nursing homes that some residential unit developments would not have proceeded within the existing timeframe without the incentive provided through the tax relief scheme.

Figure 4.1: Views of the Nursing Homes with Residential Units Likelihood that Projects (i.e. Capital Investment in Residential Units) Would Have Proceeded in Absence of Property-based Tax Incentive Scheme



Source: Indecon Confidential Survey of Nursing Home/Convalescent Facilities in Ireland.

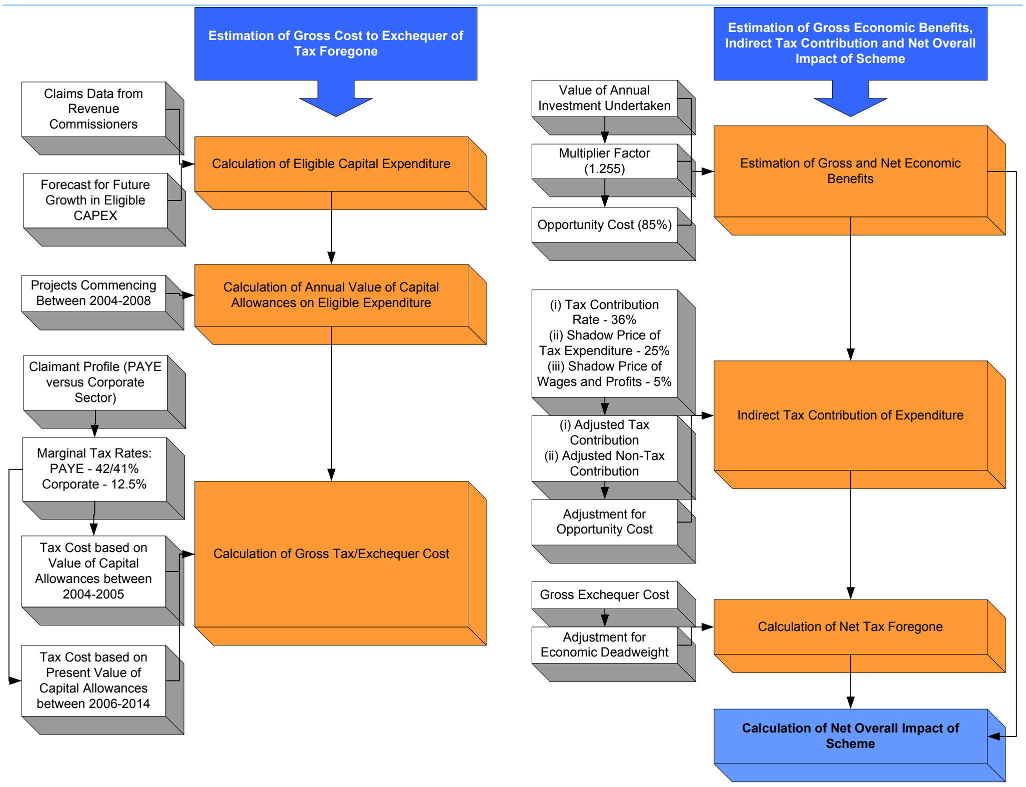
4.3 Modelling of Exchequer Costs and Economic Impact

We now turn to the evaluation of the Exchequer costs and economic impacts/benefits of the scheme of capital allowances/tax relief for investment in residential units associated with private nursing homes. We begin by setting out the methodological approach to the modelling/appraisal of the scheme.

4.3.1 Methodological Framework for Evaluation

A schematic summary of our approach and components of the estimation of the net overall impact of the capital allowances/tax relief for investment in residential units associated with private nursing homes is presented in Figure 4.2.

Figure 4.2: Schematic Summary of Components of Calculation of Net Overall Impact of Capital Allowances/Tax Relief Scheme for Investment in Residential Units Associated with Private Nursing Homes



Source: Indecon

We explain each element in the evaluation framework, including the assumptions applied within each component, in more detail below.

4.4 Estimated Investment in the Sector

The costs to the Exchequer and the economic benefits arising from the operation of the scheme of capital allowances/tax relief for investment in residential units associated with private nursing homes will be a function of the level of eligible capital expenditure undertaken in the sector.

The first step in evaluating the costs and benefits of the operation of the scheme, therefore, is to calculate the level of capital investment which has taken place to-date and the likely level of future expenditures that are eligible for capital allowances under the scheme.

