

A Guide to the Living over the Shop Scheme



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Living over the Shop Scheme

Introduction

This scheme covers commercial premises fronting onto qualifying streets in Cork, Dublin, Galway, Limerick and Waterford. The aim of the scheme is to provide traders and investors an opportunity to develop existing vacant or under-utilised space over commercial premises into residential accommodation. The scheme also provides tax incentives in respect of the commercial element of the property.

The Living over the Shop Scheme commenced on 6 April 2001 and is due to terminate on 31 December 2004. The relief applies to qualifying expenditure incurred within this qualifying period.

Note: To qualify for relief, the relevant local authority must have certified in writing that the construction, refurbishment or conversion, is consistent with the aims, objectives and criteria for the Living over the Shop Scheme as outlined in circular UR43A dated 13 September 2000 issued by the Department of the Environment and Local Government. This certificate is referred to as a “Letter of Certification” throughout this guide. Persons intending to carry out such work are advised to contact their local authority in advance.

Enquiries

Enquiries regarding taxation matters may be made to your local tax office (whose address and telephone number will be on any communication you received from that office).

Enquiries regarding the issue of Certificates of Compliance and Certificates of Reasonable Cost should be made to:

**The Department of the Environment and Local Government,
Government Buildings,
Ballina,
Co. Mayo.**

Enquiries regarding qualifying streets in the cities of Cork, Dublin, Galway, Limerick or Waterford should be made to the local authority in whose functional area the street is situated.

This guide gives details on the commercial and residential parts of the scheme. While every effort is made to ensure that the information given in this publication is accurate, it is not a legal document. Responsibility cannot be accepted for any liability incurred or loss suffered as a consequence of relying on any matter published herein.

Commercial Premises

Introduction

The scheme provides accelerated capital allowances for qualifying expenditure incurred on the construction or refurbishment of a commercial building or structure or part of a commercial building or structure that fronts onto a qualifying street. Relief is available where:

- The commercial premises are contained in the ground floor of an existing building **or** a replacement building **and**
- Expenditure on the construction, refurbishment, or conversion of rented residential accommodation or owner-occupier accommodation is also incurred on the upper floor or floors of the building or replacement building. **Expenditure carried out on the commercial element of the building cannot exceed expenditure on the residential element i.e. the amount of expenditure which qualifies for relief is limited to the amount available under the residential relief sections.**

The ground floor of the building must be in use for commercial purposes. If it is temporarily vacant any future use must be for commercial purposes.

Qualifying commercial premises

Qualifying commercial premises are premises which front onto a qualifying street and which are in use either by an owner-occupier for the purposes of a trade or profession or by a lessee renting on bona fide commercial terms at arms length. No part of the commercial premises on which relief is claimed may be used or be partly in use as a dwelling. Industrial premises, offices, and premises used for the provision of mail order and financial services are excluded from the scheme.

Construction expenditure

Construction expenditure includes the actual cost of construction and in the case of the demolition of an existing building, it also includes the cost of dismantling the building (e.g. cost of erecting scaffolding etc) site clearance, site renovation, preparation, (e.g. drainage, sanitation, power and water supply).

Refurbishment expenditure

Refurbishment expenditure in relation to commercial premises, means any work of construction, reconstruction, repair or renewal, including the provision or improvement of water, sewerage or heating facilities, carried out in the course of the repair or restoration, or maintenance in the nature of repair or restoration, of the building or structure.

Refurbishment expenditure qualifies only where it amounts to 10% or more of the market value of the commercial part of the building before refurbishment.

Apportionment of costs

Where a commercial property is purchased from a builder and forms part of a building, (i.e. commercial on ground floor and residential on upper floor/s) the site cost and cost of the building will be apportioned on a just and reasonable basis.

Withdrawal of Relief

A balancing charge will arise if the commercial premises are sold or cease altogether to be used within 13 years of first being used after the construction expenditure was incurred, or in the case of capital expenditure on refurbishment, within 13 years after the capital expenditure on the refurbishment was incurred.

