

## **High Income Individuals' Restriction**

### **Order of offset of reliefs, allowances and deductions**

#### **Part 15-02a-06**

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<sup>1</sup> See also Tax and Duty Manual Part 04-08-08 on further issues relating to capital allowances. This section of the manual is not a complete summary of the provisions and restrictions relating to capital allowances. It looks solely at the manner in which certain allowance are granted and the order in which these allowance is made.

## 1. Purpose of manual

This manual clarifies the order of offset of reliefs, allowances and deductions for individual taxpayers. This is particularly important for taxpayers who are subject to the High Income Individuals' Restriction ("HIIR") under Chapter 2A of Part 15, Taxes Consolidation Act 1997 (TCA).

Consideration must first be given to the order of offset of reliefs implicit in each relief and then to any impact the provisions of the HIIR have on that.

While this manual is intended to provide guidance on HIIR cases, it also covers issues around the order of offset of various reliefs and allowances.

## 2. General principles

To understand the order of offset of reliefs it is necessary to understand how a tax liability is computed. The steps are as follows.

- i. Calculate the profits or gains from a source.

Certain amounts are deductible in calculating the profits or gains from a source, e.g. amounts which qualify under section 81 TCA for trading income or section 97 TCA for rental profits (Case V).

- ii. Calculate the profits or gains which are to be charged to tax.

Certain amounts are deductible in charging profits to tax. These sections often refer to the profits for a year of assessment; for example, under section 278(1) TCA, Case V allowances for a year of assessment are relevant in charging the Case V profits for that year of assessment to tax.

- iii. Calculate the profits or gains on which a person is to be assessed to tax.

Once the profits have been charged, or brought to account, certain amounts are deductible from the profits or gains on which a person is assessed. Where a person has a Case V loss forward, relief under section 384 TCA is given by deducting the loss forward from the profits on which the person is chargeable under Case V.

- iv. Calculate total income.

Total income is defined in section 3 TCA as "the total of income from all sources". Certain amounts are deductible in computing total income. Relief for payments under a deed of covenant (section 792 TCA) is given by providing that the income is deemed to be the income of the person who receives the payment and not the income of any other person. That income therefore cannot form part of a person's total income, as defined, and relief is given by way of deduction in computing total income.

- v. Calculate taxable income.

Taxable income is defined as the amount of income on which a person is to be charged to income tax<sup>2</sup>. It is calculated as total income, less the deductions from total income allowed under section 458 TCA. For example, section 458 includes section 502 as one of the deductions permitted under total income, and section 502(2) provides that relief for investments which qualify for the Employment Investment Incentive (“EII”) scheme is given as a deduction from total income for the year of assessment.

### 3. Main reliefs claimed by individuals who are also subject to the HIR

Implicit in how certain reliefs are granted is the order in which they must be granted. While an individual who is subject to the HIR may claim reliefs other than those dealt with in this manual, it should be possible to determine the place of any other relief in this order of offset based on how the relief is phrased, exactly what the relief is deducted from, or in computing or charging.

#### 3.1. Rental Capital Allowances <sup>3</sup>- Case V

##### 3.1.1. Industrial Building Allowances (e.g., nursing homes)

Where a lessor of a building is entitled to claim industrial buildings allowances <sup>4</sup>section 278(1) TCA provides that relief for these allowances will be given in charging the individual’s Case V income.

##### 3.1.2. Plant and Machinery

A lessor of furnished rented residential accommodation is entitled to an annual wear & tear allowance for plant & machinery (e.g. fixtures & fittings) under sections 284(6) and (7) TCA. Section 300(4) provides that these allowances shall be made in charging the individual’s income under Case V<sup>5</sup>.

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<sup>2</sup> Taxable income, being the income on which a person is chargeable to tax, should not be confused with the amount of profits being charged to tax under various Schedules / Cases in (i) above.

<sup>3</sup> See also [Tax and Duty Manual Part 04-08-08](#) on further issues relating to capital allowances. This section of the manual is not a complete summary of the provisions and restrictions relating to capital allowances. It looks solely at the manner in which certain allowance are granted and the order in which these allowance is made.

<sup>4</sup> For example, an Industrial Buildings Annual Allowance under section 272(2).

<sup>5</sup> See [Tax and Duty Manual Part 09-02-03](#) which provides detailed guidance on the treatment of leasing income and capital allowances for plant and machinery in leased commercial buildings.

### 3.1.3. Excess Case V capital allowances

Situations where Case V allowances are greater than the Case V income are dealt with under section 305 TCA.

