

# Apartment Owners' Network

*Representing the owners of apartments and houses in managed estates*

**BY EMAIL:** [taxpolicy@finance.gov.ie](mailto:taxpolicy@finance.gov.ie)  
Tax and Fiscal Treatment of Landlords Consultation  
Tax Policy Division  
Department of Finance  
Government Buildings  
Upper Merrion Street  
Dublin 2  
D02 R583

6 April 2017

Dear Sirs,

**Re: Tax and Fiscal Treatment of Landlords  
Public Consultation**

On behalf of the Apartment Owners' Network I enclose a short submission in relation to the above.

We should be obliged if you would confirm safe receipt of the enclosed in time for your deadline of Friday 7 April 2017.

Yours faithfully,



David Rouse  
**Director**

*Encl.*

# **Apartment Owners' Network**

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## **Tax and Fiscal Treatment of Landlords Consultation**

**Submission**

**to**

**Tax Policy Division**

**Department of Finance**

**6 April 2017**

## **CONTENTS**

**1.0 Introduction**

**2.0 Details of Submission**

**3.0 Conclusion**

## Abbreviations Used

AON	Apartment Owners' Network CLG
MUD Act	Multi-Unit Developments Act 2011
OMC	Owners' Management Company
PIA	Personal Insolvency Act 2012
PMA	Property Management Agent
PRTB	Private Residential Tenancies Board
PSRA	Property Services Regulatory Authority
RTA	Residential Tenancies Act 2004
TCA	Taxes Consolidation Act 1997

## **1.0 Introduction**

### **1.1 Executive Summary**

This submission responds to the public consultation of 10 March 2017 issued by the Tax Policy Division of the Department of Finance in relation to the tax treatment of residential landlords.

The Apartment Owners' Network submits that the following amendments to tax law be considered-

1. Home Renovation Incentive Scheme to allow relief for OMCs/apartment owners
2. Tax deduction for management fees only where tenancy registered with PRTB
3. Tax deduction for management fees available only on paid basis
4. Exemption from Corporation Tax for OMCs in respect of incidental income
5. Exemption from Income Tax for fees and expenses paid to OMC directors
6. VAT recovery on sinking fund capital expenditure incurred by OMCs
7. Temporary exemption from Income Tax for "accidental" landlords
8. Increase Revenue powers to inspect OMC records

Further details on each proposal are set out in Section 2.

### **1.2 About the Submitter**

The AON is a volunteer-led, independent, non-party political organisation. We represent the interests and views of owners, both owner occupiers and investors, and OMCs, of dwellings in managed estates throughout Ireland.

Membership of the Network is diverse. We include owners who are directors of OMCs, residents living in estates where the OMC remains controlled by the estate developer, and residents of houses in managed estates.

As of the date of this submission, residents of 300 estates approximately are recorded as being engaged with the AON- see details on [www.apartmentownersnetwork.org](http://www.apartmentownersnetwork.org). Many more estates engage with the Network on an ad hoc or informal basis.

The AON has working relationships with various national and local government agencies. These include the Law Reform Commission, the Department of Justice and Equality, the PSRA, the ODCE, Society of Chartered Surveyors Ireland (Residential Committee), and Dublin City Council (“DCC”).

The Network played a central role in securing the formulation and enactment of the Multi-Unit Developments Act 2011 (“the MUD Act”).

The AON meets in open forum approximately once a month at DCC Civic Offices, Wood Quay, Dublin 8. Meetings and activities are currently facilitated by funding from DCC, and by the work of its volunteer members.

The Network incorporated as a Company Limited by Guarantee (No. 592683) on 10 November 2016, and is establishing formal structures as a representative organisation.

Further information about the Network’s activities is available at-  
[www.apartmentownersnetwork.org](http://www.apartmentownersnetwork.org).

### **1.3 Context to submission**

#### **1.3.1 Apartment numbers**

It has been estimated that in Ireland 500,000 people approximately live in homes in multi-unit developments<sup>1</sup>.

There has in the last 10-15 years been a rapid growth in the number of apartment/multi-unit development homes as a component of the national housing stock.

According to Census 2016<sup>2</sup> since 2011 there has been an increase of 15% in the number of apartment dwellings in the State. In the same period the total number of homes in the country grew by 3%. This means that the apartment sector represents by far the fastest growing component of the national housing stock.

Apartments now comprise 11% of all occupied homes nationally. They account for 34% of all occupied homes in Dublin City.

Given these changes public policy, including tax policy, should support the sustainability of apartment and multi-unit developments as a key component of the national housing stock.

