An Roinn Airgeadais
Department of Finance

Public Consultation Paper

Tax and Fiscal Treatment of Landlords

Tax Policy Division
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1. Introduction

On foot of a commitment contained in the *Rebuilding Ireland – Strategy for the Rental Sector* published by the Department of Housing, Planning, Community and Local Government (DHPCLG) in December 2016, a Working Group has been established to examine and report on the tax treatment of landlords (or rental accommodation providers), and to put forward options, where appropriate, for amendments to such treatment. The Working Group is chaired by the Department of Finance and its membership includes officials from DHPCLG, Revenue and the Residential Tenancies Board.

During the process of developing the *Rebuilding Ireland* strategy a public consultation was undertaken by DHPCLG on a broad range of issues relating to the housing market. A number of taxation issues were raised in the responses received to this consultation and the Working Group has decided to conduct a focused consultation seeking further detailed input from interested parties on these matters.

2. Consultation Process

This public consultation process will run from Friday 10 March to Friday 7 April 2017, a period of four weeks. Any submissions received after this date may not be considered.

How to Respond

The preferred means of response is by email to: taxpolicy@finance.gov.ie. Please ensure that Tax and Fiscal Treatment of Landlords Consultation is stated in the subject line.

Alternatively, you may respond by post to:

Tax and Fiscal Treatment of Landlords Consultation
Tax Policy Division
Department of Finance
Government Buildings
Upper Merrion Street
Dublin 2 D02 R583

When responding, please indicate if you are a landlord (individual or corporate), tenant, adviser, representative body or member of the public.

Freedom of Information

Responses to this consultation are subject to the provisions of the Freedom of Information Acts. The Department may receive requests for any or all information supplied as part of this process. Parties should also note that responses to the consultation will be published, in full, on the website of the Department of Finance.

Meetings with key stakeholders

The Working Group may also invite key stakeholders to meet with them, including representative bodies and other interested groups or individuals who make submissions to this consultation.

3. Background/Context

Objectives

Landlords are an essential feature of a fully functioning residential property market. The current shortage of supply of residential rental properties is driving upward pressure on rental prices and making it difficult for prospective tenants to find affordable homes.

At the same time, increases in house prices might be facilitating some individuals who may not wish to be landlords to exit the market and may be prompting some multi-property landlords to reduce their property holdings, thereby further constricting the supply of residential rental property.

The rental housing market is also intrinsically linked with the owner-occupier housing market. In the short term, increases in supply to the rental market may be achieved at the cost of a reduction in supply to the owner-occupier market, and vice versa. Policy actions targeted at the rental market must therefore take cognisance of the potential consequential impacts in other areas of the housing market, in addition to the Government's policies of tenure neutrality and of increasing overall housing supply and new residential construction activity.

The majority of landlords in Ireland are individuals, owning one or two rental properties. Statistics from the Residential Tenancies Board (RTB) show that over 68% of landlords have a single tenancy, and over 91% of landlords have three or fewer tenancies. Large professional landlords – such as Real Estate Investment Trusts (REITs), corporate vehicles and investment funds – accounted for just over 2% of residential tenancies as of June 2016.

The objectives of this consultation are two-fold. Firstly, it will inform the review being undertaken by the Working Group on the tax treatment of landlords to determine if it is fit for purpose in the current housing market and in the longer term.

Secondly, the submissions received will be reviewed as part of a process to determine if a policy rationale exists to introduce new reliefs or otherwise alter the tax system to incentivise landlords to remain in, or to enter, the residential accommodation market. This assessment will have regard to the wider regulatory framework for accommodation providers to ensure that any taxation proposals would not act merely as an alternative source of income for other control measures implemented by the Government.

Related issues raised in the DHPCLG *Rebuilding Ireland* public consultation

As noted above, a number of taxation issues were raised in the responses received by DHPCLG to their public consultation *on the Strategy for the Rental Sector*, which was conducted in late 2016. These included proposals/requests in the following four broad categories:

A: Taxation of Rental Income

- Tax relief / exemption for income from long-term leases
- Tax relief similar to pension contributions for rental income
- Reduced tax rate (e.g. 25% corporation tax rate) to apply to rental income
- Tax relief targeted at 'accidental landlords'

B: Expense Deductions

- Improved deductibility of expenses, including:
  - Restoration of 100% mortgage interest relief
  - Deduction for cost of personal time spent managing / maintaining property
  - Up-front deduction for full cost of furnishings and fittings
  - Increased tax relief for refurbishment works
  - Deduction for Local Property Tax, potentially tied to longer term leases

C: Rent-a-Room Scheme

- Abolition of Rent-a-Room scheme
- Increase or abolish the cap on the scheme
- Extend the scheme to apply to full property rentals

D: Administration / Other

- Certainty as to the tax treatment of income / expenses over the longer term
- Transfer of Local Property Tax liability to tenants
- VAT relief on construction of rental accommodation
- Tax-incentivised build-to-rent programme
- Introduction of penalty taxes for unoccupied property and/or idle development land

Department of Finance Guidelines for Tax Expenditure Evaluation

In October 2014 the Department of Finance published guidelines for the evaluation of tax expenditures, which provides a framework for the *ex-ante* and *ex-post* analysis of tax expenditures. In principle, tax expenditures should address a market failure where the market mechanism leads to a sub-optimal outcome in terms of economic efficiency.