Commercial Premises	
Owner-Occupier/Trader	<p>50% initial allowance in Year 1 with 4% annual allowance thereafter until the balance of the qualifying expenditure has been written off, or</p> <p>For those who do not wish to claim 50% of the expenditure in year 1, the annual allowance of 4% may be increased up to 50% in any year (known as free depreciation) with 4% annual allowance for other years until the qualifying expenditure has been written off.</p> <p>Initial allowance The building does not have to be in use in order to claim this allowance but a trade must be carried on. The allowance is given for the chargeable period related to the expenditure. It is made in taxing the trade. Expenditure incurred before trading is deemed to have been incurred on the first day of trading. Accordingly, the allowance is not available until the chargeable period in which the trade commences. The allowance is fixed and must be claimed in the one year.</p> <p>Free Depreciation Free depreciation allows an owner-occupier to increase the amount of annual allowance due for any tax year over a number of years. This allowance is more flexible than the initial allowance and may be claimed over a number of years. However, the total amount claimed in this way may not exceed 50% of the qualifying expenditure. Free depreciation may not be claimed if the initial allowance has already been claimed.</p> <p>Annual Allowance To qualify for annual allowance the building must be in use at the end of the “basis period” for the tax year involved. The annual allowance may be claimed by the person who holds the relevant interest in relation to the qualifying expenditure, incurred on the building. An initial allowance and an annual allowance may not be claimed in respect of the same expenditure in the same tax year.</p>
Investor/Lessor	<p>50% initial allowance in Year 1 and a 4% annual allowance thereafter until the balance of the qualifying expenditure has been written off.</p> <p>Initial Allowance In a rental situation, the entitlement to initial allowance does not arise until the property is let and a tenancy has commenced.</p> <p>Free Depreciation Free depreciation is not available to lessors</p> <p>Annual Allowance To qualify for annual allowance the building must be in use at the end of the “basis period” for the tax year involved. The annual allowance may be claimed by the person who holds the relevant interest in relation to the qualifying expenditure which was incurred on the building. An initial allowance and an annual allowance may not be claimed in respect of the same expenditure in the same tax year.</p>

How relief is granted

Owner-Occupier

The capital allowances are given in taxing the individual's trade. If the capital allowances are greater than the person's trading income, an excess capital allowance will arise. Where an excess capital allowance arises it is carried forward to future years and is granted against the trading income of the person. Alternatively, the person may elect to have the excess capital allowance set off against his/her other income of the year in which the excess arises.

Example – Trader

In the year 2002 an individual has trading income of €20,000 and is due an initial allowance of €23,000 in respect of refurbishment work carried out to his business premises. He is also in receipt of employment income of €20,000.

2002	€
Trading profits	20,000
Capital allowance	<u>23,000</u>
Taxable profits	Nil

Excess capital allowance: €3,000 – in this example the individual has opted to have the excess capital allowance treated as a trading loss, shown as follows:

2002 Liability

	€
Trading profits	Nil
Employment income	<u>20,000</u>
	20,000

Less

Trading loss (i.e. excess capital allowances)	<u>3,000</u>
Taxable income	17,000

Lessors

The allowances are available primarily against rental income from all sources within the State. Where the allowance is greater than the income the excess is carried forward or the person may elect to have the excess set against their other income. The amount that can be offset against non-rental income in certain cases is restricted to €1,750,

Example -Lessor.

In the year 2002 an individual has rental income of €7,000 and is due capital allowances, of €40,000 (initial allowance). He is also in receipt of employment income of €36,000.

2002	€
Rental income	7,000
Capital allowance	<u>40,000</u>
Assessable	Nil

Excess capital allowance: €33,000 – in this example the individual has opted to have the excess capital allowance set against his other income in the year of assessment, however, this is restricted to €1,750. The unused capital allowance (i.e. €1,250) is carried forward to set against the rental income for the year 2003.

2002 Liability	€
Rental Income	Nil
Employment income	<u>36,000</u>
	36,000

Less (excess capital allowances)	<u>31,750</u>
Taxable income	4,250

Owner-occupier (traders) and lessors must elect to have excess capital allowances set against other income **within two years of the end of the tax year in which the excess arises.**

How to claim the relief

A claim for the relief should be included with the annual tax return.

The following documents, as appropriate, are required in support of a claim. They should be retained and submitted to the tax office if required:

- Letter of Certification issued by the local authority.
- In the case of property, which has been purchased, a copy of the purchase contract between the parties showing the purchase price. Where the building is let, a copy of the lease(s).
- Where all or part of a commercial building is newly constructed, evidence of the total cost of the work. If any of the work was carried out outside the qualifying period, details of the cost of work carried out during the qualifying period should be shown separately. In the case of the purchase of a newly constructed building, evidence of the cost of the site including the cost of any building originally on the site and incidental costs relating to that building should be retained.

- Where a commercial building is newly refurbished, evidence of the total cost of the work. If any of the work was carried out outside the qualifying period, details of the cost of work carried out during the qualifying period should be shown separately. In the case of the purchase of a newly refurbished building, evidence of the site cost and the cost of the building before refurbishment should be retained.