4.4.1 Eligible Capital Expenditure

Our approach to estimating the level of investment taking place in relation to residential units attached to private nursing homes entails a number of component, as follows:

- Identification of level of claims made for tax relief, based on information lodged as part of annual tax returns submitted to Revenue Commissioners;
- Estimation of annual eligible capital expenditures related to claimed levels of tax relief, based on 'grossing up' procedure utilising annual capital allowances available.

Eligible capital expenditure to-date

Given that the capital allowances/tax relief for capital expenditures on the development of residential units associated with private nursing homes was introduced in 2002, and taking into account the presence of a 'ramp up' period before the full impacts of the incentive become evident, we have assumed that new activity in the sector following the introduction of the relief does not become evident until 2004.

Our estimate of the implied total cumulative value of eligible capital expenditure on the development of residential units that have availed of the tax incentive scheme between up to 2005 is presented in the table below. We estimate a total cumulative value of eligible investment amounting to €12.7 million up to 2005.

Table 4.11: Estimate of Total Eligible Capital Expenditure on Development of Residential Units Associated with Private Nursing Homes - €

Detail	Estimated Value – Cumulative Eligible Expenditure 2004-2005 - €
Estimated cumulative eligible capital expenditure to 2005	12,666,667*

Source :Indecon Calculations based on data supplied by Revenue Commissioners
* Based on 'grossed up' value of cumulative claims made to Revenue Commissioners during 2004 and 2005 assuming 15% rate of capital allowance during first 5 years following expenditure.

Future eligible capital expenditures

In evaluating the costs and benefits of the capital allowances/tax reliefs pertaining to residential units, it is necessary to factor in anticipated future capital expenditures that may avail of the relief in addition to eligible expenditures since the introduction of the scheme.

In relation to likely future expenditures, while detailed information was not available to the consultancy team in relation to the likely course of future investment in the sector, we believe that the evidence from our review of planning applications, our assessment of future demographic development and implied demand, and the expressed plans of the nursing homes sector in this area together point to strong growth in the sector. For the purposes of this appraisal we have assumed that annual eligible capital expenditures grow at a rate of 10% per annum up until the current termination of the scheme in 2008. Based on this assumption the implied level of eligible capital expenditure which would qualify for capital allowances under the scheme over the period between 2006 and 2008 (when the current scheme is set to terminate) is indicated in the table below. We forecast eligible capital expenditure to increase towards €14.2 million in 2008 after €11.7 million in 2006 and €12.9 million in 2007.

Table 4.12: Projected Annual Eligible Capital Expenditure on Development of Residential Units Associated with Private Nursing Homes – 2006-2008 - €

	2006 - €	2007 - €	2008 - €
Estimate Annual Eligible Capital Expenditure*	11,733,333	12,906,667	14,197,333

Source: Indecon calculations
* Based on assumption that annual capital expenditures grow at a rate of 10% per annum between 2006 and 2008.

4.4.2 Calculation of Capital Allowances

To estimate the cost to the Exchequer of the tax foregone through the operation of the incentive scheme for investment in nursing home residential units, it is necessary to firstly calculate the annual level of capital allowances implied by the capital expenditures eligible for these allowances. The gross tax cost to the Exchequer is then estimated by applying the appropriate tax rates to these capital allowances.

As indicated in Section 2, capital allowances available under the scheme involve a write-off period of 7 years. Allowances at a rate of 15 percent per year are available for the first 6 years with the balance of 10 percent being written off in year 7. The Finance Act 2006 extended the original termination date for the scheme from March 2007 to 31st July 2008. However, the 2006 Act also stipulated that only 75% of eligible capital expenditure attributable to the year 2007 and 50% of expenditure attributable to the period 1st January-31st July 2008 may qualify for the relief.

In calculating the annual capital allowances, we again assume 2004 as the start year for the purposes of the evaluation. Applying the capital allowance rates to estimated eligible capital expenditure over the period 2004-2008 yields the overall values for capital allowances eligible for tax relief shown in the next table. It should be noted that these allowances extend over the period to 2014, since projects commencing in 2008 will be eligible for relief spread over the 7-year period to 2014.