The five questions to be considered as part of *ex ante* evaluation are:

1. What objective does the tax expenditure aim to achieve?
2. What market failure is being addressed?
3. Is a tax expenditure the best approach to address the market failure?
4. What economic impact is the tax expenditure likely to have?
5. How much is it expected to cost?

The four questions to be considered as part of *ex post* evaluation, such as an evaluation of existing tax expenditures are:

1. Is the tax expenditure still relevant?
2. How much did the tax expenditure cost?
3. What was the impact of the tax expenditure?
4. Was it efficient?

The Department of Finance Guidelines for Tax Expenditure Evaluation can be found on the Department's website at http://www.budget.gov.ie/Budgets/2015/Documents/Tax_Expenditures_Oct14.pdf.

EU Considerations

EU State aid considerations must be borne in mind in considering any options for change to the current regime for the taxation of residential property landlords or for the introduction of new incentives particularly where the proposals are targeted at certain types of landlords or at certain sub-sectors of the rental market only.

Compatibility with the freedoms guaranteed under the EU Treaties must also be considered. This could require the extension of eligibility for any new measures to landlords subject to tax in Ireland in respect of rental property located in other EU / EEA States.

4. Consultation Questions

Interested parties are invited to make submissions regarding the following questions. It is not necessary for each submission to address every question, and other issues relevant to the tax and fiscal treatment of landlords may also be raised.

In all cases, submissions should have regard to the potential Exchequer cost of any measure proposed and, where such a cost would arise, the potential avenues for financing the cost though counterbalancing taxation and/or cost-saving measures elsewhere.

Respondents are also requested to bear in mind two related considerations; (i) the capacity of a proposed change to protect the existing supply of rental units; and (ii) the capacity of a proposed change to encourage new supply of rental units. As noted elsewhere in this document, measures proposed should be cognisant of the relationship between the home purchase and residential rental markets.

1. What is the single most significant issue which is causing existing landlords to consider exiting the rental market, or deterring potential investors from entering the residential property market? Is there any tax or fiscal measure that could address this issue, having regard to existing Budget constraints?

2. Property is, in many cases, a highly leveraged investment involving significant mortgage borrowings in addition to the capital invested by the landlord. Mortgage interest paid is allowable as a deduction in calculating taxable income from rental property. Similar treatment is not afforded to interest on borrowings used for other forms of income-generating investment – for example interest on monies borrowed to invest in shares is not allowable as a deduction against dividend income. Is it appropriate for the State to incentivise concentrated investment risk through the granting of interest relief for rental property investment?

3. It has been noted that landlords may have a taxable rental profit in instances where their net rental income after making mortgage repayments and meeting other outgoings associated with the property is negative. Amortisation mortgage repayments are comprised of both an interest charge and a capital repayment element. Would it be appropriate for the State to subsidise the acquisition of a capital asset by a private individual by allowing relief in respect of the capital repayment element, and if so should some additional element of future income and/or gains from the property accrue to the State as a consequence?

4. Some submissions to the D/Housing public consultation referred to investment in residential rental property as an alternative form of pension investment, and proposed that tax reliefs should be provided accordingly. However there are significant conditions attached to pension reliefs and pension funds cannot normally be accessed before the individual's retirement date. Furthermore, pension income replaces an individual's earned income in retirement. In contrast individuals with investment income, such as property rental income, do not lose that income source when they reach "retirement age". The income will continue as before and they have the investment asset, in this case the rental property, which may be converted to a capital sum with which they can purchase an annuity if they so wish. Taking these factors into account, should a tax relief in any way comparable to tax reliefs for pension investments be considered for investments in, or income from, residential rental property?

5. Other submissions to the D/Housing public consultation proposed that property rental should be regarded for tax purposes as being more in the nature of an active business activity, rather than as passive investment income, and that improved expense deductibility should be allowed on this basis.
    a. Would improved deductibility for rental expenses make a material difference to landlords when deciding to enter or remain in the rental market, and if so what expenses? **Note:** In this context it should be noted that the proposals relate to the treatment of the provision of rental accommodation as an active business, and therefore responses should have regard to the tax treatment of an equivalent expense in a trading context if proposing a new deduction
    b. Would improved expense deductibility be passed on to tenants in the form of reduced rents, or are rental values driven by external market forces more so than by individual landlord profitability?

6. Would a relief from capital gains tax on disposal of a long-term rental property in the future encourage landlords to remain in, or to enter, the residential letting market at present? Alternatively is it possible that it would lead to a greater exodus of landlords from the rental market?

7. Would a relief from capital gains tax on disposal of a rental property, conditional on the property being sold with a tenant in situ and/or a requirement for the property to continue in use as a rental property, be operable in practice? What protections could be used to ensure the continued tenancy rights of the sitting tenant, and in what manner could a clawback of relief be achieved if the new owner ceases to let out the property.

8. It is possible that 'accidental' landlords may choose to exit the rental market as property prices rise, reducing or eliminating negative equity on the rental property. Is there a specific tax measure or treatment which could incentivise such individuals to remain in the rental market as landlords?

9. With regard to owners of vacant residential property, what are the primary reasons why such individuals do not choose to rent out the property, and are there tax measures which would encourage vacant residential property owners to enter the rental market?

10. Is the threshold for the Rent-a-Room scheme set at the right level? Do increases in the threshold lead to increases in rent charged by those using the scheme? In view of the scheme's objective of increasing supply of rented residential accommodation, should the threshold vary depending on the number of individuals who are renting in the home or the number of rooms let? Should additional reporting requirements apply to those who use the scheme?