Non-Availability of Capital Allowances

Capital allowances are not available under the Living over the Shop Scheme in the following cases:

Property Developers

Capital allowances for expenditure incurred on the construction or refurbishment of industrial or commercial premises are not available to a property developer where the property developer owns the relevant interest for capital allowances purposes in the building and the construction or refurbishment was carried out by the property developer or by a person connected with the property developer.

A property developer is defined as a person carrying on a trade, which consists wholly, or mainly of the construction or refurbishment of buildings or structures with a view to their sale.

Small or Medium Enterprises

As regards expenditure incurred on or after 6 April 2001, the special incentives are available only to small or medium-sized enterprise within the meaning of Annex 1 to Commission Regulation (EC) No 70/2001 of 12 January 2001. [OJ No L10 of 13 January 2001, p33]

Excluded Activities

The special incentives are not available in respect of expenditure incurred by an owner-occupier trading in the following trades or activities:

1. In the sector of agriculture, including the production, processing and marketing of agricultural products,
2. The coal industry, fishing industry or motor industry,
3. The transport, steel, shipbuilding, synthetic fibres or financial services sectors, or

In relation to any building or structure or qualifying premises which is provided for the purposes of a project, the regional aid for which is limited under the “Multisectoral framework on regional aid for large investment projects” prepared by the Commission of the European Communities.

*Further details regarding these exclusions are included in **Tax Briefing, Issue 41 - September 2000** which is available on our website - www.revenue.ie*

Rented Residential Relief

Introduction

Usually referred to as “Section 23 relief” it allows the lessor of newly constructed, refurbished, or converted, residential accommodation fronting onto a qualifying street, to write off against Irish rental income (including rental income from other lettings) the cost of qualifying expenditure incurred on the construction, refurbishment or conversion of the residential accommodation.

Qualifying property

A qualifying house is a house where:

- It fronts onto a qualifying street or is comprised in a building or part of a building, which fronts onto a qualifying street.
- It is located in the upper floor or floors of an existing building or a replacement building, the ground floor of which is used for commercial purposes.
- The total floor area is not less than 38 square metres and no greater than 125 square metres. These floor area limits apply in respect of construction, refurbishment and conversion.
- A certificate of reasonable cost **or** a certificate of compliance has been issued by the Department of the Environment & Local Government.
- Without being used, it is first let under a qualifying lease, and from then on, continuously for a period of 10 years, except for reasonable periods of temporary disuse between qualifying leases.
- It is used solely as a dwelling.

How relief is granted

The amount of the expenditure, which qualifies for relief, is deducted in full from the rental income of the property. If this deduction exceeds the rental income the excess can be deducted from other rental income arising in the State for that year. Any rental loss created in the first year can be carried forward against rental income of succeeding tax years until the relief is exhausted.

Qualifying Expenditure

The expenditure, which qualifies for relief is the actual cost of the construction, refurbishment or conversion work. Where a property is purchased from a builder, the purchaser is granted relief based on the relevant price paid.

The **Relevant Price Paid** is calculated using the following formula:

$$\text{Price paid to builder (multiplied by)} \frac{\mathbf{A}}{\mathbf{B + C}}$$

Where

A = necessary construction/refurbishment conversion expenditure incurred in the qualifying period.

B = total expenditure on necessary construction/refurbishment or conversion.

C = site cost and including the cost of the building prior to construction, refurbishment or conversion.

Where a qualifying property is purchased from a builder and forms part of a building, (i.e. commercial on ground floor and residential on upper floor/s) the site cost and cost of the building will be apportioned on a just and reasonable basis.

Example – Investor

In June 2002, an individual converts the vacant first floor in a building owned by him, which has been designated under the Living over the Shop Scheme. The floor is converted into two apartments. He intends to let the apartments and claim rented residential relief. He is also in receipt of rental income from two other properties.

The details are as follows:

Conversion costs in the qualifying period	€186,000
Total conversion costs	€186,000

The rented residential relief is €186,000 and is allowed as a deduction from the gross rent payable as follows:

Apartments are let from November 2002

	€
Gross rent in 2002	3,000

Less

Insurance	300
Services (gas & electricity)	400

Rented residential relief	186,000
	<u>186,700</u>
Rental loss/deficiency:	183,700

This loss is available to carry forward against Irish rental income in the following year(s). If there is other Irish rental income arising in the same year the deficiency (loss) is to be set against the surplus (profits) from the other properties to arrive at the amount to be assessed to tax in that year.