Table 4.13: Estimated Value of Capital Allowances Eligible for Tax Relief under Incentive Scheme for Investment in Residential Units Associated with Private Nursing Homes - €

	2004-2005 – Total - €	2006-2014 – Total - €
Capital Allowances on Eligible Expenditure	2,200,000	38,978,667

Source: Indecon calculations

The implied value of capital allowances relating to eligible capital expenditures between 2004 and 2005 and based on expenditure undertaken to 2008 are shown in the next table. The total value of claims between 2004 and 2005 is €2.2 million, while the total value of projected claims under the scheme over the period 2006-2014 is estimated at just under €39 million.

4.5 Gross Tax Cost to Exchequer of Incentive Scheme

The gross tax cost to the Exchequer arising from the operation of the scheme for residential units is calculated by simply applying the investor/claimant profile and the applicable tax rates to the annual levels of capital allowances claimed over the lifetime of the scheme.

In relation to the investor/claimant profile, we have examined the evidence both from Indecon's survey of private nursing homes and from the Revenue Commissioners. A summary of the findings from each source is presented overleaf.

In estimating the gross tax costs to the Exchequer it is necessary to add the tax costs relating to capital allowances pertaining to expenditures undertaken in the past (i.e. 2004-2005) and over the remainder of the lifetime of the scheme (i.e. on expenditures undertaken up to 2008 or capital allowances claimed until 2014). Given that the initial investment undertaken is written off over a 7-year period, capital allowances claimed in the future are subject to a Net Present Value calculation, which discounts the actual value of the cost to reflect its current value. A discount rate of 5% has been applied in discounting the value of future capital allowances.

Table 4.14: Profile of Investors/Claimants - Capital Allowances/Tax Reliefs for Investment in Residential Units Associated with Private Nursing Homes

Investor/Claimant	Estimated % Breakdown – Indecon Survey	Estimated % Breakdown – Revenue Commissioners
Individuals in Sector	20%	-
Company-based Investors	10%	0%
Passive Investors	70%	100% PAYE-based investors*

Source: Indecon Confidential Survey of Nursing Home/Convalescent Facilities in Ireland and Revenue Commissioners
* Discussions with Revenue Commissioners indicate that all claimants are individuals claiming at PAYE tax rates

We have modelled two scenarios in relation to the modelling of estimated gross Exchequer costs of tax foregone, as follows:

- Scenario 1 or Base Case scenario: entailing the assumption that 10% of investors are claiming relief at the corporate tax rate of 12.5%, 90% of investors – encompassing individual investors in the nursing homes sector and passive investors – claiming relief at the top rate of PAYE tax (i.e. 42% until 2006 and 41% from 2007). (We accept, however, that some corporates may be able to claim relief at the higher rate); and
- Scenario 2: entailing the assumption that 100% of investors are claiming relief under the scheme at the top rate of PAYE tax.

Details of the estimated gross tax cost to the Exchequer arising from the operation of the current tax incentive scheme for investment in residential units up to the termination date in 2008 are presented in the table overleaf. Based on the above assumptions, we estimate the gross cost of tax foregone to the Exchequer arising from the operation of the scheme at between €13-14 Million in total, taking into account capital allowances claimed between 2004 and 2005 and the present value of capital allowances claimed over the period 2006-2014.

Table 4.15: Gross Tax Cost to Exchequer of Capital Allowances on Investment in Residential Unit Developments Associated with Private Nursing Homes - €

Details	Allowances Claimed To-Date (2004-2005) - €	Present Value of Allowances to be Claimed in Future (2006-2014) - €*	Total – 2004-2014 - €
Gross Exchequer Cost of Tax Foregone:			
Scenario 1: Assuming 10% of Investors are claiming at Corporate Tax Rate @ 12.5%	859,100	12,141,918	13,001,018
Scenario 2: Assuming 100% of Investors are claiming at Top PAYE Tax Rate @ 42% to 2006 and 41% thereafter	924,000	13,050,124	13,974,124

Source: Indecon calculations
* Assuming discount rate of 5%

The estimated gross tax cost of the scheme must, however, be evaluated against the economic benefits and indirect Exchequer tax contribution arising from these benefits. We discuss this component of the appraisal below.

4.6 Economic Benefits of Incentive Scheme

The increased levels of investment arising from the existence of the tax incentive scheme for residential units will give rise to increased economic activity. In order to take this into account in our model we include a 'multiplier' effect, which estimates the increase in economic activity due to the increased level of investment.