Under section 305(1)(a), unused allowances are carried forward to be deducted from an individual's Case V income in future years; that is, unused allowances carried forward are deducted in charging the income to tax in that future period.

Section 305(1)(b) provides that an individual may elect to have excess current year Case V capital allowances<sup>6</sup> deducted from their other income for a year of assessment. This is a deduction in computing total income. An excess of current year Case V capital allowances over a person's other income may then be claimed as a deduction against the income of a spouse / civil partner in the case of joint assessment. Any amount of such allowances not so relieved in the current year are then carried forward under section 305(1)(a).

Where an election is made to offset excess current year capital allowances section 305(1)(b)(i) clarifies that any capital allowances carried forward into that year are used against Case V income before current year allowances<sup>7</sup>.

Where the tax acts are silent on the order of offset the taxpayer can choose whether to claim carried forward capital allowances or current year capital allowances first.

## 3.2. Rental losses

Section 384 TCA provides that a Case V loss is carried forward and deducted from the amount of profits on which the person is assessed under Case V in the next year of assessment. In addition, section 384(4) states that other allowances to be made in charging income under Case V should be made in priority to this loss relief.

Case V capital allowances are therefore used in priority to Case V losses forward.

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<sup>6</sup> Section 406 disapplies this section for the purposes of capital allowances on plant and machinery in residential lettings and section 403 disapplies it, with certain limited exceptions, in the case of leased plant and machinery. Therefore, section 305(1)(b) generally only has relevance in the case of capital allowances for industrial buildings and in most cases the restrictions contained in section 409A on the amount which can be offset apply.

<sup>7</sup> While section 304(4) provides that capital allowances and IBAs carried forward from an earlier year are generally deemed to be part of the current year allowances, section 304(6) disapplies that section when looking at Case V.

### 3.3. Trading Capital Allowances

#### 3.3.1. Industrial Building Allowances (e.g., nursing homes)

Where a trader is entitled to claim industrial buildings allowances, section 278(1) TCA provides that these allowances are given in taxing the individual's trade.

Section 321(4) provides that references to an allowance being made in taxing a trade means in charging the profits or gains of the trade to income tax.

#### 3.3.2. Plant and Machinery

Section 284(1) TCA provides for an annual wear and tear allowance for plant and machinery used for the purposes of a trade. Section 300(1) provides that these allowances are made in taxing the individual's trade. Applying section 321(4), relief for these capital allowances is given in charging the profits or gains of the trade to tax.

#### 3.3.3. Excess trading capital allowances

Where all capital allowances granted in respect of a trade cannot be used against the profits of that trade in the current year, section 392 TCA provides that the individual may elect to use those excess capital allowances<sup>8</sup> to increase or create a trading loss under section 381<sup>9</sup> (see paragraph 3.4 below). Under section 392(2) relief is given for an actual trading loss in advance of relief being given for these excess capital allowances.

Where trading capital allowances are greater than the related trading profits, then any amount not used (and not subject to a claim under section 392) is carried forward under section 304(4), which provides that capital allowances which cannot be used against trading profits in a year are carried forward and will be deemed to be part of the current year allowances in future years. Where a claim is made under section 392 and the resultant 'loss' is greater than the profits against which it is to be relieved, any amount of capital allowances not so used are carried forward as capital allowances and not as a trading loss (section 393(1)).

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<sup>8</sup> Section 391(2)(a) provides that any capital allowances carried forward from previous years cannot form part of a section 392 claim.

<sup>9</sup> Section 403 provides that, with certain exceptions, a loss sustained in a trade of leasing plant and machinery cannot, to the extent that it is attributable to wear and tear allowances on leased assets, be set off against any profits/gains other than profits/gains from the trade of leasing.

Section 409A restricts the relief that a partner who is not an active partner can claim for any portion of a loss from a partnership trade referable to certain IBAAAs.

Where relief is claimed under section 392, then relief is granted for allowances carried forward in advance of relief for current year allowances (section 391(2)(b)). In other circumstances where the Tax Acts are silent on the order of offset, the taxpayer can choose whether to claim carried forward capital allowances or current year capital allowances first.

### 3.4. Trading losses

Section 381 TCA is used to determine at what point relief is given for a normal trading loss. Relief is technically given on a repayment basis by re-computing the taxpayer's liability to income tax for the year of claim. Section 381(5)(b) provides that relief for the losses is regarded as a deduction made from a class of income or income from a source, in computing total income.

To claim relief under section 381, it is therefore necessary to determine the income related to a class of income, or the amount of income from a source, as it is from that amount that the loss relief is deducted. This means relief under section 381 is one of the last reliefs which a taxpayer claims in computing total income.