#### **1.3.2 Brief overview of apartment management**

In order to inform the reader, and to provide context for the tax proposals in this submission, we provide a brief explanation of how apartment and multi-unit developments are structured and managed.

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<sup>1</sup> Presentation to AON by P Mooney, Benchmark Property, 14 January 2016

<sup>2</sup> Census 2016, Chapter 9 “Housing”

[www.cso.ie/en/media/csoie/releasespublications/documents/population/2017/Chapter\\_9\\_Housing.pdf](http://www.cso.ie/en/media/csoie/releasespublications/documents/population/2017/Chapter_9_Housing.pdf)

An Owners' Management Company comprises a board of volunteer directors, typically civic-minded residents or owners in the estate. The directors are elected by the wider body of apartment/unit owners in the estate, i.e. the membership of the OMC.

In the vast majority of cases the directors are not paid. However, they are charged with the primary responsibility of managing the estate common areas and shared services, and of ensuring adherence to the principles of good estate management. Effective stewardship of the OMC is vital to ensuring the upkeep of the estate. It is essential to ensuring that the estate is a good community in which to live.

The OMC agrees a budget each year and levies an annual service charge on each unit owner. This management fee pays for the aforementioned services. It is required by law to include a contribution to a long-term sinking fund for non-recurring/capital expenditure (e.g. lift replacement).

A management agent is appointed by the OMC to attend to the day-to-day operational running of the estate. This includes common area maintenance and upkeep, block insurance, domestic waste disposal, landscaping, etc.

### ***Mutuality/community***

It is important to note that while taking the form of a body corporate, an OMC is in reality a community/mutual organisation. This is borne out by the fact that an OMC is often heard to be referred to as "the residents' committee".

An OMC is established in law as company limited by guarantee. It is not-for-profit, by definition has no shareholders, and does not pay a dividend.

Any excess of income over expenditure is either allocated to a sinking fund, or it is carried forward towards the cost of provision of estate services for the following year.

### **1.3.3 Service charge recovery challenges**

Service charge debt recovery is widely accepted as the most significant and immediate financial challenge confronting OMCs and their directors.

Many OMCs are faced with current fee recovery rates of less than 70%. Aged debtors can run to five or more years, and cumulatively can represent in excess of 100% of the OMC annual budget. Sinking Fund provision is in many cases tied up in debtors. As a consequence many OMCs are forced to give priority to the costs of basic estate services only: insurance, refuse collection and common area lighting.

The mutual and unique nature of annual service charge debt was given recognition in law by Section 2(1) of the Personal Insolvency Act 2012. Services charges are an "excludable" debt under the PIA, meaning that they may be covered by a Personal Insolvency Agreement only with the consent of the creditor, in this case the Owners' Management Company.

In many ways service charge debt and estate services represent a microcosm of Exchequer revenues and public services. They have the same collective and mutual

features. In both cases, where compliance levels and recovery rates are poor, service provision can deteriorate. Where a proportion of individuals fails to contribute there are adverse effects for the wider community. In the case of apartment developments the adverse effects are felt by neighbours and other owners.

Properly funded OMCs that can-

- meet their annual expenses (particularly non-discretionary costs such as insurance and waste collection), and
- appropriately enhance the estate over time,

ensure the maintenance and improvement of apartments as a growing component of the national housing stock. Sound financial management reduces the risk of developments looking to the State or local government for support in the future for funding; this is in contrast to regrettable difficulties experienced in recent high profile cases.

As noted, arrears in the payment of management fees are endemic in the OMC sector. This problem severely restricts the optimal management of estates. It restricts the provision of vital services, negatively impacting the overall quality and supply of owner occupier and rental property to the market.

The Network submits that through the practical tax measures laid out in this submission the State can support the proper funding of OMCs. It is submitted that these tax measures will sustain the apartment/MUD sector as a housing type into the future.

## **2.0 Details of Submission**

We expand below on the detail of our tax proposals. They reflect the community and not-for-profit nature of OMCs. Our proposals are intended to support the sustainability of apartment dwellings as a growing proportion of the national housing stock.

Our proposals are borne out of our practical and lived experience of issues arising in the management of multi-unit developments.

### **1. The Home Renovation Incentive Scheme should be amended to allow relief to OMC members for qualifying expenditure incurred by OMCs**

There is a clear inequity in the Home Renovation Incentive (“HRI”) Scheme as between the tax treatment of owners of traditional residential dwellings and the tax treatment of the owners of apartments/multi-unit developments.