Based on research on appropriate multipliers in the Irish economy, we have applied a multiplier of 1.255 to the annual level of capital investment undertaken (which is assume to equal to annual level of eligible capital expenditure) to yield an estimate of the overall annual *gross* economic benefits arising from this activity. The table below indicates our estimated value of the gross economic benefits arising from the operation of the scheme. This is based on capital expenditures undertaken between 2004 and the current termination date for the scheme in 2008. We estimate the overall gross economic benefits over the period 2004-2008 at €64.6 million.

Table 4.16: Calculation of Gross Economic Benefits Arising from Capital Expenditures on Residential Units Associated with Private Nursing Homes - €

Economic Benefits	Total – 2004-2005 - €	Total – 2006-2008 - €	Total – 2004-2008 - €
Actual Investment Undertaken	12,666,667	38,837,333	51,504,000
Multiplier Factor – 1.255			
Estimated Gross Economic Benefits	15,896,667	48,740,853	64,637,520

Source: Indecon calculations

Net economic impacts of scheme

The estimate indicated above in relation to the gross economic benefits of the scheme must be adjusted for the opportunity cost of the investment, reflecting the fact that had this money not been invested in the nursing home residential units sector it could have been invested in other sectors of the economy. The standard assumption applied in the evaluation of similar property-based tax incentive scheme entails opportunity cost of 95%, reflecting current economic conditions. However, in the case of the nursing homes sector and associated residential units, we believe there is likely to be a wider benefit to the economy, arising from the role which these facilities play in reducing demands on the public health sector, which we estimate to be of the order of 15%-20% of the total spend. We assume 15% in our estimate and therefore reduce the assumed opportunity cost to 85% of total expenditure. The implied estimate of net economic benefit after adjusting for opportunity costs is presented in the table below and indicates a net economic benefit overt the period 2004-2008 amounting to €9.7 million.

Table 4.17: Calculation of Net Economic Benefits Arising from Capital Expenditures on Residential Units Associated with Private Nursing Homes - €

Economic Benefits	Total – 2004-2005 - €	Total – 2006-2008 - €	Total – 2004-2008 - €
Estimated Gross Economic Benefits	15,896,667	48,740,853	64,637,520
Assumed Opportunity Cost	85%	85%	85%
Estimated Net Economic Benefit	2,384,500	7,311,128	9,695,628

Source: Indecon calculations

Indirect tax contribution of economic benefits

The estimated economic benefits arising from the operation of the incentive scheme for residential units will give rise to indirect benefits to the Exchequer in relation to the tax contribution of these activities. There are two components of the indirect tax contribution, namely:

- The Gross Tax Contribution of this activity, which is calculated by applying a tax contribution rate of 36% to the gross economic benefit.
- The Net Tax Contribution, which is calculated by assuming an opportunity cost of 75%. This relates to the investment forgone in some other part of the economy as investors take advantage of the tax incentive scheme.

The table overleaf indicates the gross and net tax impacts arising from the estimated economic benefits of the incentive scheme for residential units. Adjusting for opportunity costs, we estimate the net tax contribution arising from the economic activity supported by the incentive scheme at €5.8 million in total over the period 2004-2008.

Table 4.18: Calculation of Gross and Net Tax Contribution Arising from Economic Benefits of Capital Expenditures on Residential Units Associated with Private Nursing Homes - €

Economic Benefits	Total – 2004-2008 - €
Estimated Gross Economic Benefits	64,637,520
Gross Tax Contribution @ 36% rate	23,334,145
Net Tax Contribution adjusted for opportunity cost @75%	5,833,536

Source: Indecon calculations

Calculation of Net Exchequer cost and Net Cost of Tax Foregone

In the table below we detail the calculation of the net Exchequer cost and the net cost to the Exchequer of the tax foregone arsing from the operation of the incentive scheme.