It should be noted that a taxpayer cannot choose to claim relief under section 381 against some of their other income. That is, a taxpayer can claim relief against all their other income in the year, or against none of their other income in a year. They cannot claim relief against, for example, Case V income only while paying tax on Case III income.

Where relief for the full amount of the loss is not claimed under section 381, then the amount of unused loss is carried forward and, under section 382, deducted from the profits of the same trade which are assessed under Case I in subsequent years of assessment.

## 4. Impact of HIIR legislation on the order of reliefs

In a year of assessment, an individual who is subject to the High Income Individuals' Restriction (HIIR) may be able to claim some reliefs which are 'specified reliefs' and subject to the HIIR and other reliefs which are not subject to the restriction. Therefore, in addition to the order of offset determined with reference to the relieving provisions themselves, section 485C (3) TCA indicates the order of offset between specified and non-specified reliefs. The rules in this provision apply across the Tax Acts and apply whether or not a taxpayer is subject to the HIIR.

#### 4.1. Capital allowances – section 485C(3)(a)

Section 485C (3) TCA does not alter the priority in which capital allowances are given but provides that, where another provision requires that carried forward allowances are used in priority to current year allowances<sup>10</sup>, non-specified capital allowances carried forward (for example, industrial buildings allowance on a factory) are deemed to be used in priority to specified capital allowances (for example, industrial buildings allowance on a nursing home).

In general terms, the order of priority for these allowances for the purposes of the Tax Acts is:

- i. Carried forward non-specified capital allowances
- ii. Carried forward specified capital allowances
- iii. Current year non-specified capital allowances
- iv. Current year specified capital allowances

However, as indicated at paragraph 3.1 and 3.3 above, there are instances where the Tax Acts do not specify the order of offset between carried forward and current year allowances.

#### 4.2. Other rental deductions – section 485C(3)(ab)

Any deductions which are specifically set out in section 97 TCA as an allowable deduction (for example, rent payable on a “head” lease) are allowable in priority to anything deemed to be deductible under a specified relief (those listed in Schedule 25B TCA).

#### 4.3. Deductions from total income - section 485C(3)(ac)

Where a person has deductions from total income which are both specified and non-specified, those which are non-specified are given in priority.

For example; where a person invested in EII shares (specified relief) and also pays permanent health insurance premiums, when claiming the reliefs priority is given to the permanent health insurance premiums over the EII investment.

#### 4.4. Losses - section 485C(3)(b)

Loss relief for a loss which is not referable to a specified relief – for example, a rental loss created by having rental expenses in excess of rental income - is used in priority to a loss which is referable to a specified relief (e.g. a loss created by a “**section 23**” type relief).

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<sup>10</sup> E.g. s.305(1)(b)(i) or s.391(2)(b)



#### 4.5. Order of offset

Each category of relief or deduction must be looked at separately. Within each category, non-specified reliefs must be used before specified reliefs.

No comparison should be made between categories of relief. Section 485C(3) TCA does not provide that non-specified reliefs in general should be used before specified reliefs. It only provides for priority within each individual category of relief or deduction.

#### 4.6. Carry forward of excess reliefs

Any amount of excess reliefs carried forward to future years are allowed as a deduction from total income under section 485F(1) TCA. Relief for excess reliefs will always be given after any other relief under section 485F(3) TCA.

### 5. USC Property Relief Surcharge<sup>11</sup>

The order of offset of reliefs for the USC property relief surcharge is the same as that for the HIIR with the proviso that a specified relief which is a specified property relief is used before a specified relief which is not a specified property relief.

### 6. Are reliefs claimed before or after the application of the HIIR?

The HIIR calculation is carried out after claiming all reliefs and deductions.

Section 485G (4) provides that where the calculation of a relief, deduction, credit or reduction in the amount of tax payable requires that total income, taxable income, tax payable or tax chargeable for the year be taken into account, then that calculation should be done **before** the application of the HIIR. The main exception to this is the calculation of a credit for foreign tax due under a double taxation agreement<sup>12</sup>.

Any relief which is claimed, for example section 381 TCA loss relief, must therefore be claimed before the HIIR is applied. An additional amount cannot be claimed after the application of the HIIR to reduce the recalculated taxable income.

### 7. Taxpayers seeking to 'disclaim' allowances and reliefs

Some taxpayers have sought to 'disclaim' certain allowances and reliefs. Generally, this is only an issue where those allowances and reliefs are specified reliefs – for example, nursing home capital allowances - and the taxpayer is seeking to claim a non-specified relief such as a section 381 claim to offset a trading loss sideways against other income rather than the specified relief.

