

## Soothing the Tax Headache of Commercial Property Investment

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*By Aubrey Calderwood, Director of Capitus*

Economically, Ireland is facing the challenge of a lifetime, with the property sector taking direct hits from all sides. Movement in the property sector has all but ground to a halt, with many investors facing negative equity and would-be investors (if there are still any out there) unable to get finance deals from the banks.

Could the outlook really be any bleaker for property investors in a country that was once one of the 'jewels in the crown' of the global property market?

Unfortunately it would seem possibly so. The raft of punitive tax changes announced last year as part of Ireland's economic recovery plan, have been well publicised and much talked about. However, less has been written about the way these changes specifically affect commercial property investors and the impact on rental income. What has been publicly acknowledged is that anyone receiving rental income from a commercial property could be facing hefty tax bills, where prior to the changes many such investors were receiving this income tax-free.

So what are the property tax changes and how will they affect you if you have invested in commercial property in order to provide a tax-efficient income? And perhaps more importantly, what steps can you take to reduce your tax liability?

### **Ill Winds of Change**

Prior to the tax changes announced last year, commercial property offered a very tax efficient means of taking an income (in the form of rent) from your investment. This was because property investors could shelter any rental income completely against the 'losses' they made when buying the property. So, if they bought the property for €500k and took an annual rental income of €200k, this income would be completely sheltered from tax because of the initial 'loss' – in this case the €500k purchase price.

This provided a very attractive investment proposition for individuals and businesses alike and during the boom years many rushed to take advantage of it.

However, with the proposed tax changes, property investors will only be able to shelter the higher of either 20% or €80k of their rental income from tax, with the rest being subject to tax as high as 50%, depending on the investors' circumstances.

So, in the example used above, the investor, having paid €500k for the property and taking €200k annual rent, would have to pay tax on €120k of the rental income as they would only be allowed to use tax allowances to shelter €80k. The result is a significantly increased tax burden for anyone who has invested in commercial property where previously they had been getting this income tax-free.

This is a stinging blow that will be felt by anyone with commercial property holdings – from larger corporations through to individuals, including many who, during better times, invested large amounts of their savings directly in commercial property believing it would provide a good means of tax efficient income, perhaps for retirement.

## **A Stay of Execution**

In recent weeks, following determined lobbying by the Irish Taxation Institute, the Irish Property Owners Association and other influential groups, a stay of execution has been granted until a fuller assessment of the economic impact of these changes is completed.

While in the interim this is good news for property investors, it does mean the exchequer will miss out on the €60 million that these changes had been expected to bring into the treasury. This money will have to be made up from somewhere else, most likely by tweaking business taxes.

But before commercial property investors heave a collective sigh of relief, a word of caution. While this economic assessment is likely to take several months, it should be noted that the powers-that-be have reserved the right to enforce any tax changes sixty days after the economic assessment has been completed.

Should these changes or some less heavy-handed but still punitive alternative be implemented, this does not reasonably give property investors much time to make plans to reduce their tax liabilities. Offloading property is not likely to be a great option for the foreseeable future with so many facing negative equity, assuming they can even find a buyer.

So what steps can property investors take to plan for increased property taxes and when should they take them?

### **Plan Today for Tax-Saving Tomorrow**

Thankfully there are still steps that commercial property investors can take to help reduce their potential tax liability – both now and after the tax changes are finalized. One effective but often overlooked way of doing this, is by making sure all Capital Allowances and other available property tax reliefs are being fully utilised.

Capital Allowances are tax reliefs which apply to certain items of capital expenditure including plant and machinery. In commercial properties, items such as fixtures and fittings within the building are included, for example heating, lighting and ventilation systems, sanitary ware, lifts, carpets – even desks and items of furniture. The vast majority of property investors, both professional commercial property investors and individual private investors, either under-claim capital allowances or do not claim them at all. As a result, many property investors are, unknowingly, sitting on potential goldmines of unclaimed tax relief. And as there is no limit to the number of years you can go back, you can still make a claim for property you bought ten or even twenty years ago.

The value of these tax reliefs on plant and machinery should not be underestimated and could make a significant difference to anyone facing a hefty tax bill on their rental income in future – and perhaps even a significant tax rebate right now.

So what now? If you own any property assets and are worried about the impending tax changes and how they will affect you, it's worth asking a property tax specialist to carry out a review of your position now. By taking action today, you could be saving yourself from a huge tax headache tomorrow.

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