Table 4.19: Calculation of Net Exchequer Cost and Cost of Tax Foregone Arising from Operation of Incentive Scheme for Investment in Residential Units Associated with Private Nursing Homes - €

Exchequer Costs	Total – 2004-2014* - €	
	Scenario 1**	Scenario 2**
(A) Gross Exchequer Cost of Tax Foregone	13,001,018	13,974,124
(B) Net Tax Contribution arising from Economic Benefits	5,833,536	5,833,536
(C) Net Exchequer Cost (=(A) – (B))	7,167,482	8,140,588
(D) Net Tax Contribution from economic benefits adjusted for deadweight (assuming 15% of projects would have proceeded in absence of incentive)	4,958,506	4,958,506
(E) Net Tax Foregone (=(A) – (D))	8,042,513	9,015,618

Source: Indecon calculations

* Where 2004-2014 represents the period over which capital allowances and tax relief on these allowances are claimed. Note that economic benefits arising from capital expenditures occur over period to the current termination data of the scheme, i.e. July 2008.

** Scenarios relate to profile of investors and applicable tax rates, as shown in Table 4.14.

The net Exchequer cost of the scheme equates to the gross Exchequer cost of the capital allowances less net tax contribution (after adjusting for opportunity costs) arising from the economic benefits of the capital expenditures undertaken on the development of residential units. Under Scenario 1 (which, as described previously, assumes that 10% of investors are claiming tax relief on allowances at the corporate rate of income tax of 12.5%), we estimate the net Exchequer cost at just over €8 million, while under Scenario 2 (which assumes that 100% of investors claim tax relief under the scheme at the top rate of personal income tax) the net cost to the Exchequer comes to just over €9 million.

4.7 Net Overall Impact of Incentive Scheme

Taking into account the different elements described above, the calculation of the net overall impact of the incentive scheme for investment in residential units associated with private nursing homes is detailed in the table below. We estimate that a small net positive overall benefit arises through the operation of the scheme of capital allowances/tax relief for investment in residential units, amounting to between €0.7-1.65 million, dependent on the tax profile assumed in relation to investors utilising the scheme.

Table 4.20: Calculation of Net Overall Impact of Incentive Scheme for Investment in Residential Units Associated with Private Nursing Homes - €

Overall Impacts	Total – 2004-2014* - €	
	Scenario 1**	**Scenario 2****
Net Economic Benefit	9,695,628	9,695,628
Less Net tax Foregone	8,042,513	9,015,618
Net Overall Benefit of Scheme	1,653,115	680,010

Source: Indecon calculations

* Where 2004-2014 represents the period over which capital allowances and tax relief on these allowances are claimed. Note that economic benefits arising from capital expenditures occur over period to the current termination data of the scheme, i.e. July 2008.

** Scenarios relate to profile of investors and applicable tax rates, as shown in Table 4.14.

4.8 Assessment of Scope for Reducing Tax Liabilities

In evaluating the costs to the Exchequer of a tax incentive scheme such as that available in relation to residential units associated with private nursing homes, an important issue concerns the profile of investors utilising the scheme.

The next table presents the evidence from Indecon's survey of private nursing homes in relation to profile of individuals utilising the tax incentive scheme for residential units.

Table 4.21: Profile of Individuals Utilising Tax Incentives for Residential Units

Background	% of Responses
Individuals in business/Passive Investors	80
Company	20
Total	**100%**

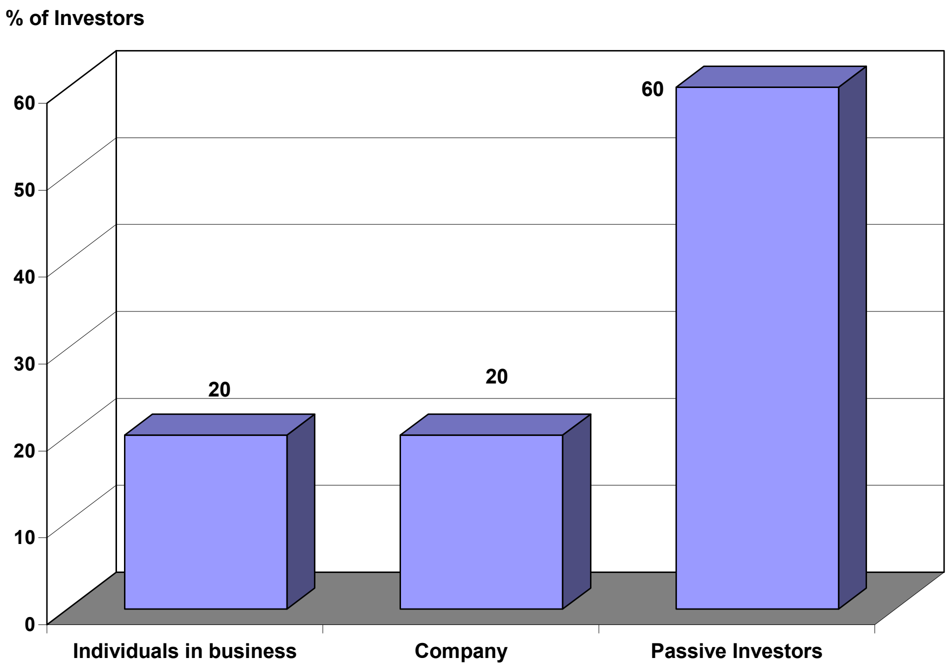
Source: Indecon Confidential Survey of Private Nursing Homes in Ireland

