



**An Roinn Airgeadais**  
**Department of Finance**

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## **Impact Assessment of Legacy Property Reliefs**

Department of Finance Consultation Paper

23 June 2011

Tax Consultation June 2011

Budget Taxation and Economic Division

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## **Table of Contents**

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Executive Summary .....	1
1. Introduction .....	4
2. Review of the "Legacy" Property-based Tax Relief Schemes.....	7
3. Analysis of Outturn Data .....	12
4. Economic Issues .....	24
5. Next Steps .....	31
ANNEX 1: List of Schemes .....	33
Annex 2: Summary Information on Property-Based Tax Relief Schemes .....	34

## Executive Summary

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1. The purpose of this paper is to initiate a consultation with interested parties as part of the economic impact assessment of the potential effects of amending, curtailing and/or abolishing the legacy property reliefs.
2. Finance Act 2011 provided a legislative basis for initially restricting the use of the legacy property reliefs and ultimately 'guillotining' all outstanding reliefs subject to a commencement order. The Act requires that an economic impact assessment be undertaken in advance of the commencement of the measures. The Programme for Government states that property tax reliefs will be reduced, capped or abolished and the Minister for Finance directed that a process be initiated to assess the possible impacts of such changes. This document is the first stage in that process.
3. The impact assessment will enable the Department to better understand the benefits that may accrue to the exchequer in terms of additional tax yield as well as consequences for investor groups and the wider economy arising from possible changes to the treatment of property-based legacy reliefs.
4. The Department's preliminary analysis has benefited from detailed data provided by the Revenue Commissioners on claims made for Section 23 type relief and accelerated capital allowances for the years 2004-2009. Some data on investor income levels were provided for the years 2007 and 2008. The Department has also developed a draft economic model for assessing the effects on investors of budgetary changes. The results of the Department's analysis of the data and certain scenarios from the economic model are presented later in the paper. Based on these results a number of emerging issues and consultation questions arise.
5. The proposed measures as set out in Finance Act 2011 are targeted only at non owner-occupiers, i.e. landlord investors in Section 23 properties and passive investors in industrial buildings. Residential owner-occupier relief would be unaffected. The proposed measures can be summarised as follows:
  - Section 23 tax relief will be restricted in use to rental income from the Section 23 property only and unused relief after a ten year period will be lost;
  - Accelerated capital allowances will be restricted to be offset only against income from the property that gave rise to the accelerated allowances and may not be carried forward beyond 7 or 10 years, depending on the period over which the allowances were initially given;
  - In addition where a Section 23 property is sold within the 10 year relevant period, the new owner gets no relief.
6. Non- owner-occupiers in residential buildings and passive investors in industrial buildings (collectively "passive investors") made close to 60,000 claims during 2004-2009, with close to €5 billion in claims made which equates to approximately €1.9 billion in potential tax costs. The €5 billion in claims – which can be used to shelter up to €5 billion in income from various sources – is not time bound.
7. Two thirds of the total tax cost to the State comes from the urban renewal, hotels and student accommodation schemes. When we include the town and rural renewal schemes, this group of five schemes account for over 80% of the total tax cost to the State. These five schemes also account for 69% of the total number of claims and the inclusion of the seaside resort scheme brings the share of total claims to 80%.

8. We also note that the take up of tax relief schemes is highest amongst tax units with incomes of less than €100,000 with 45% of all claims coming from this grouping. This income group mainly participates in the area based schemes. Their counterparts in the 'greater than €275,000' income grouping had a higher intensity of investment in the hotels scheme with a lower participation in some of the area based schemes.
9. Given that a small number of the 25 schemes appear to be prominent in terms of their size and their distribution throughout different income groups, there may be value in focusing the terms of reference of the impact assessment on just these schemes. It is possible that a focused study on a narrow set of schemes would capture the economic impacts of possible changes if these schemes have similar characteristics as other schemes. In addition, economic impacts in terms of systemic effects on the economy may be expected to be more prominent in the more popular schemes. We leave this issue as one for consultation.
10. The economic effects arising from the budgetary proposals will be at both the individual investor level and at a macro level. At the investor level an unforeseen tax liability will affect the investor's cash flows and consequent economic decisions. For wider economic issues to arise that affect equilibrium outcomes in markets, the effects at a micro level would have to have systemic consequences.
11. Another issue to consider is whether the budgetary measures represent only a transfer of wealth (represented by the present value of future tax benefits) from investors to Government or whether there is also a deadweight loss in terms of loss of economic activity. It should be noted that a deadweight loss does not necessarily need to arise immediately and could instead occur in the future if long term reputational risks or changes of behaviour arise.
12. The paper considers hypothetical or 'stylised' examples of investors and looks at how the changes proposed in the Budget would affect cash flows by the introduction of an unforeseen tax liability for these investors. We compare the net present value to the stylised investor if the investment was under the status quo and with the proposed changes. We also look at what the long term legacy cost to the State in terms of foregone tax may be from the Section 23 scheme.
13. The Department is keen to reduce the long term exposure to legacy property reliefs and is keen to elicit alternative policy proposals from interested parties. Parties should also consider if there is merit in treating the outstanding legacy costs of the Section 23 reliefs separately from Accelerated Capital Allowances, given the differences in the possible duration of reliefs and also the profile of investors as described in the consultation paper.
14. A full list of the consultation questions is summarised in the table below. The consultation questions emerge from the analysis presented throughout this paper. Interested parties are invited to consider and comment on the analysis in responding to the questions and may present their own evidence in formulating responses. Parties are also invited to use and comment on the Department's economic model, published alongside this paper, in responding to the consultation. Any updates relating to the consultation will be published on the Department of Finance tax policy website <http://www.taxpolicy.gov.ie>.
15. The closing date for responses is **29 July 2011**.

### Questions for Consultation

1. Based on the evidence presented in the paper do interested parties agree that there is merit in limiting the scope of the study to a small number of core or representative schemes?
2. Which schemes may be candidates for the 'focused study', and why?
3. What issues other than those described herein should be taken into account in determining which schemes to study in greater depth?
4. What do parties believe are the economic arguments for restricting or terminating the legacy property reliefs?
5. What do parties believe are the economic arguments against restricting or terminating the legacy property reliefs? Responses should focus on risks to economic activity rather than individual circumstances.
6. Should the Department consider separate treatment of Section 23 and Accelerated Capital Allowances?
7. What alternative policy proposals would interested parties suggest to minimise the costs to the State?

### Consultation Process

Period of Consultation: 23 June – 29 July 2011

Address for submissions: By email: [Taxconsult.June2011@finance.gov.ie](mailto:Taxconsult.June2011@finance.gov.ie)

By post: Tax Consultation June 2011,  
Department of Finance, Government Buildings,  
Upper Merrion Street, Dublin 2.

Organisations and individuals making submissions are asked to address the Consultation Questions set out throughout the report and summarised on pages 3, 6 and 31 of this paper

## 1. Introduction

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- 1.1 The Programme for Government "*Government for National Recovery 2011-2016*" commits to reducing, capping or abolishing property tax reliefs (and other tax shelters which benefit very high income earners). In line with this the Department of Finance is undertaking an economic impact assessment into the effects of changes to the legacy property tax reliefs. Organisations and individuals are invited to submit their views as part of the assessment process.
- 1.2 The purpose of this paper is to initiate a consultation with interested parties as part of the economic impact assessment of the potential effects of amending, curtailing and/or abolishing the legacy property reliefs. This paper presents the issues that have emerged following data analysis relating to the legacy property reliefs. Based on our analysis we set out a number of consultation questions on how we might progress in conducting the impact assessment.

### Consultation Process

Period of Consultation: 23 June – 29 July 2011

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Organisations and individuals making submissions are asked to address the Consultation Questions set out throughout the report and summarised on pages 3 and 25 of this paper

- 1.3 The legacy reliefs can be described in terms of two broad categories, reliefs relating to rented residential property (commonly referred to as "Section 23" reliefs) and reliefs which allow for accelerated capital allowances in respect of investment in industrial buildings (referred to as "accelerated capital allowances").
- 1.4 Finance Act 2011 provided, subject to a commencement order, a legislative basis for initially restricting the use of the legacy property reliefs and ultimately 'guillotining' all outstanding reliefs. The Act requires that an economic impact assessment be undertaken in advance of the commencement of the measures. The Programme for Government states that property tax reliefs will be reduced, capped or abolished and the Minister for Finance directed that a process be initiated to assess the possible impacts of such changes. This document is the first stage in that process.

### Background

- 1.5 Budget 2011 announced measures aimed at abolishing property-based legacy reliefs on a phased basis with all such reliefs terminating after 2014. It was also proposed that an impact assessment would be undertaken into the effects of the phased abolition of the property-based measures and the "guillotine" provision.

- 1.6 Sections 23 and 24 of the Finance Act 2011 made the introduction of the measures subject to a commencement order which could only be enacted following the publication of an impact assessment.
- 1.7 The proposed measures are targeted only at non-owner occupiers, i.e. landlord investors in Section 23 properties and passive investors in industrial buildings. Residential owner occupier relief would be unaffected. The measures can be summarised as follows:
- Section 23 tax relief would be restricted in use to rental income from the Section 23 property only and unused relief after a ten year period would be lost.
  - Accelerated capital allowances would be restricted to be offset only against income from the property that gave rise to the accelerated allowances and may not be carried forward beyond 7 or 10 years, depending on the period over which the allowances were initially given.
  - In addition where a Section 23 property is sold within the 10 year relevant period, the new owner would get no relief.
- 1.8 The impact assessment will enable the Department to better understand the benefits that may accrue to the exchequer in terms of additional tax yield as well as consequences for investor groups and the wider economy arising from possible changes to the treatment of legacy reliefs.
- 1.9 The Department's preliminary analysis has benefited from detailed data provided by the Revenue Commissioners on claims made for Section 23 type relief and accelerated capital allowances for the years 2004-2009. Some data on investor income levels were provided for the years 2007 and 2008. The results of the Department's analysis of the data are presented later in this paper. The Department has also created an economic model which has assisted the Department in understanding the impact on individual investors of terminating the reliefs.

