The Local Property Tax

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Introduction

This report examines the Local Property Tax which comes into effect on the 1st of July 2013. It looks into the background to property taxation in Ireland and assesses why the introduction of such a tax is necessary at present. The report also explains the disposition of The Local Property Tax; how it is calculated, how it is paid and possible benefits or drawbacks that may arise as a result.

Background

Up until the end of 1996 Ireland had utilised property tax as a source of revenue. Firstly there were Domestic Rates on residential properties which were abolished in 1978, followed by the Residential Property Tax introduced in 1983 that was in place up until the end of 1996. The Residential Property Tax was due on valuable properties if the income of the owner exceeded a certain limit. The tax base was narrow and revenue yields were insignificant. The amount of households that were liable never exceeded 20,000 until a flat rate (as opposed to a proportion of valuation) was introduced in 1994. Despite the introduction of a flat rate only 1,500 more households paid the tax in 1994, less than 2% of the population, which resulted in roughly €16.5 million in revenue in the last two full years of operation of the tax (195 and 1996).

A tax on second homes was introduced in 2009. The Non-Principal Private Residence Charge is a flat rate charge of €200 levied on the owner of the property.

A new property tax was proposed in the National Recovery Plan in November 2010 as a means of correcting large fiscal imbalances. Since then, two separate taxes have been introduced; an interim Household Charge and the Local Property Tax.

The Household Charge was introduced in 2012 and required homeowners pay a flat rate of €100. Due to its regressive nature, amongst other things, it was not readily accepted and it is believed that at present approximately 700,000 have still failed to pay this fee.

Both the Household Charge and the Non-Principal Private Residence Charge are to be replaced by The Local Property Tax (LPT) which is a tax based on the market value of a property. The LPT is due to come into effect on the 1st of July 2013. The Household Charge was abolished from the 1st of January 2013 and the NPPR will be abolished from the 1st of January 2014. All outstanding balances however will remain attached to the property even after the taxes have been abolished.

Stamp Duty and VAT will remain alongside The Local Property Tax as is the case in the majority of countries that have a property tax. It is important for the government to move away from stamp duty as its main source of income from property taxation. The over reliance on transactional property taxes such as VAT and especially stamp duty greatly contributed to the unsustainable bubble in the governments' finances that was a major component in the current economic crisis.

Why a Local Property Tax is Being Introduced

Budget 2013 was the third budget delivered under the EU/IMF/ECB recovery programme, and contained a target to raise €1.25 Billion in additional tax revenue. Over the past four years the government has become increasingly reliant on income taxes to raise much needed revenue, so much so that despite the on-going high levels of unemployment, income tax in 2012 made up 42% of the total tax yield compared with 27% in 2006 at the height of the boom. This creates a problem as high rates of income tax act as an impediment to job creation. As a result, Budget

2013 introduced base broadening measures which are considered to be less damaging to economic recovery and job creation than income tax rate increases.

An element of this was the introduction of the Local Property Tax. The Local Property Tax is expected to yield €250 million in 2013 and €500 million from 2104 onwards. €250 million is the equivalent of a 1% increase in the standard rate of income tax.

Features of the Local Property Tax

The Local Property Tax is to be a self-assessed tax based on the market value of the property. As it is being implemented in July, property owners will only be obliged to pay an initial half a year's tax in 2013. The main features of the Local Property Tax are:

- Homeowner's are the liable persons. Only in cases of long-term tenancy agreements of twenty years or more are the tenants responsible.
- The amount payable is dependent on the market value of the property. Market value will factor in fundamentals such as property size and features, location, access to amenities, transport links etc.
- It is a self-assessment system. Therefore although people will be provided with a Revenue estimate of the amount of property tax due, households can supply their own estimates which can differ.
- The Revenue Commissioners will be in charge of administering and collecting the tax.
- The full amount of the tax will be payable to local authorities. Most of the tax raised in each area will go towards funding the provision of local services in the area the tax was collected. The balance will go into a central fund for use as an equalisation mechanism for poorer Local Authority Areas where the Property Tax receipts will be low.

Calculating the Tax and Payment Methods

The Local Property Tax will be calculated by first placing a property within a number of market value taxable bands. Tax liability will be determined by applying a tax rate of 0.18% to the mid-point of the respective band. The Society of Chartered Surveyors Ireland (SCSI) has advised the government that they need to put in place very clear guidelines for homeowners when valuing their property so as to assist homeowners in submitting realistic valuations.