According to the survey evidence, some 20% of responding nursing homes stated that the incentives were claimed by individuals in the business, while 60% were passive investors. A further 20% of respondents stated that investors availing of the incentives were in corporate sector. This suggests that at least 80% are claiming allowances at the personal tax rate.

Further evidence in relation to the profile of investors availing of the tax reliefs for investment in residential units was provided to the consultancy team by the Revenue Commissioners. According to the Revenue, their belief is that all claimants under the scheme fall within the personal sector and are therefore claiming relief at the higher personal tax rates.

The profile of investors has implications for the consideration of Exchequer costs arising from the operation of the scheme in relation to the proportion of claimants that are paying tax at higher PAYE rates versus those paying tax at the lower corporate rates of 12.5% or 25%.

Figure 4.3: Profile of Claimants of the Capital Allowances in the case of Residential Units Associated with private Nursing Home/Convalescent Facilities which have Utilised Tax Incentive Scheme



Source: Indecon Confidential Survey of Private Nursing Home/Convalescent Facilities in Ireland.

In our previous analysis of nursing homes and nursing home residential units, we sought the views of accountancy/tax professionals on the likely income category of investors availing of the tax incentive. All felt that investors were likely to be earning over €100,000, with 16.7% of respondents considering it likely that investors would be earning over €200,000.

Table 4.22: Views of Accountancy/Tax Professionals - Estimates of Gross Annual Income Category accounting for the Majority of Investors Utilising the Nursing Home Tax Incentive

Gross Annual Income Category of Investors	% of Survey Respondents
Majority of investors were likely to be earning in excess of €200,000	16.7%
Majority of investors were likely to be earning between €100,000 and €200,000	83.3%
Majority of investors were likely to be earning between €50,000 and €100,000	0.0%
Majority of investors were likely to be earning less than €50,000	0.0%
Total	100.0%

Source: Indecon Confidential Survey of Accountancy/Tax Professions in Ireland.

5 Overall Conclusions and Recommendations

5.1 Conclusions

A summary of the overall costs and benefits arising from historic and projected future capital allowances and related tax relief provided under the incentive scheme for investment in residential units associated with private nursing homes is presented in the table below. We estimate the gross tax cost of this incentive scheme to the Exchequer to be between €13-14 million over the period 2004-2014 (the period over which allowances are claimed in respect of capital expenditures taking place between 2004 and 2008). Taking into account the projected net economic benefits arising from the scheme, which are estimated to amount to approximately €10 million, in addition to indirect tax benefits on foot of these benefits totalling an estimated €5 million, a small overall net benefit is observed through the operation of the scheme. The Indirect Exchequer Tax Revenues and the Net Tax Foregone estimates are adjusted for opportunity cost and deadweight.

Table 5.1: Costs and Benefits of Capital Allowances/Tax Reliefs for Investment in Nursing Home Residential Units: Indecon Estimates

Estimate	Scenario 1 - € million	Scenario 2 - € Million
Estimated Capital Expenditure on Projects that have Proceeded – 2004-2005	10.7	10.7
Capital Expenditure on likely Future Projects – 2006-2008	38.8	38.8
Gross Tax Cost of Allowances – 2004-2014	13.0	14.0
Indirect Exchequer Tax Revenues – 2004-2008	5.0	5.0
Economic Benefits – 2004-2008	9.7	9.7
Net Cost of Tax Foregone – 2004-2014	8.04	9.02
Net Overall Benefit – 2004-2014	1.7	0.7

Source: Indecon calculations

5.2 Recommendations

Based on our detailed analysis and evaluation of the costs and benefits arising from the operation of the capital allowances/tax relief scheme pertaining to residential units attached to registered private nursing homes, we present Indecon's recommendations designed to inform future policymaking in this area in the table below.