### **Structure of the consultation paper**

- 1.10 The next chapter describes the history of the schemes and discusses the proposed changes set out in the Budget, Finance Act and the Programme for Government.
- 1.11 *Chapter 3 looks* at data from Revenue on claims under the property incentives from 2004 to 2009 and identifies emerging issues from an internal data analysis
- 1.12 *Chapter 4* discusses economic issues in terms of how the proposed changes may impact on the economy.
- 1.13 *Chapter 6* provides some further information on how to respond to the consultation.

### **The next steps**

- 1.14 The next step is for interested parties to respond to this consultation paper. The deadline for responses is 29 July 2011. Details on how to make a submission are set out in Chapter 6. The following chapters highlight some issues that parties may consider important when developing their response.

- 1.15 A number of consultation questions are proposed throughout the document and are summarised below. These questions have emerged from the initial internal scoping exercise and data analysis.
- 1.16 The Department used an economic model to assist it in understanding the impact on individual investors of terminating the reliefs. The model has been published on the Department's website alongside the consultation document (and is available to download at <http://www.taxpolicy.gov.ie>). It is adaptable to allow for the effects of alternative policy approaches on individual investors to be identified. The results of certain stylised scenarios are outlined in this paper. Respondents to the consultation are invited to use this model in formulating their response if they so wish.
- 1.17 Parties are encouraged to participate in the consultation as it is likely that those parties that do not engage with the Department of Finance during the formal consultation period may not have another opportunity to do so. Parties should also note that responses to the consultation may be published on the Department of Finance's website, and in any event are potentially subject to release under the Freedom of Information Act.
- 1.18 The box below summarises the consultation questions. The consultation questions emerge from the analysis presented throughout this paper. Parties are invited to consider and comment on the analysis in responding to the questions and may present their own evidence in formulating responses.

#### **Questions for Consultation**

1. Based on the evidence presented in the paper do interested parties agree that there is merit in limiting the scope of the study to a small number of core or representative schemes?
2. Which schemes may be candidates for the 'focused study', and why?
3. What issues other than those described herein should be taken into account in determining which schemes to study in greater depth?
4. What do parties believe are the economic arguments for restricting or terminating the legacy property reliefs?
5. What do parties believe are the economic arguments against restricting or terminating the legacy property reliefs? Responses should focus on risks to economic activity rather than individual circumstances.
6. Should the Department consider separate treatment of Section 23 and Accelerated Capital Allowances?
7. What alternative policy proposals would interested parties suggest to minimise the costs to the State?



## **2. Review of the Legacy Property Relief Schemes**

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### **History**

- 2.1 The legacy property incentives can be characterised as falling within two broad categories – Section 23 Relief (so called as it was first introduced by section 23 of Finance Act 1981) in respect of residential property, and accelerated capital allowances in respect of industrial buildings. We limit our discussion of the schemes herein to how they operated in respect of parties that will be affected by the proposals in Budget 2011 and Finance Act 2011 (“the Finance Act”), namely non-owner occupier investors in Section 23 properties and passive investors in industrial buildings.
- 2.2 In the case of Section 23 properties investors deduct the full amount of qualifying relief against rental income from the Section 23 property in the first year of letting. Where the amount of relief exceeds the rental income of the property the excess relief can be set off against other Irish rental income. Any unused relief is treated as a rental loss for the year and can be carried forward against any Irish rental income arising in later years until fully used up. In addition, to avoid a claw-back of reliefs the property must continue to be let for a period of 10 years from the first letting.
- 2.3 In respect of industrial buildings capital allowances can be earned over an accelerated period of time to the standard period thus increasing the net present value of the allowances to investors. For the majority of the non-area based property reliefs on industrial buildings the reliefs were for either 7 or 10 year periods. The area based reliefs were spread over a longer period. Others, including investments in childcare facilities could be recovered in their entirety in the first year.
- 2.4 Passive investors and lessors of industrial buildings may use their annual capital allowances against passive partnership trading income or rental income, as appropriate. Other than in the case of investment in hotels,<sup>1</sup> holiday camps or registered holiday cottages (where excess capital allowances cannot be set against other income), excess capital allowances may be used against other income up to a maximum of €31,750. Thereafter unused capital allowances may be carried forward into subsequent years but may only be used against the income from the business which gave rise to it.
- 2.5 In 2005 the Department of Finance commissioned Indecon Economic Consultants and Goodbody Economic Consultants to undertake detailed reviews of the various property-based reliefs.<sup>2</sup> The Goodbody study examined the area-based renewal schemes while the Indecon study examined the remainder.<sup>3</sup> The studies were both published and are available on the Department’s website.<sup>4</sup>

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<sup>1</sup> No restriction applies in the case of investment in certain 3 star (or better) hotels in some border, midland or western counties.

<sup>2</sup> Many of the reviewed schemes were at the time ‘expiring schemes’, i.e. schemes for which transitional arrangements were already in place for their termination.

<sup>3</sup> The ‘area-based renewal schemes’ examined by Goodbody Economic Consultants consisted of Urban Renewal, Rural Renewal, Town Renewal and the Living Over a Shop Scheme. Indecon looked at the remainder of schemes which related mostly to industrial buildings and accelerated capital allowance type reliefs.

<sup>4</sup> <http://www.finance.gov.ie/viewdoc.asp?DocID=3749&CatID=76&StartDate=01+January+2006>

- 2.6 With the exception of the capital allowances schemes for childcare facilities, private hospitals and private nursing homes Indecon recommended that the schemes be discontinued either with immediate effect or through limited transitional arrangements. The Goodbody study made similar recommendations in respect of each of the area based reliefs with the exception of the 'Living Over The Shop Scheme' for which it recommended continuation.

**Extract from the Indecon Review of Tax Incentive Schemes**

"In many cases, while the schemes have had a benefit our analysis suggests they have served their purpose and there is absolutely no case for further government incentives and there is absolutely no case for future government incentives. Continuing to approve new projects would contribute to oversupply and represent a clear waste of scarce public resources.

In a number of cases on-going government support for the activity is needed (for example in the case of third level buildings) but the tax incentives are an extremely high cost and a wasteful mechanism to achieve the objectives. In a limited number of cases (private hospitals, nursing homes and childcare facilities) increased private sector investment is needed to address the economic and social needs"

- 2.7 In Budget 2006, following the review of the property relief schemes, the Minister for Finance announced the termination, subject to certain transitional arrangements, of each of the schemes proposed for termination by Indecon and Goodbody.
- 2.8 A full list of the property schemes for which relief was claimed in 2009 is set out in Table 1 below.

Schemes	Start Date
<b>Both Residential (S23) and Industrial Buildings Schemes</b>	
Urban Renewal	1998
Town Renewal	2000
Rural Renewal	1998
Living over the shop	2001
Park and Ride	1999
Student Accommodation	1999
<b>Industrial Buildings Schemes Only</b>	
Seaside resorts	1995
Multi-storey car parks	1995
Living Over the shop	2001
Enterprise Areas	1994
Park and Ride	1999
Holiday Cottages	1968
Hotels	1994
Nursing Homes	1997
Housing for the Elderly/infirm	2002
Hostels	2005
Guest houses	2005
Convalescent Homes	1998
Private Hospitals	2002
Sports injury clinics	2002
Childcare Facilities	1998
Mental Health Centres	2007
Caravan Camps	2008
Special Palliative Care	Scheme not commenced
Mid-Shannon Corridor Tourism Infrastructure	2008

**Table 1: List of schemes**

*Source: Department of Finance*

## **Government decisions to close down the reliefs**

2.9 In the period since Budget 2006 virtually all of the schemes referred to in Table 1 above have been terminated subject to transitional arrangements for certain schemes where projects were already in the pipeline. The only scheme still open to new entrants is the Mid-Shannon Corridor Tourism Infrastructure Scheme, which is subject to State Aid approval from the European Commission

## **Budget 2011 and Finance Bill 2011**

2.10 Budget 2011 proposed that as of 1 January 2011 the use of relief was to be restricted to income earned from the property which gave rise to the relief. This was to apply to rented residential and accelerated capital allowance

schemes. In addition, any unused relief remaining after the expiry of 7 or 10 years (depending on the scheme) would be lost. Finally, where that period had already elapsed as of Budget day, unused relief would be immediately lost. Amongst other measures was a proposed 'guillotine' on all reliefs to be introduced by 2014. The Budget also proposed that an impact assessment would be undertaken into the effects of the phased abolition of the property based measures and the 'guillotine' measures.

- 2.11 Following the Budget announcement, affected parties presented a number of concerns to the Department of Finance including:
- The proposed restriction on the use of reliefs to the property that gave rise to the reliefs would effectively act as an immediate guillotine of reliefs;
  - Investors and businesses may be faced with insolvency due to an unforeseen tax liability on income that had heretofore been sheltered from taxation;
  - The risk of insolvency to investors and businesses that may arise due to warranties/indemnities that were granted by investment promoters to investors that protected investors against the risks of a change in the tax treatment of their investments
  - The use of reliefs has already been curtailed due to the restrictions that have been introduced on the use of reliefs by high income earners
- 2.12 In order to properly consider these and other issues the measures proposed in the Budget and the Finance Act 2011 required that an economic impact assessment be undertaken in advance of the commencement of the measures.

### **Programme for Government**

- 2.13 The Programme for Government (Government for National Recovery 2011-2016) committed to "reduce, cap or abolish property tax reliefs and other tax shelters which benefit very high income earners".
- 2.14 This impact assessment will enable the Department to better understand the benefits that may accrue to the exchequer in terms of additional tax yield as well as consequences for investor groups and the wider economy arising from possible changes to the treatment of legacy reliefs.

### **Restrictions on High Income Earners**

- 2.15 Budget 2006 introduced a measure to ensure a minimum effective tax rate of 20% on individuals with income levels above €500,000. Budget 2006 required that individuals with income levels between €250,000 and €500,000 would pay a minimum effective tax rate of up to 20%. Individuals' use of tax exemptions were restricted to the higher of €250,000 of specified reliefs or 50% of total reliefs available to the individual.
- 2.16 Budget 2010 introduced further restrictions on the use of tax reliefs by reducing the upper income threshold for the payment of a minimum effective tax rate to €400,000 with a minimum effective tax rate of 30% applied to these individuals. The lower threshold for the minimum payment of tax was reduced to €125,000. The new measures restricted the use of

available reliefs to the higher of €80,000 or 20% of total available reliefs. This ensured that investors with income over 125K with reliefs between 80K and 400K would only be able to use 80K of reliefs in a tax year.