As the HRI is currently constituted in Section 477B TCA neither an OMC nor its members are entitled to claim tax relief for the VAT element of the cost of repair, renovation or improvement works to the common areas of apartment blocks.

An owner (owner-occupier or landlord) of a traditional residential dwelling may access tax relief for the VAT (at 13.5%) on qualifying expenditure in respect of the entirety of the physical structure of his property. Whereas, in contrast, an owner of an apartment is not entitled to access tax relief in respect of all of the physical structure of the property. This is even though, like the first owner, he will in substance have incurred the qualifying expenditure. In the apartment owner’s case some of the expenditure in question is incurred through his annual service charge.

#### ***Qualifying expenditure***

The HRI relief applies to a wide range of expenditure including landscaping, plumbing, painting and decorating, window replacement, etc. Common areas of apartment blocks (e.g. water tanks, lifts, etc.) are obviously essential to the habitability and sustainability of an apartment as a home. In substance such facilities are an integral part of the owner’s residence or rental property. In legal form, the OMC discharges the cost of repairs, renovations and improvements to apartment common areas. However, as noted above, the works are in substance funded by a proportion of the owner’s annual service charges.

#### ***Inequitable treatment***

An apartment owner is not entitled to relief because, while he, together with his neighbours/co-owners, has funded the works, he has not “incurred” the expenditure directly. This is a clear discrimination in tax law between taxpayers who are in substance in the same economic position.

The OMC does not qualify for relief under HRI because the common areas are not considered to be “qualifying premises”. In addition, OMCs, as not-for-profit entities, are highly unlikely to have a tax liability against which a VAT refund could be credited.

In order to qualify for relief, an apartment owner would be required to pay the contractor directly for the cost of the works to the common areas. However this proposition is simply not practical. It fails to take account of the realities of how apartment dwellers and apartment owners pay for the upkeep of the complete physical structure of their homes. It does not recognise how apartment blocks are maintained and upgraded at a collective level, through the mechanism of the OMC.

The Network submits that the HRI legislation in Section 477B TCA be amended to allow OMC members access tax relief for qualifying expenditure incurred by an OMC on their behalf. This is provided the owner meets the conditions of the scheme in all other respects. It should also be conditional on the owner being in good standing with the OMC as regards service charges.

***Alternative measure***

This suggestion is made without prejudice to the above.

An element of the annual service charge comprises a contribution towards enhancement capital expenditure on the property. Explicit reference in Section 552 TCA should be made to owners in apartments/MUDs. This would ensure that they are clearly entitled to a base cost deduction for Capital Gains Tax on the element of the service charge made up of enhancement expenditure incurred by the OMC on the owner/member's behalf.

This proposal is obviously of relevance only to owners not entitled to avail of Principal Private Residence Relief from Capital Gains Tax under Section 604 TCA.

**2. Conditionality on tax deduction for landlords for apartment management fees**

A tax deduction for apartment management fees should be available to residential landlords only where the tenancy has been registered with the PRTB under the RTA.

This proposal mirrors the conditionality in Section 97(21) TCA on the tax deductibility of interest on borrowings for the purchase, improvement or repair of residential property.

This change will have multiple positive effects including:

- a. Improvement of apartment service charge recovery rates for OMCs.
- b. Reduction in the risk of future State bailouts of developments with inadequate sinking funds.
- c. Encouraging compliance with landlord and tenant law.
- d. Improvements in residential letting standards.

### **3. Tax deduction for apartment management fees available on a paid basis only**

This measure is self-explanatory. Its aim is to prevent non-owner occupiers from building up service charge arrears. As outlined earlier, such debts are detrimental to the position of other OMC members, and to the orderly management of the estate.

It is submitted that it is against public policy that delinquent owners are currently entitled to obtain the benefit of a Case V tax deduction for service charges accrued but not in fact paid to an OMC.

### **4. Exempt OMCs from the charge to Corporation Tax**

The Network submits that OMCs should be exempt from the charge to Corporation Tax in respect of incidental/non-service charge income, e.g. deposit interest on sinking fund balances.

This will have multiple positive effects including:

- a. Recognition of the not-for-profit, community/mutual nature of OMCs
- b. Making available additional funds for sinking fund provision
- c. Removal of tax administrative burden (CT1 filing) on currently affected OMCs

### **5. Exemption from Income Tax for certain fees and expenses of OMC directors**

In the vast majority of cases OMC directors are unpaid volunteers, however in Company Law they take on the full responsibilities and duties of the office of director. In cases where OMC affairs require regularisation, or where there is disharmony in the running of the estate, the role of director can involve a considerable time commitment.