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<sup>11</sup> See [Tax and Duty Manual Part 18d-00-01](#)

<sup>12</sup> See [Tax and Duty Manual Part 15-02a-05](#)

## 7.1. Capital allowances

### 7.1.1. Current tax returns

While there is no provision in the TCA which allows an individual to disclaim capital allowances, Revenue precedent IT953012, based on the ruling in UK case of **Elliss v BP** [1987] 59 TC 474, indicates that Revenue should accept tax returns where a taxpayer has chosen not to claim a capital allowance to which he or she is entitled.

A capital allowance can be claimed in full or disclaimed/not claimed. It is not possible to partially claim a capital allowance.

#### **Example:**

Jo has:

	€
Case V profits	100,000
Case V IBAs – building A	(55,000)
Case V IBAs – building B	(20,000)
Case I loss	(30,000)

Jo has the following options available in relation to the IBAs. Jo can:

- claim the full €75,000 IBAs and €25,000 of the trading loss,
- claim €55,000 IBAs on building A and the full €30,000 Case I loss,
- claim €20,000 IBAs on building B and the full €30,000 Case I loss, or
- claim none of the IBAs and the full €30,000 Case I loss.

Where a taxpayer is choosing not to claim capital allowances, the provisions of sections 287, 304(4), 305(1), 272(4) and 274(1)(b) TCA should be borne in mind.

- Section 287 provides that if a taxpayer chooses not to claim certain capital allowances in relation to plant and machinery in a given year, those allowances are deemed to have been given. They are not available for use in future periods.
- Section 304(4) and 305(1)(a) provide that where full effect cannot be given to the capital allowances in a year of assessment, the unused allowances are carried forward to the next year of assessment. Therefore, if a taxpayer chooses not to claim certain industrial buildings allowances, the tax written down value of the asset will remain unchanged and there are no unused capital allowances carried forward.

**Example:**

Mr A has a factory. Industrial buildings allowances were available in respect of the cost of €100 in Year 1, giving an annual IBAA<sup>13</sup> of €4.

In Year 1 he had profits of €3. He therefore was only able to use €3 of his Year 1 IBAA, carrying forward the other €1 under section 304(4). The tax written down value of the factory at the end of Year 1 is €96.

In Year 2 Mr A had profits of €6 but he wished to claim relief for a trading loss under s.381 instead of his IBAAs for the year. He therefore claims no IBAA in Year 2. The €1 of IBAAs carried forward from Year 1 can only be carried forward to Year 3 if there is insufficient income in Year 2 against which to use them. Therefore, Mr A can choose to either use those allowances in Year 2 or they will be lost. The tax written down value of the factory at the end of Year 2 is €96.

This can be illustrated as follows:

Cost	Year	IBAAs 'claimed'	TWDV	IBAAs c/fwd
€100	1	€4	€96	€1
	2	Nil	€96	Nil

- The general scheme of IBAAs is such that no capital allowances can be claimed after the expiry of the tax-life of the industrial building. Section 274(1)(b) provides that no balancing allowance or charge is to be made after the end of the tax life of the building. Section 272(4) provides that when a person buys a second hand building, that person's ability to claim IBAAs is linked to the tax-life of the building.

**Continuing with the Example:**

Mr A's factory has a tax life of 25 years. Ordinarily at the end of the tax life the factory will not have tax written down value. However, as Mr A has chosen not to claim all of his IBAAs his factory will have a tax written down value after 25 years. No IBAAs can be claimed after the expiry of the tax life of the factory, and no balancing allowance / charge will arise after the expiry of that tax life.

<sup>13</sup> This example ignores initial allowances.

The following material is either exempt from or not required to be published under the Freedom of Information Act 2014.

[...]

#### 7.1.2. Amending past tax returns

Attempts have been made to retrospectively amend tax returns to disclaim capital allowances and instead claim a trading loss, for example. This, if accepted, would take the taxpayer out of the HIR and thus give rise to a repayment of tax on the basis of an error or mistake. This is therefore a claim for repayment of tax to which section 865 (four year time limit) applies<sup>14</sup>.

The following material is either exempt from or not required to be published under the Freedom of Information Act 2014.

[...]

### 7.2. Excess relief carried forward

In some cases excess relief carried forward from prior years has not been claimed. Had it been claimed, the taxpayer would have been within the HIR and would have had an increased amount of tax payable. Section 485F TCA provides that a taxpayer is “entitled to a deduction” for amounts carried forward. Based on the UK courts interpretation in the *Ellis v BP* cases, it is likely that a Court would also view this wording as permissive and giving the taxpayer the choice about whether to use the relief. On that basis, as with capital allowances, branches should accept current tax returns where no claim has been made for excess relief carried forward.