- 2.17 Outstanding reliefs not claimed in a year as a result of the high earners restriction would therefore be rolled forward and, where possible, claimed in subsequent tax year. The effect of this measure may have increased the volume of outstanding reliefs that had not been claimed by the time of Budget 2011. We return to this issue in the discussion on the economic effects later.

### **3. Analysis of Outturn Data**

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- 3.1 This section presents an analysis of claims and income data provided by Revenue pertaining to property reliefs.
- 3.2 The Department has had access to two data sources from Revenue, the first relates to claims made by investors under the various incentive schemes. This covers both income and corporation tax claims for the period 2004 to 2009.
- 3.3 The second data series relates to income levels of investors across each of the schemes for the years 2007 and 2008. The income data relates to all income sources including PAYE income and covers property income. Income is provided on a gross income basis and therefore does not include deductions or credits that individuals may avail of in determining taxable income.
- 3.4 The proposals in Budget 2011 were targeted at passive rather than active investors. However the data provided by Revenue categorises tax claimants under both income and corporation tax as either owner occupiers or investor/lessors. This categorisation is provided for both residential (primarily Section 23) and industrial buildings (accelerated capital allowances).
- 3.5 For residential buildings owner-occupiers are not in receipt of rental income from the properties. We therefore exclude them from our analysis of residential buildings schemes. For industrial buildings we also exclude owner-occupiers from our analysis. However not all individuals that described themselves as owner-occupiers in their filings to Revenue qualify as active investors. Instances arise where passive investors in partnership with an owner-occupier may be categorised as owner-occupiers. We are working on methods to extract passive investors out of the owner-occupier grouping however for the purposes of this paper we consider only investor/lessors as passive investors. We believe that this is a cautious approach as it may underestimate the potential tax income that the exchequer may generate from the proposed measures.
- 3.6 Another point to note about the data is that, because of the way in which the claims forms sought information, the data only identifies new claims made for relief, rather than the ongoing use of tax relief. Thus if an investor were to make an investment in 2005 that would generate total tax reliefs of €100,000, the entirety of the €100,000 would be attributed to 2005. The data therefore measures the total possible amount of 'lifetime' tax relief and cost to State associated with that claim, but does not indicate how much of that amount is used in any given year.
- 3.7 Finally the data does not give information on regional distributions of investments. While it would be of use to the Department in its impact assessment to see where investments are located, the geographical indicator available to Revenue refers to the location of the person claiming the tax relief and not the address of the property. The latter information was never sought or provided in the tax returns. The analysis below does not examine the location of tax claimants.

## Claims and claimants over time

- 3.8 The following table (Table 2) sets out the total number of claims across all schemes from 2004 along with the total value of the claim and the total cost of the claim to the exchequer. The cost of the claim will not be incurred by the State in the year in which a claim is made, but rather be accrued over a number of years, depending on the life of the scheme. Thus a cost of €383m in 2005 means that the total number of new claims in 2005 would ultimately cost the State €383m over time in foregone taxes. It is not possible to estimate how long the liability to the State may extend, a point we return to later. All cost data is nominal and is not expressed in present value terms. For comparison purposes we include owner occupiers.

	2004	2005	2006	2007	2008	2009	Total
<b>Including owner occupiers</b>							
Number of claims	7082	10594	13106	15049	14793	13379	74003
Value of claims (€,m)	586	968	1204	1167	1013	858	5796
Cost of claims (€,m)	246	383	476	455	391	339	2289
<b>Excluding owner occupiers</b>							
Number of claims	5912	8679	10507	11879	11588	10590	59155
Value of claims (€,m)	530	821	998	972	849	718	4989
Cost of claims (€,m)	223	332	398	386	327	285	1951

**Table 2: Total number and value of claims, and total potential cost to the exchequer. All data nominal and not expressed in present value terms**

*Source: Department of Finance analysis of Revenue data*

- 3.9 The Table above (Table 2) shows that since 2004, when investors began filing claims specific to property reliefs, there have been approximately 74,000 claims across 25 schemes. Excluding owner occupiers this relates to almost 60,000 claims with a value in terms of total reliefs of almost €5bn, with a possible long term tax cost of €1.95bn. As described above this is the total tax cost of all schemes until all reliefs have been used by investors. This is displayed graphically below.

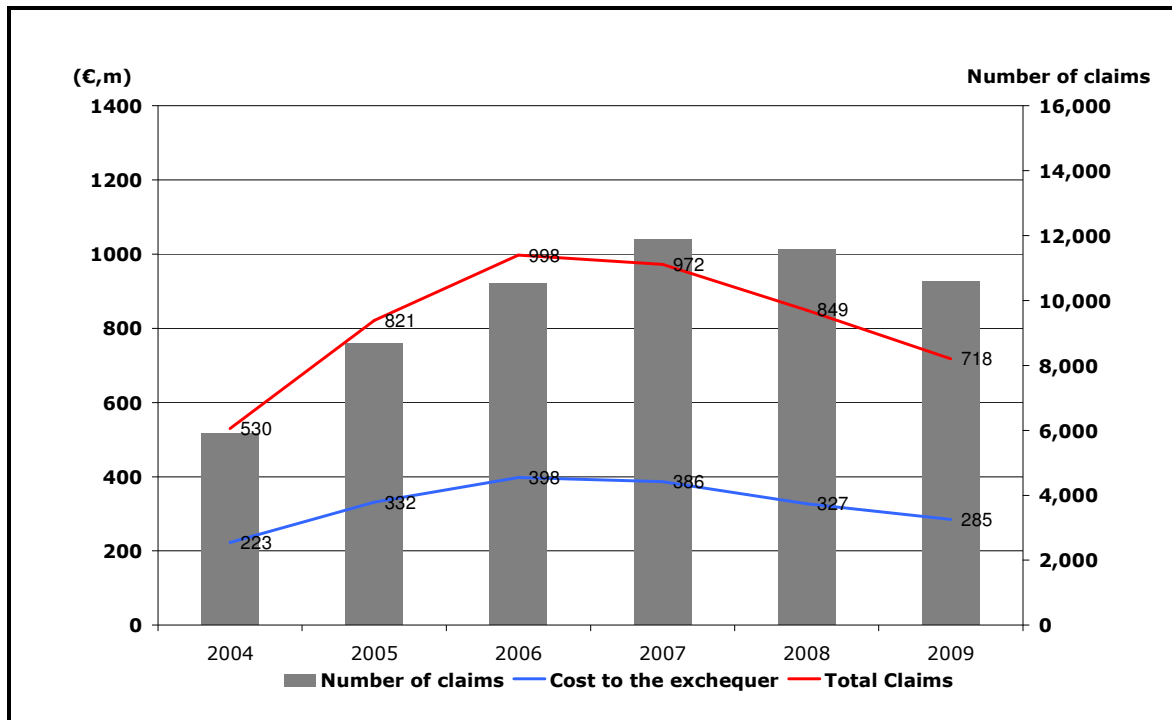


Figure 1 Total value of claims, cost of claims and number of claims (\*).

Source: Department of Finance analysis of Revenue data

\* Total value and cost of claims on the left axis and number of claims on the right axis

3.10 There is considerable variability across the schemes in terms of intensity of investment, by both number of claims and the value of claims. In terms of value the most heavily invested schemes were urban renewal, hotels and student accommodation with almost €3.2bn of claims made in respect of these schemes alone, equating to over 50% of all claims. The graph below illustrates the value of claims by schemes.



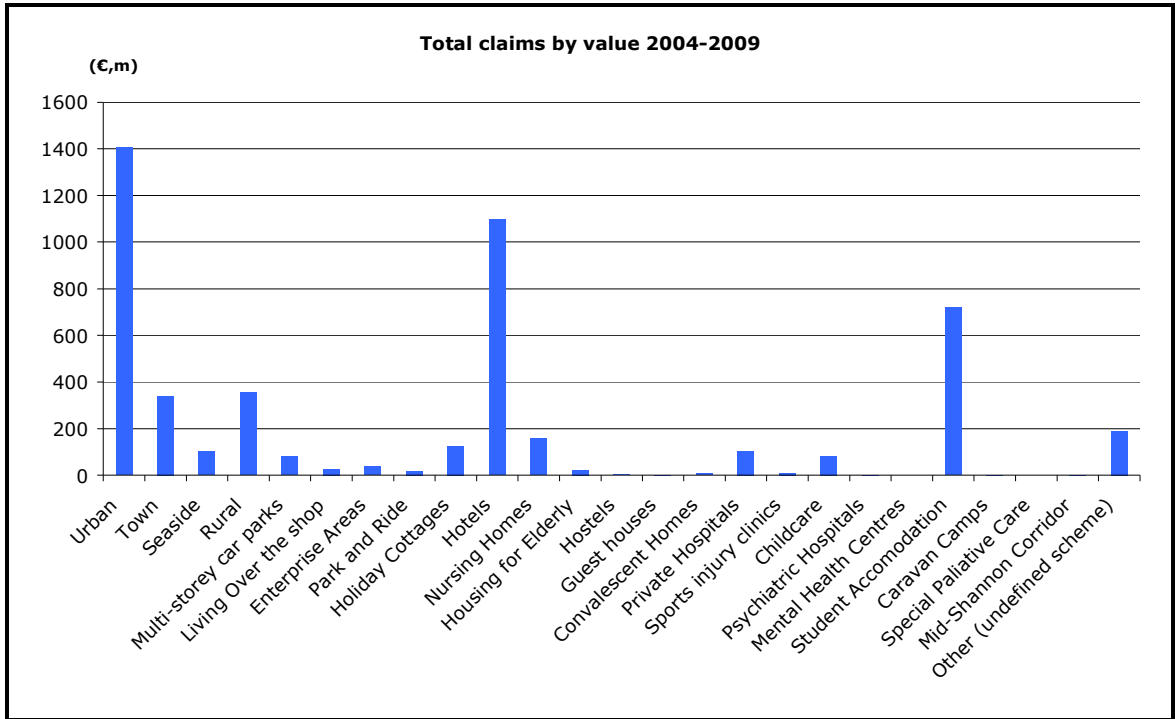


Figure 2 Total claims by value, 2004-2009

Source: Department of Finance analysis of Revenue data

3.11 In terms of share of claims, when we include rural and town regeneration and the relief for student accommodation along with the urban renewal and hotels, approximately 84% of all claims by value fall within these schemes. Figure 3 below illustrates this outturn. By looking at the total value of claims under each scheme it is possible to deduce the popularity of each scheme by number of investors and hence number of claims.

