Your Ref: Our Ref: Date: 14 December 2010

Mr Brian Lenihan TD,
Minister of Finance
Department of Finance
Government Buildings
Upper Merrion Street
Dublin 2

Re: Budget 2011
Phased Abolition of Property-Based 'Legacy' Reliefs

Dear Minister,

We are writing in relation to Budget 2011 and specifically the phased abolition of property-based 'legacy' reliefs.

While we acknowledge the difficult position the country is in at present, it is important that the impact of the decisions taken are fully considered both from a direct and indirect perspective.

In the summary of budget measures and the associated financial resolutions, it would appear that it is proposed

(a) from 1 January 2011 to restrict the S23 type relief and capital allowances to the property that gave rise to the relief
(b) any unused S23 relief and capital allowances to be lost at the end of the tax life (10 years or 7 years)
(c) termination of all unclaimed and unused S23 relief and capital allowances from 2014 (Guillotine from 2014)

- ***Abolition is <u>not</u> Phased***

Firstly, it is important to understand that most tax structured investments such as Hotels, Nursing Homes, Creches, Private Hospitals, etc do not deliver a rental profit for Investors. They are structured such that rental income equals bank interest. In addition the majority of S23 properties are loss making due to the level of debt used to acquire the properties.

Therefore, the proposed abolition is **<u>not</u>** phased and it will impact immediately from 1 January 2011.

- ***Trading Business / Nursing Homes, Private Hospitals, etc / Jobs***

The proposed changes are likely to put a strain on relationships between Promoters, Investors and the Banks who funded these developments as additional tax liabilities will arise.
It is likely that this will result in additional costs for the associated trading operations (e.g. Nursing Homes, Private Hospitals, etc), which could result in closure and/or redundancies. It is necessary to consider the implications across the whole economy.

- ***Small Family Business / Jobs***

A significant number of the taxpayers who invested in the property based incentives would be small family business owners.

We would have a number of clients, who would have a small family business, where the trading company rents the property from the owner. The owner would have acquired S23 properties with 100% finance at above market value due to the associated tax relief.

Given the current economic climate, the property value has decreased significantly and the trading businesses are already under severe financial pressure. The addition of the immediate abolition of property based tax relief is likely to result in an inability to repay the property loans and ultimately could potential lead to the failure of his trading company.

In addition to the negative impact for the tax payer, there will be a knock on affect for the Banks, employees and communities as a whole given that small family businesses are key to the survival of the Irish Economy.

- ***Retrospective Nature***

These Property Based Investments were brought in by the Government to encourage investment in areas where a social benefit was deemed would arise, (e.g. Nursing Homes, Creches, Urban and Rural Renewal, etc.).

The Investors in these property based incentives did so in good faith and with legitimate expectation that the tax incentives provided by the Government would be available.

Already, this legitimate expectation has been interfered with as these reliefs have been significantly restricted through the High Earners Restriction. What is now proposed is to restrict or guillotine these reliefs further, with the taxpayer not having the ability to utilise these reliefs.

The tax relief associated with properties resulted in a higher price being paid by investors for the properties. This resulted in higher VAT and Stamp Duty being received by the Government. Therefore, it would appear that the Government were happy to benefit from the additional tax revenue generated by the sale of these properties but wish to withdraw the relief in such a way that investors are not in a position to utilise the relief.

- ***Future Tax Based Investments (e.g. BES)***

A key feature in Budget 2011 was the expansion of BES to encourage job creation. At present, our firm manages one of the few BES designated funds. In the current economic climate raising BES investment from taxpayers is extremely difficult. Obviously, taxpayers are extremely cautious and risk averse given the decline in the value of investments in general.

The retrospective nature of the abolition of property based reliefs will undermine the positive changes introduced to BES in that it brings an additional risk that the Government may in the future decide to retrospectively withdraw BES relief.

- ***Foreign Direct Investment***

Similarly, the retrospective nature of the abolition of property based reliefs will undermine the R&D tax credit regime. Multinational companies considering incurring significant investment in R&D facilities in Ireland will make a decision based on the incentives being offered by Ireland. Where they feel that there is a risk in the future of the Government retrospectively phasing out the R&D relief, this will be factored in to their decision and may well result in them not deciding to locate in Ireland.

Conclusion

We have attached a number of examples, which clearly reflect the negative impact such a change will have on taxpayers, Banks and the economy as a whole.

In addition to the direct impact on taxpayers, trading operations and Banks, it is also necessary to consider the indirect negative impact retrospective tax legislation will have on the ability of Ireland to use tax reliefs to create future employment through BES or attracting foreign direct investment.

While we would fully accept that in the current difficult times the country finds itself in, it is necessary to restrict these property based reliefs that has already been implemented through the High Earners Restriction.

We would strongly recommend that the Government consider introducing the restriction that the relief applies to the property giving rise to the relief from 1 January 2011, would only apply to properties purchased / who first year claim for the relief is in 2011. This would result in a more phased abolition as against the almost immediate abolition of the relief.

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We would be obliged if you would consider this matter further with your colleagues and the Department of Finance. We would be happy to discuss this matter further with the Department of Finance.

Yours sincerely,

Sean McSweeney
Tax Director
Quintas
sean.mcsweeney@quintas.ie

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Examples

- Creche

We have clients who invested approximately €4.5m on two Creches. Each year there is capital allowances of €645,000. There would be a rental profit of €125,000 with the remaining €520,000 of allowances being used by our clients against other rental income and in certain instances €31,750 would be offset against total income.

Even before Budget 2011, the specified relief restriction being reduced to €80,000 (in most instances) impacted on our clients' ability to use the capital allowances.

Following Budget 2011, if the capital allowances are restricted to the property which gave rise to them then our clients will not be in a position to utilize €520,000 of allowances each year. In addition, where unused allowances are carry forward they will be lost once the 7 year period has expired. The allowances will not even be available against rental profits on the Creche properties after the 7 year period. Thus €520,000 of allowances per annum will be lost over the next 3 years with a further €305,000 in the final year giving a total of €1,865,000 of allowances being lost.

- Small Family Business

For example, we have a client who acquired two S23 properties with 100% finance at €350,000 each. He is receipt of rental income from his company of c.€70,000 per annum. This rental income is being used to repay the €700,000 debt on the S23 properties, plus additional debt on residential investment properties that he acquired.

His trading company is already struggling in the current climate. The property market has also crashed and there is significant negative equity and with addition of the abolition of tax relief it is likely that he will be unable to repay the loans, which could potentially lead to the failure of his trading company.

- Nursing Homes

We have a client that has spent over €4m on building and expanding his Nursing Home. Under the high earners restriction the capital allowances available is already restricted to €80,000 per annum. It is proposed that any allowances unused after the 7 years will be lost, therefore over €3m of capital allowances will be lost. Obviously the guillotine in 2014 would also impact to restrict further from 7 years down to 4 years. This is clearly going to impact his ability to trade and repay his Bank debt.