The Network submits that in cases where OMC directors are remunerated such income and reasonable expenses should be exempt from Income Tax. This could be subject to a cap of a maximum of €5,000 in total fees and expenses per individual per annum.

This measure will have multiple positive effects including:

- a. Encouraging owners, including landlords, to take up the OMC director role.
- b. Removal of tax administrative burden (PAYE filings) on OMCs.

In this regard, the Network notes the precedent of an exemption from tax for expenses paid to Non-Executive Directors of Irish companies travelling from abroad to Ireland. This treatment is set out in Revenue Operational Manual 05-02-19<sup>3</sup>.

We note also the favourable treatment afforded to members of non-commercial bodies under Section 195A TCA, as outlined in detail in Chapter 4.9 of Revenue's

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<sup>3</sup> <http://www.revenue.ie/en/about/foi/s16/income-tax-capital-gains-tax-corporation-tax/part-05/05-02-19.pdf>

Statement of Practice SP - IT/2/07<sup>4</sup>. The Network submits that OMC directors should explicitly be included within the terms of Section 195A.

We note for the avoidance of doubt that this measure should not apply to individuals who act as professional directors for a multiplicity of OMCs.

### ***Alternative measure***

As an alternative to an exemption from Income Tax, the Network submits that OMC directors should be entitled to a deduction from Total Income. The deduction would reflect the cost of personal time spent and the responsibilities taken on by acting as an OMC director.

## **6. Permit VAT recovery on sinking fund expenditure incurred by OMCs**

OMCs are not entitled to recover VAT. At current VAT rates most expenditure incurred by OMCs carries an additional cost of up to 23%.

The VAT Consolidation Act 2010 should be amended to allow OMCs to reclaim VAT on common areas capital expenditure, for example lift and other major plant replacement.

Without prejudice to the foregoing, VAT recovery could be subject to the condition that any VAT reclaimed must be contributed to the estate sinking fund. This would allow OMCs to maintain common areas to a high standard.

By improving OMC finances, our proposal would also reduce the likelihood of OMCs reliance on State or local authority funding where sinking funds cannot meet major expenditure.

## **7. Temporary exemption from Income Tax for “accidental” landlords**

Apartment/MUD estates have many so-called “accidental” landlords. This cohort of OMC membership is prevented from adequately maintaining, or disposing of properties. These barriers to an efficient property market arise due to negative equity, and the burden of large loan repayments relative to rental income.

The difficulties are compounded by tax liabilities arising to owners where there are rental losses. This is restricting liquidity in the residential property market. The problem is likely to be exacerbated when interest rates rise.

As noted in the consultation document, accidental landlords may have a taxable rental profit in instances where they have a rental loss in cash terms, after making mortgage repayments and meeting other outgoings, including services charges.

The Network proposes an exemption from Income Tax in such cases for the first five years of rental income. This measure would promote the quality of rented residential stock, and would contribute to liquidity in the residential property market.

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<sup>4</sup> [http://www.revenue.ie/en/practitioner/law/statements-of-practice/sp\\_it\\_2\\_07.pdf](http://www.revenue.ie/en/practitioner/law/statements-of-practice/sp_it_2_07.pdf)

This measure is not without comparable precedent. The clawback of Stamp Duty relief for accidental landlords of residential property under Sections 91, 91A, 92 and 92B of Stamp Duty Consolidation Act 1999 was removed by Finance Act 2008. Details are outlined in Tax Briefing 71 (April 2009)<sup>5</sup>.

***Mortgage Interest Relief – accelerate 100% deduction***

We submit also that the phasing in of the 100% tax deduction for interest costs introduced by Section 16(1) of Finance Act 2016 should be accelerated for such cases, such that 100% interest relief applies in respect of interest accrued on or after 1 January 2018. This measure could be made subject to the conditions outlined for Proposals 2 and 3.

**8. Increase Revenue powers to inspect OMC records for the purposes of supporting Revenue interventions, up to and including Revenue Audits, in relation to delinquent taxpayers**

OMCs retain detailed records of management fee arrears. It is submitted that owners in service charge arrears may have compliance issues in other contexts. OMC records may therefore have a function in assisting Revenue with improving compliance rates.

**3.0 Conclusion**

The Network wishes to thank the Department for the opportunity to make a submission.

We trust that the views expressed will be given due consideration in the Department's deliberations.

We would be glad to meet with the Working Group to expand on our proposals.

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<sup>5</sup> <http://www.revenue.ie/en/practitioner/tax-briefing/archive/71/stamp-duty-audit.html>