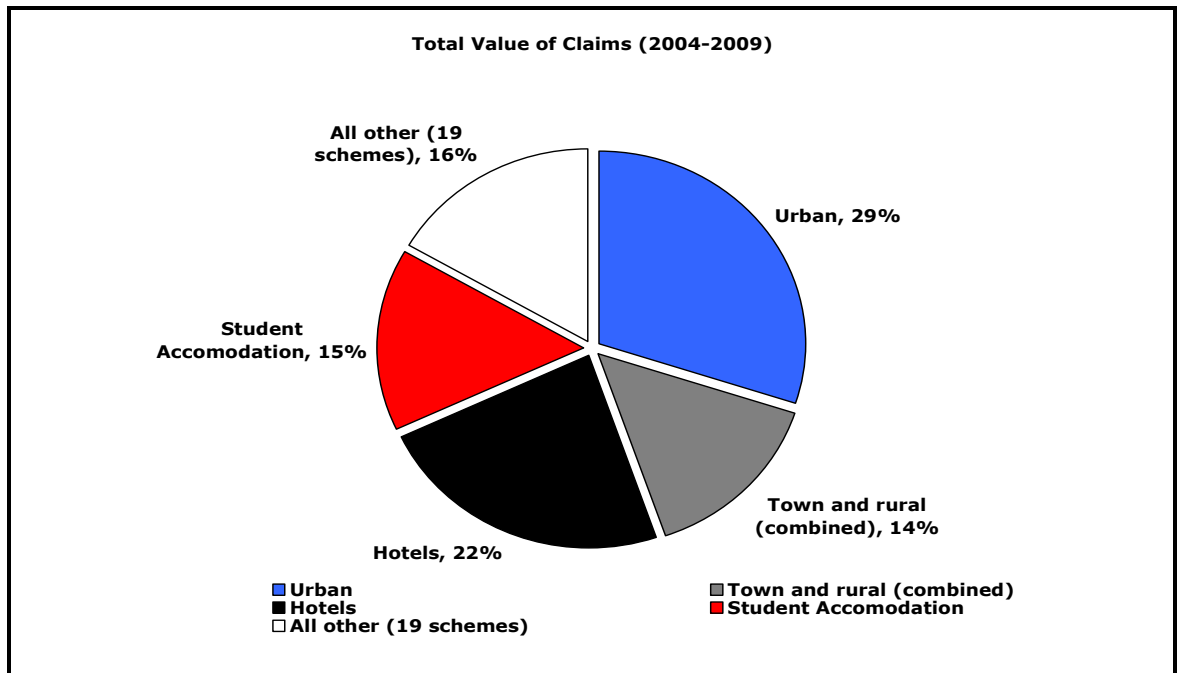


Figure 3 Relative share of total value of claims (2004-2009)

Source: Department of Finance analysis of Revenue data

3.12 Figure 4 below demonstrates the importance of the urban regeneration scheme which accounted for just over 15,700 claims or 27% of total claims received. In relation to the total value of claims, the relative importance of hotels in terms of numbers of claims has declined to less than half the number of claims made under the urban scheme. This indicates that the proportionate spend in the hotels schemes was greater than the area based schemes such as urban regeneration.

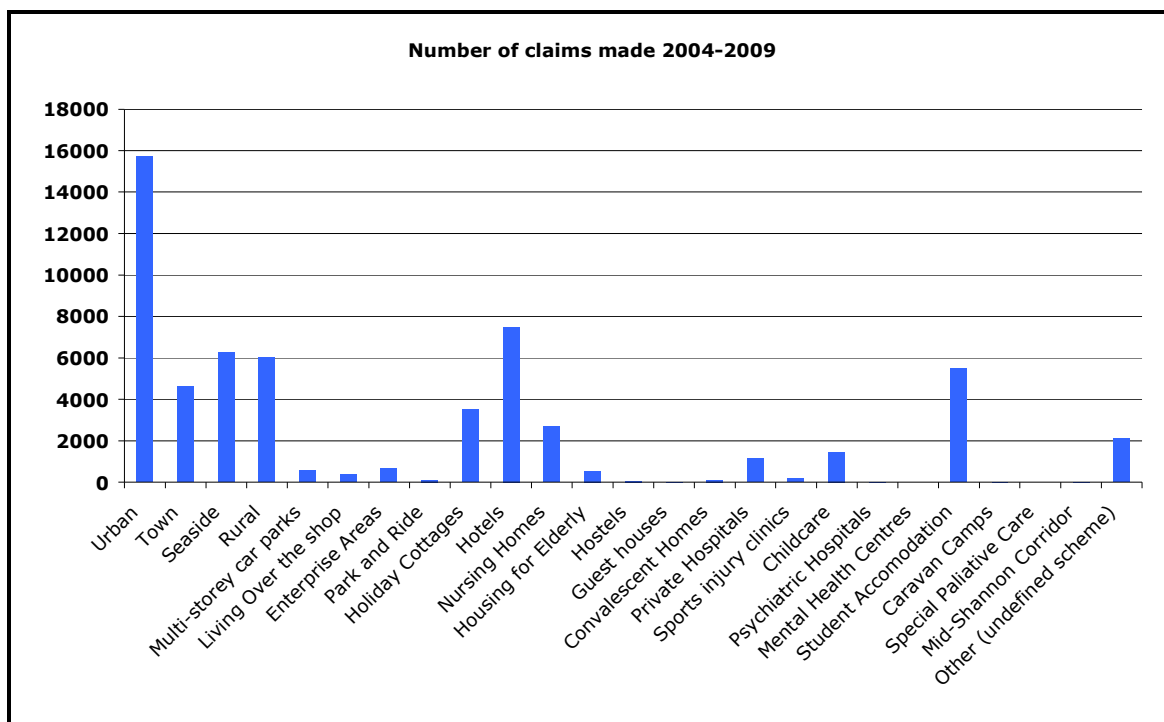


Figure 4 Total number of claims made by scheme, 2004-2009

Source: Department of Finance analysis of Revenue data

3.13 In terms of the total exposure to the exchequer in terms of foregone tax, it is not surprising that the most costly schemes are those that have the highest value of claims, namely urban renewal and hotels. The graph below illustrates relative share for each scheme in terms of number of claims and total cost to the State. What is noticeable is that there is an almost one for one relationship between share of number of claims and share of exchequer cost for the urban renewal whereas for hotels the share of exchequer cost is close to 50% higher than the share of number of claims suggesting a higher intensity of spend per investment. This pattern also occurs for student accommodation and is reversed for the rural renewal schemes with an extreme divergence arising in the seaside investments.

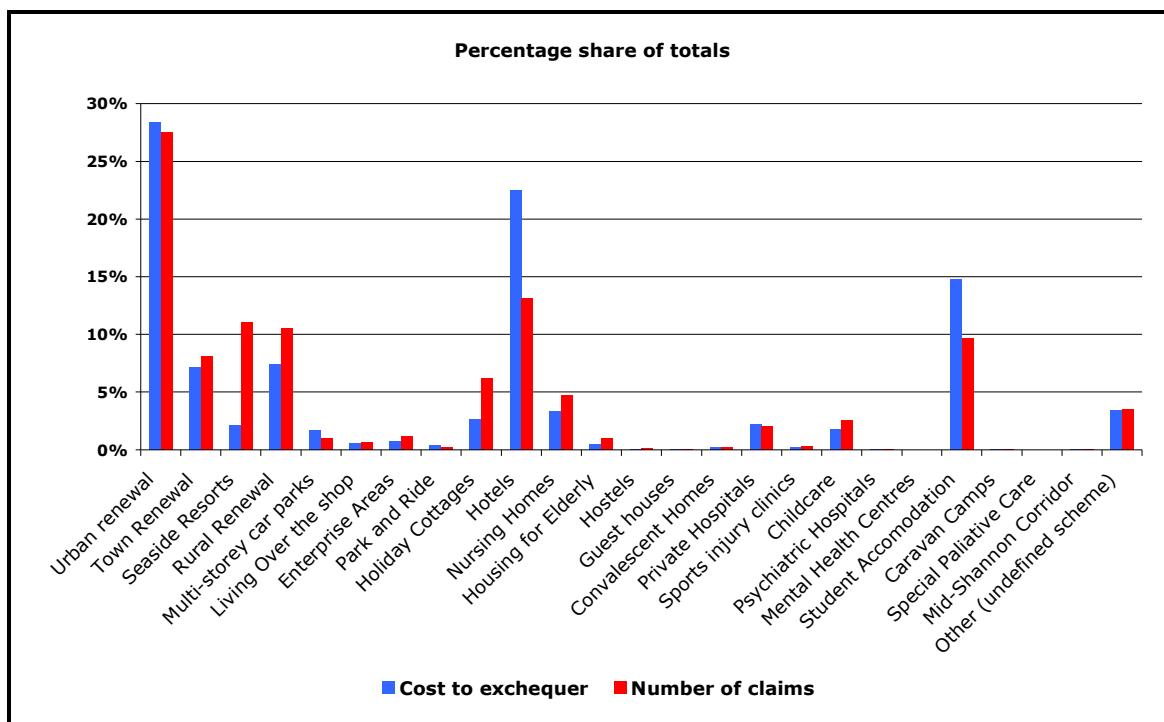


Figure 5 Percentage share of number of claims and cost to the exchequer by claim, 2004-2009

Source: Department of Finance analysis of Revenue data

- 3.14 It therefore appears that a small number of schemes accounted for most of the claims, in volume and value, with a similar profile in terms of the exchequer cost. Given that there are commonalities amongst a number of schemes in size of investments, there may be merit in the Department limiting its focus to just a core set of schemes where those schemes are seen to be representative of other schemes. By narrowing the focus it would enable the Department to devote more resources to the most important and representative schemes. Candidate schemes may include urban renewal as a representative of area based schemes and possibly hotels and student accommodation as representing accelerated capital allowance schemes.
- 3.15 A further area of interest is the profile of investors that participated in the property schemes and the types of schemes that investors of various income levels participated in. Revenue provided data for 2007 and 2008 that matches income tax filings to claims for property reliefs. It identifies the income level of a tax unit for the year that a tax unit filed an initial claim for property relief. The table below (Table 3) shows the share of claims by tax unit within five income groupings.