Table 5.2: Indecon Recommendations re Capital Allowances/Tax Relief Scheme for Residential Units Associated with Registered Private Nursing Homes

1.	The Residential Units Nursing Home Scheme should be extended for a period with allowances of 50% of capital expenditure if allowances are claimed at personal tax rate and 75% of capital if expenditure claimed at corporate tax rates.
2.	A formal assessment of the continued relevance of the scheme and the costs and benefits should be undertaken after a period. This should be co-ordinated with the previously recommended 3-year review of the nursing homes scheme.
3.	Eligibility for residential unit nursing homes should be conditional on investors/promoters obtaining a certification of the scheme by a relevant statutory body such as HSE/HIQA/SSI to ensure that they are fit for purpose and are associated with a nursing home registered by HSE/HIQA/SSI
4.	As part of certification by HSE/HIQA/SSI, promoters/investors should provide full profile details of capital costs which will be claimed, and whether the investors are corporate entities or individuals. An annual report to HSE/HIQA/SSI indicating occupancy levels disaggregated by those with and without disabilities should be provided. The profile detail forms should be forwarded by HSE/HIQA/SSI to the Department of Health and Children, and copied to the Department of Finance.
5.	The existing restriction on prohibiting owner/occupancies should continue to apply.
6.	The current condition re medical certification should be strictly enforced. In other words, eligibility for tax allowances should be strictly dependent on all occupancies of the residential units having a medical certificate indicating they require such accommodation.
7.	Immediate family relatives and immediate in-laws of purchasers should not be entitled to occupancy of units.
8.	The existing restriction on the availability of 20% of units for those eligible for a rent subsidy at 90% of costs of other units should continue to apply. This restriction should not apply where capital allowances are claimed at corporate tax rates, where corporate entities own the totality of units.
9.	The strict enforcement of the condition that the selection of occupants should remain with a registered nursing home should continue and this requirement should be made explicit in future legislation.
10.	The claw back period for allowances if the property is used for purposes other than nursing homes residential units should be extended to 20 years for both personal sector and corporate sector investors.

Source: Indecon

5.3 Assessment of Investor Perspective

An issue concerns the operation of the incentive scheme for investment in a residential unit development from the perspective of the investor and we consider this aspect below within the context of the likely impacts of our proposed recommendations and the resulting incentives facing investors.

5.3.1 Assumptions underlying assessment

In assessing the implications of our recommended adjustments to the operation of the incentive scheme for residential units, we have considered 3 scenarios. The assumptions underlying these scenarios are set out in the table below. We assume an average price for purchase of a residential unit of €350,000. It is further assumed that the property purchased has a residual value at the end of the recommended 20-year claw back period. This residual value is assumed to vary between 75% of the initial purchase price under Scenario 1, 100% of the purchase price under Scenario 2 and 200% under Scenario 3, and reflects various scenarios around likely capital appreciation/depreciation over the lifetime of the investment. In line with our recommendations, we assume that only 50% of capital expenditure qualifies for the capital allowances under the scheme.

Table 5.3: Assessment of Investor Perspective - Assumptions Underlying Investment Scenarios

Component	Assumptions		
	Scenario 1	**Scenario 2**	**Scenario 3**
Residential Unit Price	€350,000	€350,000	€350,000
Net Rental Yield	3%	3%	3%
Rental Income Growth - % per annum	4%	4%	4%
Tax Rate	41%	41%	41%
Residual Value after 15 years - % of initial capital cost	75%	100%	200%
% of capital expenditure allowable for relief - per annum over 7 years	50%	50%	50%

Source: Indecon

In addition to our assumptions regarding residual values, we also make a number of assumptions in relation to rental income and growth. In particular, we assume a net rental yield of 3% and annual growth in rental income of 4%. We also assume that tax relief applies at the 41% rate of personal income tax, on the basis that all investors are personal sector tax payers.

5.3.2 Analysis of returns

The table below sets out the analysis of returns on a hypothetical investment scenario involving the purchase by an investor of a residential unit valued at €350,000.