Assume following figures for 2002

	Property 1	Property 2	Property 3
	<i>(Apartments on which rented residential relief claimed)</i>		
Deficiency	(€183,700)		
Surplus		€20,000	€30,000

€50,000 (of the deficiency of €183,700) is set off against the surplus from Properties 2 and 3 and therefore no tax is payable on rental income for 2002. The balance of the deficiency (€133,700) can be carried forward for set off against Irish rental income in the following year/s.

Sale of Property

Where a house is sold within the 10- year period, the relief granted to the seller is withdrawn. However, the relief will be available to the purchaser providing the purchaser continues to let the property for the remainder of the 10-year period under a qualifying lease. The purchaser may claim relief on the **lower** of the amount of the seller's original relief **or** the relevant price paid calculated as follows:

Price paid to builder (*multiplied by*) $\frac{A}{B + C}$

Where

A = necessary construction/refurbishment conversion expenditure incurred in the qualifying period.

B = total expenditure on necessary construction/refurbishment or conversion.

C = site cost and including the cost of the building prior to construction, refurbishment or conversion.

Where a property is sold outside the 10-year period, the purchaser is not entitled to relief even if the relief has not been claimed in respect of the property.

The relief is also withdrawn if at any time during the 10-year period, the house ceases to be a "qualifying premises," if for example the owner used the property as his/her residence. In this case the relief will not be available to a subsequent purchaser.

The 10-year period commences from the time the property was first let under a qualifying lease.

Owner- Occupier relief

An individual who incurs qualifying expenditure on the construction, refurbishment, or conversion of property fronting onto a qualifying street, and to be used as his/her private residence is entitled to a deduction from his/her total income in respect of the qualifying expenditure.

Qualifying property

A qualifying house is a house where:

- It fronts onto a qualifying street or is comprised in a building or part of a building, which fronts onto a qualifying street.
- It is located in the upper floor or floors of an existing building or a replacement building, the ground floor of which is used for commercial purposes.
- The total floor area is not less than 38 square metres and no greater than 125 square metres. These floor area limits apply in respect of construction, refurbishment and conversion.
- A certificate of reasonable cost **or** a certificate of compliance has been issued by the Department of Environment & Local Government.
- It is first used, after the expenditure is incurred, as the main residence of the individual claiming the relief.

How relief is granted

An individual is entitled to a deduction from total income of 10% per annum of the qualifying construction, refurbishment, or conversion expenditure over 10 years.

Qualifying Expenditure

The expenditure, which qualifies for relief is the actual cost of the construction, refurbishment, or conversion work carried out in the qualifying period. Where a property is purchased from a builder, the purchaser is granted relief based on the relevant price paid. The relief due is calculated using the following formula:

Price paid to builder (*multiplied by*) $\frac{\mathbf{A}}{\mathbf{B} + \mathbf{C}}$

Where

A = necessary construction/refurbishment conversion expenditure incurred in the qualifying period.

B = total expenditure on necessary construction/refurbishment or conversion.

C = site cost and including the cost of the building prior to construction, refurbishment or conversion.

Where a qualifying property is purchased from a builder and forms part of a building, (i.e. commercial on ground floor and residential on upper floor/s) the site cost and cost of building will be apportioned on a just and reasonable basis.

Example – Owner-Occupier

In January 2002 an individual agrees with his local authority to construct an additional storey above his commercial property to enhance the streetscape. The construction is completed in November 2002 and construction costs amount to €200,000. A claim for owner-occupier relief is made in January 2003. The relief due for 2002 is €20,000 and is allowed as follows:

	€
2002	
Trading income	48,000
Less	
Owner-Occupier relief	<u>20,000</u>
Taxable income	28,000
	 28,000 x 20% = 5,600
Less	
Single persons tax credit	<u>1,520</u>
Tax due	4,080
Tax paid	<u>12,480</u>
Refund due	8,400

The individual is taxed under the self-assessment system, therefore the relief will appear on the notice of assessment in respect of the year 2002 and in respect of the nine following years, as a deduction from total income. An individual, who is taxed under the PAYE system, will receive the relief for each relevant year on the **Notice of Determination of Tax Credits and Standard Rate Cut-Off Point**.

Owner-Occupier and sharing arrangements

Owner-occupiers may decide to share their house with family or friends. In such situations the owner-occupier relief continues to apply, provided that the house continues to be used by the individual as his/her main residence in the tax year involved. Any income from the sharing arrangement should be included in the owner-occupier's tax return. Owner-occupiers are also entitled to claim Rent-a-Room relief.