<b>Income level</b>	<b>2007</b>	<b>2008</b>
Less than €100,000	43%	44%
€100,000 - €150,000	17%	18%
€150,000 - €200,000	11%	11%
€200,000 - €275,000	9%	9%
Greater than €275,000	20%	18%

**Table 3: Percentage of claimants by income band**

*Source: Department of Finance analysis of Revenue data*

- 3.16 The most interesting statistics from the table above is roughly 44% of all claimants in both years came from the less than €100,000 income grouping. This equated to 4,646 of 10,880 tax units that submitted new tax relief claims that year. The next largest grouping accounting for 2,200 claims in 2007 – 20% of total claims – came from tax units in the ‘greater than €275,000’ income grouping.
- 3.17 It is useful to map the income levels into schemes to determine how each scheme is populated in terms of income cohorts. We present two graphs below that show the most popular schemes, in terms of number of claims, for the two largest income groupings. The first graph relating to claimants in the under €100,000 category. We see that approximately 72% of all claimants in 2007 claimed for an investment in one of the area based schemes (including seaside), with the most popular investment being under the rural regeneration scheme which accounted for approximately 7% of total exchequer costs of the 2004-2009 period and 10% of costs based on investments in 2007.

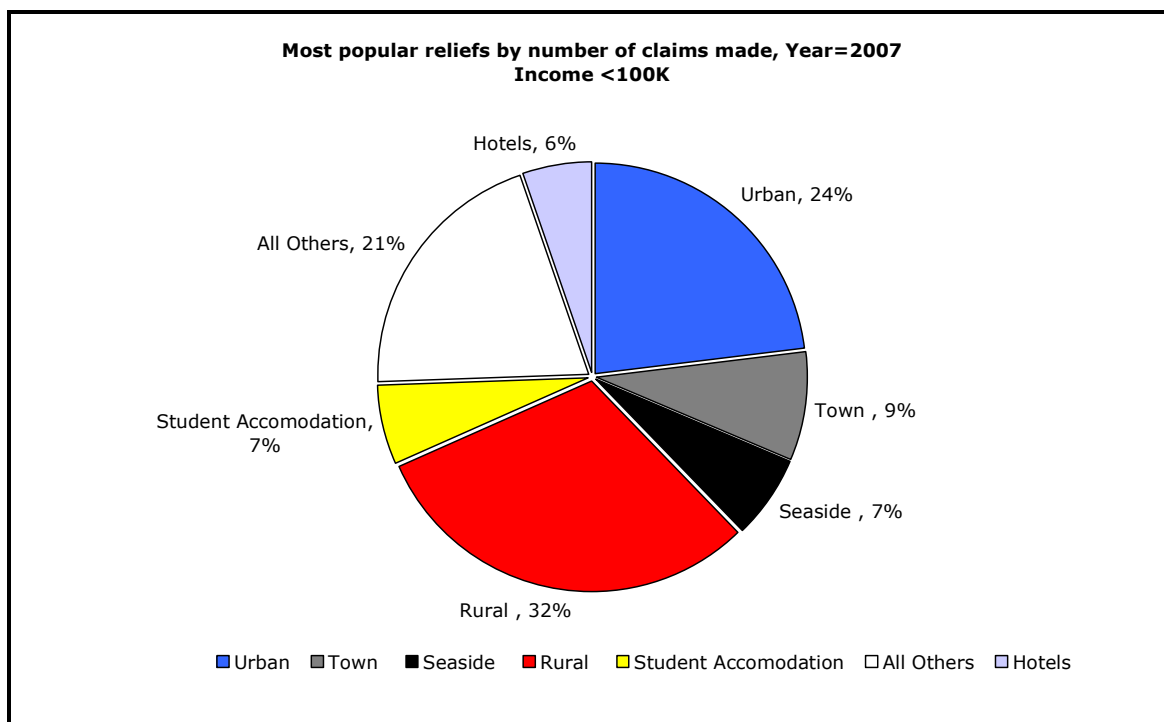


Figure 6 Share of total claims made by scheme for claimants of income less than €100,000 in 2007

Source: Department of Finance analysis of Revenue data

3.18 In the 'greater than €275,000' income grouping, we see a similar share of take-up in the urban renewal scheme, with the other area based schemes declining in share of claims. The rural renewal scheme which accounted for 32% of claims made in the 'less than €100,000' income grouping declines to a 4% share with the town renewal scheme dropping to a similar level, albeit with a much smaller proportionate decline. The hotels scheme has had the take-up amongst this group with almost one in four claims filed for this scheme.

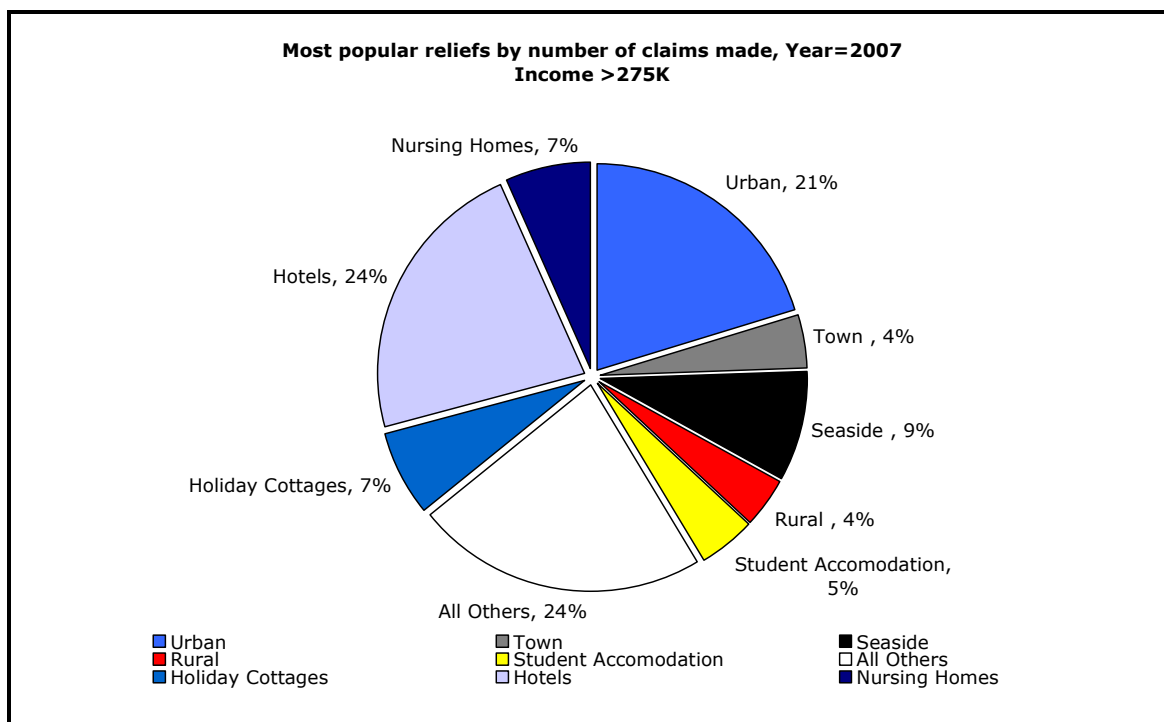


Figure 7 Share of total claims made by scheme for claimants of income less than €100,000 in 2007

Source: Department of Finance analysis of Revenue data

- 3.19 It is possible to identify certain schemes that represent popular schemes for different income groupings. We see that the area based schemes along with hotels and student accommodation feature prominently for both the lower income grouping and the higher income grouping with investments in nursing homes of importance in investments by tax units with incomes greater than €275,000. These findings may support a view that there is merit to narrowing the focus of the study to a small number of schemes.
- 3.20 Another area of interest is the size of investments made within each income grouping. The data relates to tax units rather than individuals and doesn't aggregate multiple claims where a tax unit has undertaken more than one investment. It also relates to only 2007 and so may not be representative of other tax years. The table below (Table 4) summarises these statistics for 2007.

Income level	Residential Schemes	Accelerated Capital Allowances
Less than €100,000	84,595	56,446
€100,000 - €150,000	64,623	74,287
€150,000 - €200,000	81,487	86,026
€200,000 - €275,000	73,208	91,051
Greater than €275,000	168,508	213,629
Overall Average	91,689	118,377

**Table 4: Average Claim size by income groupings, residential schemes and capital allowances (year = 2007)**

*Source: Department of Finance analysis of Revenue data*

- 3.21 Notwithstanding these qualifications, the results are somewhat surprising. Given the intensity of investments by the 'less than €100,000' income grouping we may have expected the average claim size to have been comparable to average property prices. In 2007, the peak year for property prices in the State, the average national new house price (including apartment) was €322,634, whereas the average claim under residential schemes came to €84,595. It is not clear why this discrepancy arises, although it is possible that tax incentive schemes were located in areas where the marginal price was below the national average. Another possible explanation is that multiple claimants may have made claims on the same property arising from a collective purchase which would divide the claim between investors.