Table 5.4: Analysis of Return on Investment in Nursing Home Residential Unit – Scenarios 1-3

Year	Value of Investment/ Qualifying Capital Expenditure	Annual Capital Allowances - €	Value of Annual Tax Relief - € @ 41% Tax Rate	Annual Net Rental Income - €	Annual Net Rental Income including Tax Relief - €*	Present Value of Annual Net Rental Income incl. Tax Relief @ 5% Discount Rate
1	€315,000	€23,625	€9,686	€9,450	€15,262	€14,535
2		€23,625	€9,686	€9,828	€15,485	€14,045
3		€23,625	€9,686	€10,221	€15,717	€13,577
4		€23,625	€9,686	€10,630	€15,958	€13,129
5		€23,625	€9,686	€11,055	€16,209	€12,700
6		€23,625	€9,686	€11,497	€16,470	€12,290
7		€15,750	€6,458	€11,957	€13,512	€9,603
8				€12,436	€7,337	€4,966
9				€12,933	€7,630	€4,919
10				€13,450	€7,936	€4,872
11				€13,988	€8,253	€4,825
12				€14,548	€8,583	€4,779
13				€15,130	€8,927	€4,734
14				€15,735	€9,284	€4,689
15				€16,364	€9,655	€4,644
16				€17,019	€10,041	€4,600
17				€17,700	€10,443	€4,556
18				€18,408	€10,861	€4,513
19				€19,144	€11,295	€4,470
20				€19,910	€11,747	€4,427
Cumulative Value of Income						**€150,873**

Source: Indecon analysis

* We assume that 90% of the purchase price represents the construction cost of the unit

On the basis of the assumption that construction costs are equivalent to 90% of the purchase value of the property, capital allowances are available under the incentive scheme on 50% of €315,000 and at a rate of 15% over 6 years and 10% in year 7. This would imply annual capital allowances on this investment valued at €23,625 in years 1-6 and €15,750 in year 7. Under the current legislation, these capital allowances may be offset against net rental income and then against the investor's other income up to a maximum of €31,750. Taking into account the assume net rental yield on the property and assume annual growth in rental income, together with the capital allowances available and the implied tax relief, we calculate that the cumulative present value of annual rental income over a 20-year investment lifetime at €150,873. This constitutes the rental return on the initial investment made. The overall return to the investor must also factor in the capital appreciation or depreciation in the value of the property over this period. Based on our assumption that the residual value of the residential unit at the end of the 20-year period equates to 75% of the purchase cost, this would imply a depreciation of €87,500. Subtracting this depreciation from the cumulative value of rental income would imply an overall return under this scenario of €63,373, equivalent to 18.1% of the cost of the initial outlay.

A summary of this scenario is presented in the table below. It should be highlighted, however, that this scenario is based on the unlikely event where property values fall by 25%. By contrast, under Scenario 2, where it is assumed that the value of the property remains constant over the lifetime of the investment, a net overall return to the investor of €150,873 is evident, equivalent to 43.1% of the initial investment. Under Scenario 3, where the value of the unit appreciates by 100% to €700,000, the overall return would rise to 143% of the initial outlay.

Table 5.5: Summary of Scenario 1 Analysis of Return on Investment in Nursing Home Residential Unit

Details	Scenario 1	Scenario 2	Scenario 3
Initial Investment/Residential Unit Price (A)	€350,000	€350,000	€350,000
Residual Value of Unit at end of Year 15 (B)	€262,500	€350,000	€700,000
Present Value of Annual Net Rental Income incl. Tax Relief over 20 years (C)	€150,873	€150,873	€150,873
Net Overall Return on Investment	€63,373	€150,873	€500,873
Net Overall Return - % of Initial Investment	*18.1*	*43.1*	*143.1*

Source: Indecon analysis

The assessment of investment returns on a hypothetical investment in the purchase of a residential unit associated with a private nursing home, taking into account our recommended adjustments to the current operational rules governing the incentive scheme, would indicate the following conclusions:

- The incentive scheme for residential units would continue to provide an attractive, tax efficient option for investors;
- This remains the case even under an adjusted regime involving only 50% of capital expenditure as qualifying for capital allowances, and where the property cannot be put back on the market for a 20-year period.