Sale of property

If the property is sold any unused relief cannot be passed to the purchaser. There is no claw-back of owner-occupier relief already granted to the owner. A full year's owner-occupier relief may be claimed for the year of sale providing the property is the only or main residence of the individual at some time during that year.

Rented residential and owner-occupier

The following documents, as appropriate, are required in support of a claim. They should be retained and submitted to the tax office if required:

- Letter of Certification issued by the local authority.
- In the case of property, which has been purchased, a copy of the purchase contract between the parties showing the purchase price. Where the building is let, a copy of the lease(s).
- A Certificate of Compliance in the case of a newly constructed refurbished or converted house purchased from a builder, which will be lived in or let by the purchaser.
- A Certificate of Reasonable Cost where a new house is to be lived in or let by the person who built it or had it built, or where a refurbished or converted house is to be lived in or let by the person who refurbished/converted it or had it refurbished or converted.
- Where a building is newly constructed, evidence of the total cost of the work. If any of the work was carried out outside the qualifying period, details of the cost of work carried out during the qualifying period should be shown separately. In the case of the purchase of a newly constructed building, evidence of the cost of the site including the cost of any building originally on the site and incidental costs relating to that building should be retained.
- Where a building is newly refurbished or converted, evidence of the total cost of the work. If any of the work was carried out outside the qualifying period, details of the cost of work carried out during the qualifying period should be shown separately. In the case of the purchase of a newly refurbished or newly converted building, evidence of the site cost and the cost of the building before refurbishment or conversion should be retained.
- Work on the residential element of the building should be itemised separately to work on the commercial element of the building.

Rented residential and owner-occupier

The following definitions apply in relation to construction, refurbishment and conversion expenditure for both rented residential relief and owner-occupier relief.

Construction expenditure

Construction carried out on the residential element of a building must be “**necessary construction.**” Necessary construction means one or more of the following:

- Construction of an extension to the building not exceeding 30% of the existing floor area of the building, where such an extension is necessary for the purposes of facilitating access to, or providing essential facilities in, one or more qualifying premises.
- Construction of an additional storey or additional storeys to the building, which are necessary for the restoration or enhancement of the streetscape.
- Construction of a replacement building where a Dangerous Building Order has been issued on or after 13 September 2000 and before 31 March 2001 in respect of the existing building and a replacement building is required to restore the natural streetscape. The replacement building must be consistent with the character and size of the original building. Also, the demolition of an existing single storey building may be required for structural reasons to facilitate the construction of an additional storey/storeys to the building, which are necessary for the restoration or enhancement of the streetscape.

Conversion expenditure

Qualifying conversion expenditure is the conversion into a house of part of a building (i.e. the upper floor/s) which fronts onto a qualifying street and which before the conversion had not been in use as a dwelling or the conversion into two or more houses of part of a building which fronts onto a qualifying street and which before the conversion, had not been in use as a dwelling or had been in use as a single dwelling only.

Conversion expenditure includes expenditure incurred on either or both of the following-

- a) The carrying out any work of construction, reconstruction, repair or renewal, and
- b) The provision or improvement of water, sewerage or heating facilities.

Note: Relief on conversion expenditure applies only to the residential element of the building.

Refurbishment expenditure

Qualifying expenditure is expenditure incurred on the refurbishment of a building which fronts onto a qualifying street which, before being refurbished consisted of two or more houses and since refurbishment consists of two or more houses.

Refurbishment expenditure includes expenditure incurred on either or both of the following-

- a) The carrying out any work of construction, reconstruction, repair or renewal, and
- b) The provision or improvement of water, sewerage or heating facilities.

In order to obtain tax relief in respect of refurbishment on the residential element of the property, it is essential that the Department of Environment & Local Government certify that the work was necessary to ensure the suitability of the accommodation as a dwelling.

House

House includes any building or part of a building used or suitable for use as a dwelling and any out-office, yard, garden or other land usually enjoyed with that building or part of a building. It also includes a flat or an apartment.

Certificate of Reasonable Cost

A certificate of reasonable cost is required where:

- A newly constructed house/flat is to be lived in or let by the person who built it or had it built, or,
- A refurbished or converted house/flat is lived in or let by the person who refurbished/converted it or had it refurbished or converted.

Certificate of Compliance

A certificate of compliance is required where a newly constructed, refurbished or converted house/flat is purchased from a builder.

Applications for a certificate of compliance or a certificate of reasonable cost may be made to the Department of the Environment & Local Government, Government Offices, Ballina, Co. Mayo.

Certificates of Reasonable Cost and Certificates of Compliance are required only in respect of the residential element (i.e. rented residential or owner-occupier) of the building.