### Emerging findings

- 3.22 There are some limits in the data. The data do not permit us to perfectly identify the extent of passive investors of investments in the industrial buildings schemes. The data does not identify the extent of tax reliefs used in a tax year, rather it identifies only the number and size of new claims made in a tax year and thus the total potential loss in tax revenues to the State. Nor can we predict or forecast a time period within which all outstanding reliefs will be used. In respect of income tax information, the data links the income levels of tax units rather than individual claimants. Despite this a number of interesting patterns emerge.
- 3.23 Passive investors made close to 60,000 claims during the 2004-2009, with close to €5 billion in claims made which equate to approximately €1.9 billion in potential tax costs. As stated throughout this consultation paper, the €5 billion in claims - which can be used to shelter up to €5 billion in income from various sources - is not time bound. Nor are we aware as to how much this potential stock of claims has already been used.
- 3.24 Two thirds of the total tax cost to the State comes from urban renewal, hotels and student accommodation. When we include the town and rural renewal schemes, this group of five schemes account for over 80% of the total tax cost to the State. These five schemes also account for 69% of the total number of claims and the inclusion of the seaside brings the share of total claims to 80%.
- 3.25 We also note that the take up of tax relief schemes is highest amongst tax units with incomes of less than €100,000 with 45% of all claims coming



from this grouping. This income group mainly participates in the area based schemes. Their counterparts in the 'greater than €275,000' income grouping had a higher intensity of investment in the hotels scheme with a lower participation in some of the area based schemes.

- 3.26 Given that a small number of the 25 schemes appear to be prominent in terms of their size and their distribution throughout different income groups, there may be value in focusing the terms of reference of the impact assessment on just these schemes. It is possible that a focused study on a narrow set of schemes would capture the economic impacts of possible changes if these schemes have similar characteristics as other schemes. In addition, economic impacts in terms of systemic effects on the economy may be expected to be more prominent in the more popular schemes.
- 3.27 We leave this issue as one for consultation but it appears that a narrow focused study should include at least urban renewal, hotels and student accommodation.

#### **Questions for consultation**

1. Based on the evidence presented in the paper do parties agree that there is merit in limiting the scope of the study to a small number of core or representative schemes?
2. Which schemes may be candidates for the 'focused study', and why?
3. What issues other than those described herein should be taken into account in determining which schemes to study in greater depth?

## **4. Economic Issues**

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- 4.1 The economic effects arising from the budgetary proposals will be at both the individual investor level and at a macro level. At the investor level an unforeseen tax liability will affect the investor's cash flows and consequent economic decisions. For wider economic issues to arise that affect equilibrium outcomes in markets, the effects at a micro level would have to have systemic consequences. We discuss the micro and macro effects separately below.
- 4.2 Another issue to consider is whether the budgetary measures represent only a transfer of wealth (represented by the present value of future tax benefits) from investors to Government or whether there is also a deadweight loss in terms of loss of economic activity. It should be noted that a deadweight loss does not necessarily need to arise immediately and could instead occur in the future if long term reputational risks or changes of behaviour arise.
- 4.3 We discuss possible deadweight below. The impact assessment will need to consider these against the benefits of additional tax revenue.

### **Deadweight Loss**

- 4.4 Investors may have already behaved in a manner that they otherwise would not have, on the basis of the capitalised (or present) value of expected future tax benefits. Deadweight loss may arise if the removal of these capitalised tax benefits from an investor's cash flow analysis lead to a loss of economic activity through the direct effect on an investor or how that investor's consequent economic actions or decisions impact on the economy.
- 4.5 The long term costs of a policy change may lead to a deadweight loss if there was to be a lower instance in take-up of future incentives. This could harm the economy particularly where those incentives seek to remedy market failures or to promote other societal benefits. Against this we have to consider the atypical economic circumstances and the reality that the current proposals are a reaction to a sharp economic downturn and a severe deterioration in the economy and exchequer finances. It could be argued that under the current macroeconomic and fiscal environment it is less likely that the 'long term credibility' argument would apply to the extant policy proposals. However were this policy approach to be implemented in normal economic circumstances there would be a stronger and more likely risk in terms of long-term credibility.
- 4.6 Parties are invited to identify other possible deadweight losses and to suggest ways in which they may be quantified. Parties may also wish to consider if as a result of an impact in one market or sector of the economy wider systemic effects on the macroeconomy also arise.

### **Horizontal restriction on high income earners**

- 4.7 As discussed above Budgets 2006 and 2010 restricted the use of reliefs by high income earners to ensure a minimum effective tax rate by these individuals. A consequence of this policy is to defer the use of reliefs into future tax years. Parties may wish to consider the cumulative effect of the restriction on high income earners and the proposed treatment of legacy property reliefs and whether this is an area for further study.

## Effect on investors

- 4.8 The Department has developed a model to identify the impact of possible Budget proposals on individual investors. The model is in draft form and we welcome comments for further refinements and improvements. The model has been published alongside this consultation paper on the Department's website. The model relates only to Section 23 investments, though certain commonalities exist between Section 23 and the accelerated capital allowances schemes for hotels – namely that the benefit is a shield on rental income only. It is also useful to look at Section 23 in the first instance given the open-ended duration of possible claims under this type of scheme. Parties are invited to suggest how the model could be adapted for use in other schemes.
- 4.9 The model assumes that investors are taxed on all of their income at 41% with PRSI contributions of 3% and a USC of 7%. We also assume non mortgage interest deductions on €1000 per annum per property. Consistent with recent budgetary changes mortgage interest deductions are allowed at 75%. We do not account for the high income earner restriction in our modelling.
- 4.10 We also assume that investors have mortgages on Section 23 properties only and not on non Section 23 properties although the model can provide this functionality. Consistent with the historical relationship we also assume that the tax benefits accruing from the Section 23 property amount to 90% of the purchase price. Finally we assume the Section 23 property was purchased in 2008 and the changes in policy arise from 2012 onwards.
- 4.11 We outline below a stylised case of investor cash flows from the model (Table 5). The example is of an individual with gross rent from non Section 23 property of €20,000. We introduce a Section 23 property with an associated loan of €300,000 over 15 years at an interest rate of 3.23%. The investor has annual rent of €6000 per annum.
- 4.12 The investment in a Section 23 property enables the investor to shelter their rental income from tax. In our example we see that while the after tax net income falls when a Section 23 investment is introduced this investor has now added a property to his or her portfolio while also maintaining a positive stream of cash flow. We can see that a mortgage could be structured in a way that overall cash flow remains positive provided that the difference between gross rent and bank payments is positive. The investor has capitalised the future gains from the tax shield to expand his/her property portfolio.

	2010	2011	2012	2013	2014	2015
Status quo – non Section 23 only						
Gross Rent	20000	20000	20000	20000	20000	20000
Bank payments (on S23)	-	-	-	-	-	-
Tax	(7790)	(7790)	(7790)	(7790)	(7790)	(7790)
Net Income (no S23)	18210	18210	18210	18210	18210	18210
Status quo – addition of a Section 23 property						
Gross Rent	26000	26000	26000	26000	26000	26000
Bank payments (on S23)	(25261)	(25261)	(25261)	(25261)	(25261)	(25261)
Tax	-	-	-	-	-	-
Net Income (with S23)	739	739	739	739	739	739

**Table 5: Cash flow implication on 'stylised' investor**

*Source: Department of Finance modelling*

- 4.13 The tax benefits of the current situation are described in the chart below. As we can see this investor would have expected to have continued to benefit from a tax shield until 2021. Assuming a discount rate of 4% - the Department of Finance's test discount rate - the present value of the tax benefit in 2008 to that investor would have been €86,040.<sup>5</sup> Of course if a higher discount rate is assumed it would generate a lower present value.

<sup>5</sup> Parties will see that the default setting of the model describes this exact situation.

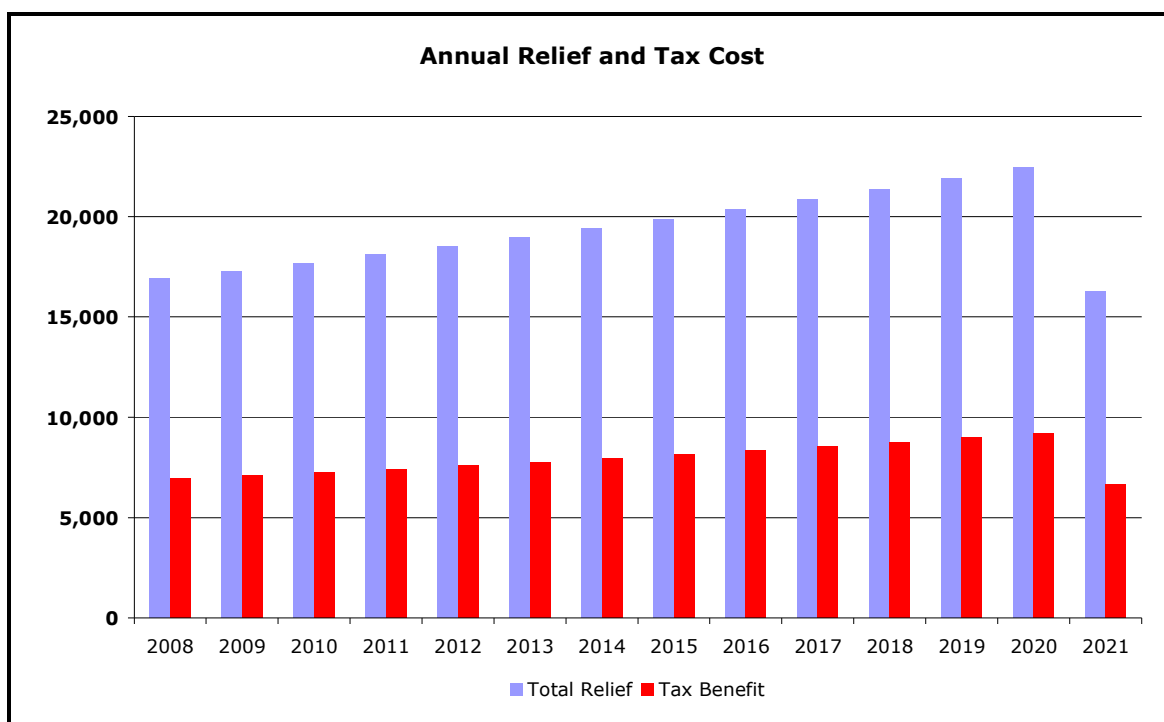


Figure 8 Graphical representation of 'stylised' investor

Source: Department of Finance modelling

4.14 The introduction of the budgetary changes on this investor is described below. We see that a tax liability on the non-Section 23 rent arises from 2012 onwards. In addition the relief that would otherwise be earned on the Section 23 property is also guillotined from 2014.