As with allowances, branches need to consider on what basis a taxpayer is entitled to a repayment of tax before processing any retrospective amendments to prior year returns.

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<sup>14</sup> See [Tax and Duty Manual Part 37-00-30](#)

## 8. Worked Example

### Step 1. Calculate the profits from each source.

		<i>Available</i>		<i>Total</i>	<i>Legislative References</i>
		€	€	€	
<b><u>Case I</u></b>					
Trade 1	Tax adjusted profits		100,000		
Trade 2	Tax adjusted loss	(300,000)	-		
Trade 3	Tax adjusted profits (leasing trade)		20,000		
<b><u>Case IV</u></b>	Deposit Interest		10,000		
<b><u>Case V</u></b>					
Property 1	Profits (rented residential)		10,000		
Property 2	Profits		20,000		
<b><u>Schedule E</u></b>	Emoluments		400,000		

**Step 2. Charge the income to tax (claiming relevant deductions such as capital allowances).**

			Available		Total	Legislative References
			€	€	Chargeable €	
<b><u>Case I</u></b>						
Trade 1	Tax adjusted profits			100,000		
	Capital allowances carried forward	Non-specified		(20,000)		s.391(2)(a) &
	Capital allowances current year	Non-specified		(30,000)		s.485C(3)(a)
		Specified		(10,000)	40,000	
Trade 2	Tax adjusted loss		(300,000)	-		
	Capital allowances carried forward	Non-specified	(15,000)	-		
		Specified	(5,000)	-		
	Capital allowances current year	Non-specified	(15,000)	-		
		Specified	(5,000)	-	-	
Trade 3	Tax adjusted profits (leasing trade)			20,000		
	Wear & tear allowances <sup>15</sup>	Non-specified		(3,000)		s.391(2)(a) &
	Industrial buildings allowances	Non-specified		(7,000)		s.485C(3)(a)
	Wear & tear allowances	Specified	35,000	(10,000)		
	Industrial buildings allowances	Specified	12,000	-	-	
<b><u>Case IV</u></b>						
	Deposit Interest			10,000	10,000	
<b><u>Case V</u></b>						
Property 1	Profits (rented residential)			10,000		
	Wear & tear allowances	Non-specified		(2,000)		s.300(4)
Property 2	Profits			20,000		
	Wear & tear allowances	Non-specified		(2,500)		s.300(4)
	Industrial buildings allowances carried forward	Specified		(7,000)		s.305(1)(b)(i)
	Industrial buildings allowances current year	Specified	15,000	(10,500)	8,000	s.278(1) & s.305(1)(b)
<b><u>Schedule E</u></b>						
	Emoluments			400,000	400,000	

<sup>15</sup> The law does not specify whether W&T or IBAs should be used first.

**Step 3. Assess the income (claiming relevant deductions such as losses forward).**

		<i>Available</i>		<i>Total</i>	<i>Legislative References</i>
		€	€	<i>Assessable</i>	
<b><u>Case I</u></b>				€	
Trade 1	Chargeable to tax		40,000		
	Loss carried forward	Non-specified	50,000	(40,000)	- s.382
Trade 2	Chargeable to tax		-	-	
Trade 3	Chargeable to tax		-	-	
<b><u>Case IV</u></b>	Chargeable to tax		10,000	10,000	
<b><u>Case V</u></b>	Chargeable to tax		8,000		
	Case V loss carried forward	Non-specified	(4,000)		s.384(4) &
		Specified	50,000	(4,000)	- 485C(3)(b)
<b><u>Schedule E</u></b>	Emoluments		400,000	400,000	

**Step 4. Calculate Total Income (claiming relevant deductions).**

			Total €	Legislative References
<u>Case I</u>	Assessable		-	
<u>Case IV</u>	Assessable		10,000	
<u>Case V</u>	Assessable		-	
<u>Schedule E</u>	Assessable		400,000	
<b><u>Deductions in computing Total Income</u></b>				
	Trading losses		(300,000)	s.381
	Current year trading capital allowances	Non-specified	(15,000)	s.392, s.391(2)(b) &
		Specified	(5,000)	485C(3)(a)
	Excess Case V industrial buildings allowance (subject to s.409A restriction)	Specified	(4,500)	S. 305(1)(b)
<u>Total Income</u>			85,500	

**Step 5. Calculate Taxable Income (claiming relevant deductions from Total Income).**

			Total €	Legislative References
<u>Total Income</u>			85,500	
	Excess relief carried forward under section 485F	Specified	(85,500)	485F(1)
<u>Taxable Income</u>			-	