4.15 The introduction of the tax liability brings the investor from a situation with a small positive cash flow to a significant loss.

	2010	2011	2012	2013	2014	2015
Effect of proposed budget changes						
Gross Rent	26000	26000	26000	26000	26000	26000
Bank payments	(25261)	(25261)	(25261)	(25261)	(25261)	(25261)
Tax	-	-	(7601)	(7767)	(7790)	(8147)
Net Income	739	739	(6862)	(7028)	(7051)	(7408)

**Table 6: Effective of Budget 2011 on 'stylised' investor**

Source: Department of Finance modelling

4.16 In looking at the table above (Table 6) and the graph below we see that the loss of tax benefits after 2011 represent a transfer of wealth from the investor to the State. In present value terms the value to the investor making the investment in 2008 would have fallen from €86,040 to €27,189. This would represent a transfer of wealth from the investor to the State of €58,851. The cash flow losses in the table represent an additional

'externality' of the policy. The compound effect of these losses across many investors will need to be considered.

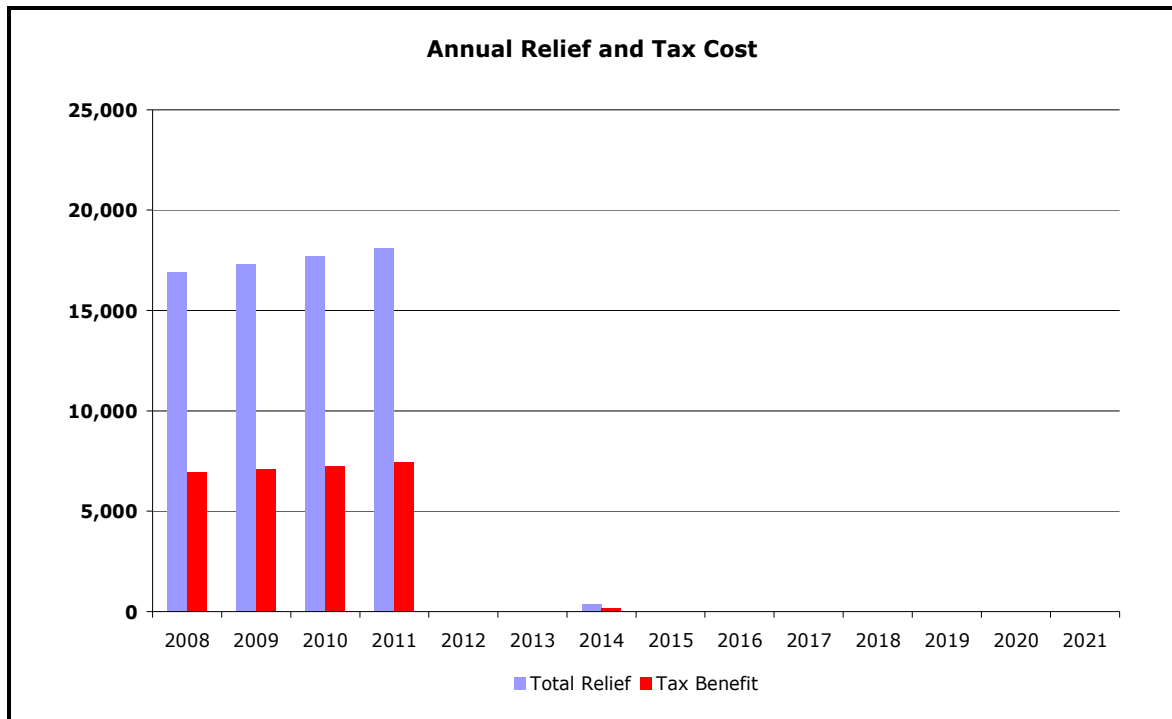


Figure 9 Graphical representation of effect of Budget 2011 changes on 'stylised' investor  
 Source: Department of Finance modelling

- 4.17 A point that needs to be considered in this discussion is the long term legacy cost to the State that may arise from the open ended nature of some of the schemes. While some of the accelerated capital allowances schemes have relatively short life spans and the legacy costs to the State may expire naturally over the medium term, there are potentially much longer term costs associated with the Section 23 Schemes.
- 4.18 The graph below looks at the possible exposure to the State from a hypothetical Section 23 investor earning €6000 p.a. in rental income on a S23 property with no other properties in their portfolio. This is the same example as above except this investor does not have a non-Section 23 property. We see that this investor will continue to benefit through a shelter from income tax until a period after 2050. This represents the outstanding 'tail' of legacy reliefs that the State remains exposed to.

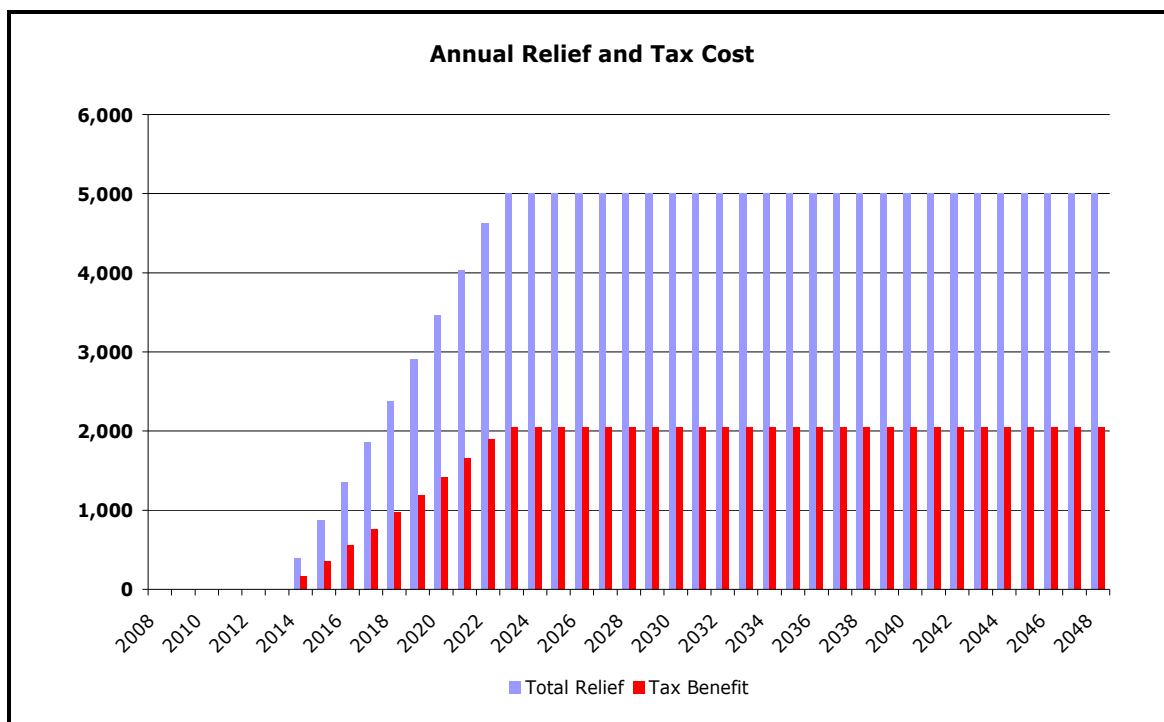


Figure 10 Graphical representation of possible long term tax cost to the exchequer under 'stylised' case

Source: Department of Finance modelling

4.19 Given the potential longer duration in terms of relief that the State may be exposed to from Section 23 reliefs, there may therefore be merit in considering separate policy responses in the treatment of Section 23 type reliefs and accelerated capital allowances. In considering alternative policy proposals parties should also note that in a present value analysis cash flows into the future are worth considerably less than cash flows today, and so applying a guillotine at a point in the future would have a lower present value impact than the expected 'nominal' benefit of the cash flow.

## Emerging Issues

- 4.20 Whilst the economic benefits to the State of restricting and ultimately guillotining the reliefs need to be further studied, the unintended consequences in terms of a loss of economic activity will also have to be considered.
- 4.21 The Department is keen to reduce the long term exposure to legacy property reliefs and is keen to elicit alternative policy proposals from parties. Parties are invited to use the model published alongside this paper, or an alternative tool, in supporting their positions.
- 4.22 Parties should also consider if there is merit in separately treating Section 23 reliefs from Accelerated Capital Allowances, given the differences in the possible duration of reliefs and also the profile of investors as described in the previous chapter.

### Questions for consultation

4. What do parties believe are the economic arguments for restricting or terminating the legacy property reliefs?
5. What do parties believe are the economic arguments against restricting or terminating the legacy property reliefs? Response should focus on risks to economic activity rather than individual circumstances.
6. Should the Department consider separate treatment of Section 23 and Accelerated Capital Allowances?
7. What alternative policy proposals would parties suggest to minimise the costs to the State?



## 5. Next Steps

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### Consultation

- 5.1 The Department of Finance would like to hear the views of interested parties in relation to the issues discussed in this consultation paper. Respondents are asked to support any views and comments expressed in submissions with relevant evidence. Evidence may include but is not limited to the use of the model published alongside this paper. Parties may be asked to supply calculations and other material to support their submissions. This may include spreadsheet models.
- 5.2 The full set of consultation questions are summarised below.

#### List of Consultation Questions

1. Based on the evidence presented in the paper do parties agree that there is merit in limiting the scope of the study to a small number of core or representative schemes
2. Which schemes may be candidates for the 'focused study', and why?
3. What issues other than those described herein should be taken into account in determining which schemes to study in greater depth?
4. What do parties believe are the economic arguments from restricting or terminating the legacy property reliefs?
5. What do parties believe are the economic arguments against restricting or terminating the legacy property reliefs? Response should focus on risks to economic activity rather than individual circumstances.
6. Should the Department consider separate treatment of Section 23 and Accelerated Capital Allowances?
7. What alternative policy proposals would parties suggest to minimise the costs to the State?

- 5.3 Responses to this consultation paper should be titled "Response to Impact Assessment of Legacy Property Reliefs Discussion Paper" and should be received no later than 29 July 2011 and should be sent to

Tax Consultation June 2011  
Budget, Taxation and Economic Division  
Department of Finance  
Government Buildings  
Merrion Street  
Dublin 2

Submissions may also be sent by email to  
[Taxconsult.June2011@finance.gov.ie](mailto:Taxconsult.June2011@finance.gov.ie)

- 5.4 Respondents should be aware that the Department is subject to the provisions of the Freedom of Information legislation.

- 5.5 The Department may include the information contained in submissions in forthcoming reports and elsewhere as required. Any party submitting information to the Department shall have sole responsibility for the contents of such information. If submissions contain confidential material, it should be clearly marked as confidential, and a version of the submission should be provided which can be used for publication.

## ANNEX 1: List of Schemes

A1.1 The table below lists the various tax-based property schemes and respective termination dates

Scheme	Closing Date
Urban Renewal	31/07/2008
Town Renewal	31/07/2008
Seaside Resort	31/12/1999
Rural Renewal	31/07/2008
Multi-storey Car Parks	31/07/2008
Living over the Shop	31/07/2008
Enterprise Areas	31/12/2000
Park and Ride	31/07/2008
Student Accommodation	31/07/2008
Hotels	31/07/2008 <sup>6</sup>
Holiday Cottages	31/07/2008
Holiday Hostels	-
Guest Houses	-
Nursing Homes	30/06/2010 or 30/06/2011 <sup>7</sup>
Housing for elderly/infirm	30/04/2010
Convalescent Homes	30/06/2010 or 30/06/2011 <sup>8</sup>
Qualifying Hospitals	30/06/2010 or 31/12/2013 <sup>9</sup>
Qualifying Mental Health Centres	30/06/2010 or 30/06/2011 <sup>10</sup>
Qualifying Sports Injury Clinics	31/07/2008
Childcare Buildings	31/03/2011 or 31/03/2012 <sup>11</sup>
Specialist Palliative Care Units	Scheme not commenced
Registered caravan & camping sites	-
Mid-Shannon Corridor Tourism Infrastructure	31/05/2015 (subject to EU State Aid approval)

**Table 7: List of property incentive schemes and closing dates**

Source: Department of Finance

<sup>6</sup> This is the termination date for incurring construction/refurbishment expenditure in order to avail of the accelerated rate of capital allowances of 15% per annum for the first 6 years and 10% in year 7. Capital allowances are still available for hotel projects at a rate of 4% per annum.

<sup>7</sup> The termination date for these schemes is 31 December 2009 except for pipeline projects. The latter dates in the table relate to these pipeline projects. The earlier termination date relates to projects where no planning permission is required and certain proportion of expenditure has been incurred by 31 December 2009. The later termination date relates to projects where planning permission is required.

<sup>8</sup> Same as footnote 10.

<sup>9</sup> Same as footnote 10.

<sup>10</sup> Same as footnote 10.

<sup>11</sup> The termination date for this scheme is 30 September 2010 except for pipeline projects. The latter dates in the table relate to these pipeline projects. The earlier termination date relates to projects where no planning permission is required and certain proportion of expenditure has been incurred by 30 September 2010. The later termination date relates to projects where planning permission is required

## **Annex 2: Summary Information on Property-Based Tax Relief Schemes**

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A2.1 The various property related relief schemes can be divided into three broad categories:

- Seven year schemes,
- Ten year schemes and
- Schemes greater than 10 years.

### **Seven year Schemes**

A2.2 The tax code provides for tax-based property incentives on a sectoral basis in the form of capital allowances for capital expenditure incurred on the construction or refurbishment of certain types of buildings which are designated as industrial buildings under tax law.

- Among the buildings which qualify are certain health care related facilities e.g. nursing homes, nursing home residential units, private hospitals, convalescent homes and mental health centres.
- The schemes of accelerated allowances for the above developments were generally terminated with effect from 31 December 2009 - the date by which qualifying construction/refurbishment expenditure had to be incurred except for pipeline projects for which transitional arrangements were put in place. If certain conditions are met, the termination date is extended for these pipeline projects. See table at Appendix 1 which sets out the termination dates for the various schemes.
- Hotels and registered holiday cottages, sports injury clinics, childcare facilities and buildings in use for third level educational purposes could also qualify and these schemes have also been terminated.
- In general the qualifying expenditure is written off at a rate of 15% per annum for the first 6 years with 10% in year 7 (with the exception of registered holiday cottages where the rate was 10% p.a.).
- Claims in respect of capital allowances may only commence to be made after the development to which the qualifying expenditure relates comes into operation.
- The schemes have various conditions regarding clawback of the allowances where the building ceases to be used for the purpose for which the allowances were given within a specified period.
- An annual limit of €31,750 may also apply in certain schemes in relation to any excess capital allowances over rental or trading income which an individual passive investor can set off against other non-rental or non-trading income.
- In the case of childcare facilities there was an option to avail of a 100% initial allowance or free depreciation of up to 100% (for owner-occupiers).
- A scheme of capital allowances for palliative care units was not commenced.
- While the Mid-Shannon Corridor Tourism Investment Scheme is similar in certain respects to previous "area" based incentive schemes capital

allowances were only made available for certain approved tourism infrastructure projects. This scheme has a final termination date for incurring construction expenditure of 31/5/2015.

### **Ten Year Schemes**

A2.3 Section 23 relief is a commonly used term for rented residential relief. And was first introduced by Section 23 Finance Act 1981. The relevant legislation is contained in Chapter 11 of Part 10 of the Taxes Consolidated Act, 1997.

- Section 23 is a tax relief that applies to rented residential property in a tax designated area.
- It is available on expenditure incurred on the construction, refurbishment or conversion of a qualifying property and who lets that property having complied with certain conditions
- Following construction it is the first use of the property that determines the type of relief that will apply e.g. owner occupier or lessor relief.

### **Schemes Under Section 23**

A2.4 The following is the list of Schemes under Section 23 currently with legacy relief:

- Integrated Area Urban Renewal Scheme
- Living over the Shop
- Park and Ride
- Rural Renewal Scheme
- Town Renewal Scheme
- Student Accommodation Scheme

### **Rented Residential Relief**

A2.5 In the case of Rented Residential relief the following applies:

- The full amount of the relief is deducted from the rental income of the particular property in the first year of letting, together with other allowable deductions such as management expenses and interest relief etc.
- If, as is most likely, the deductions exceed the rental income from the property, the excess can be deducted from other Irish rental income for that year.
- Any remaining excess deductions are treated as a rental loss for that first year and can be carried forward against any Irish rental income arising in later years until the loss is used up.
- If an individual does not have sufficient rental income to absorb a rental loss, the carry forward of the rental loss can continue beyond the 10-year period following the first letting of the property under a qualifying lease.
- If a section 23 property is sold within 10 years from first being let under a qualifying lease then the section 23 relief is clawed back.

- If a second-hand property is purchased within the 10 year period, and is still a qualifying property at the time of purchase, section 23 relief will be available to the new purchaser provided he or she fulfils all of the relevant conditions.
- If a section 23 property is sold more than 10 years after the date on which the property was first let under a qualifying lease, there is no withdrawal of the relief granted and the new purchaser is **not** entitled to relief, even if relief was not claimed by the original owner.

### **Residential Owner-Occupier Relief**

A2.6 In the case of a newly constructed property, 50% of the qualifying expenditure is allowed. Relief is granted at the rate of 5% per annum over a period of 10 years as a deduction from total income.

- In the case of a refurbished or converted property, 100% of the qualifying refurbishment or conversion expenditure is allowed.
- Relief is granted at the rate of 10% per annum over a period of 10 years as a deduction from total income.
- The first claim can be made for the year in which the individual first uses the property as his or her sole or main residence.
- Where an individual's income for a year of assessment is not sufficient to absorb the relief for that year, the excess relief cannot be carried forward and is lost.
- Owner-occupier relief is terminated if there is a disposal of the property or if it otherwise ceases to be a qualifying property by, for example, ceasing to be used as the sole or main residence of the individual claiming the relief, within the period of 10 years beginning when the property was first occupied by the owner.
- Unlike section 23 relief, there is no withdrawal of the relief already granted to the first owner.
- Owner-occupier relief is only available to the first owner and occupier of the property after it has been constructed, converted or refurbished.
- Unlike section 23 relief, there is no provision for any relief to be passed on to any subsequent owner of the property.

### **Property Developers**

A2.7 A property developer is not precluded from section 23 relief or indeed owner-occupier relief provided, obviously, that it is not a company as owner-occupier relief can only be claimed by the person who is using the property as their sole or main residence.

A2.8 This group of commercial schemes is generally where the writing down period is 14 years.

- An initial allowance of 50% can be claimed in the first year
- An annual allowance of 4% for the next 12 years
- Commercial Schemes include : Seaside Resort Scheme, Enterprise Areas, Multi Storey Car Parks, Town renewal, Rural Scheme, Living Over the Shop, Park and Ride Scheme

## **Clawback of capital allowances**

A2.9 Where certain events (known as balancing events) occur within **13 years** of a qualifying building being first used this can potentially lead to a clawback of part or all of the allowances claimed.

- Among the events, which could lead to a clawback of the allowances granted, is the sale of the building.
- The clawback of the allowances is known as a balancing charge and occurs when the tax written down value of the building (qualifying expenditure less allowances claimed to date) is less than the sales proceeds.
- Alternatively where the tax written down value of the building is greater than the sales proceeds this will give rise to a balancing allowance (basically an additional allowance).
- No balancing charge will be imposed if the sale (or other balancing event) occurs more than 13 years after the building is first used however a balancing allowance may still arise.
- Other events which could potentially give rise to a balancing charge, where they occur within 13 years of the building being first used, are the building being demolished or destroyed or ceasing altogether to be used.
- This is not a full list of possible balancing events.