For properties valued at over €1 million, the first million will be taxed at a rate of 0.18% and there will be a rate of 0.25% charged on balances in excess of €1 million. For the excess balances no banding will apply, the tax rate will be assessed according to the actual value of the property.

There is a minimum charge of €90 for properties valued at less than €100,000.

It is worth noting that from 2015 onwards the local authorities will be given the option to vary the rate of tax by 15% upward or downward at their discretion. Subsequently, when calculating the tax from 2015 onwards, the rate of tax may differ from one place to another, although it will still be calculated the same way.

There are a number of ways for those liable to pay the Local Property Tax so as to allow ease of payment for all individuals. It can be paid by a once off payment of cash, single debit, or using a credit card. It can also be paid through instalments either by direct debit, cash payments from a number of premises, or also through voluntary deductions from salary and welfare payments. The first payments are to be made on the 1st of July 2013.

The valuations made in May 2013 will hold for three years until revaluation in November 2016 regardless of any improvements made.

Exemptions and Deferrals

There are a few cases in which persons are exempt from paying the tax. These include:

- First time buyers that buy between the 1st of January 2013 and the 31st of December 2013. These will be exempt from the tax until the end of 2016.
- New and previously unused properties bought between 1 January 2013 and 31 October 2016. These will be exempt from the tax until the end of 2016.
- Residential properties that remain unoccupied due to the owner having a long term physical or mental illness.
- Residents of the so called 'ghost estates'.
- Owners of newly constructed but unsold properties.
- Mobile homes, boats, registered nursing homes and diplomatic properties are not included.
- There is an exemption for homes that have a certifiable level of damage caused by Pyrite.

There are also instances in which the tax can be deferred:

- Single persons whose gross income does not exceed €15,000 or couples whose joint gross income does not exceed €25,000 may defer payment until they have the means to pay.
- Those with an outstanding balance on their mortgage can deduct 80% of their mortgage interest from their gross income to determine if their adjusted gross income limit deems them eligible for deferral.
- Homeowners who are engaged in a personal insolvency arrangement can qualify for a deferral during their insolvency period.
- There is also an option for marginal deferrals in which those accountable can defer 50% of the Local Property tax. To meet these requirements the respective person's gross income or adjusted gross income must fall within €10,000 of the above limits.

Interest on deferred balances will be charged at 4% per annum.

Advantages and Disadvantages

The following are some of the advantages of a Local Property Tax:

- The economic impact is expected to be relatively small since a recurrent tax on residential property is deemed much less distortionary than a tax on income or capital.
- It is a reliable, sustainable source of revenue. Revenue generated from immobile assets is more stable than from property transaction taxes such as Stamp Duty and Capital Gains Tax.
- It will give local authorities an independent source of revenue, and enable citizens to exercise choice over the amount of public services they receive.
- It is progressive since it is assessed on the market value of the property unlike the flat rate Household Charge.

Below are a few obstacles the Local Property Tax may encounter when introduced in July:

- Some homeowners may under-estimate the value of their property. It has been suggested that random audit checks may address this problem.
- It may be difficult for those in rural areas living in their home for maybe 30 or 40 years to estimate the value of their property when only new builds surround them, and also each build is unique.
- Although 'fairer' than a flat rate charge, given that is based on the market value of the property it will not be based on peoples' incomes.
- Difficulties may arise when assessing the amount of tax due from properties that are close to the edges of the taxable bands.
- Due to a shortage of transactions in the property market it may be difficult to determine the market value of many properties.
- Differences in tax rates among local authorities could create distortions. Specifically, low tax rates on the periphery of urban areas may encourage sprawl.

- It may be perceived as an urban property tax since properties in urban areas are usually more expensive and so liable persons will pay much more than their rural counterparts[1].
- The only other countries that use a self-assessed property tax are Tunisia, Thailand, Hungary, Bogota in Columbia, and The Philippines.

Conclusion

Irelands' previous approach to property taxation led to an over reliance on property transaction taxes. In 1996, the last year the Residential Tax was in place, it only managed to raise €16.5 million whereas in that same year Stamp Duty raised €134 million and was accountable for 14% of the total exchequer revenue. After the Residential Tax was abolished, especially from 1998 onward, the government became increasingly reliant on Stamp Duty as a source of revenue. A revenue stream that depends on the magnitude and value of property transactions is not as stable as an annual property tax. This over-reliance led to serious fiscal problems when the property market crashed. It is clear that a new configuration of taxation of property in Ireland is necessary.

[1] See Convery, Frank 2013. Property Tax-Why Dubliners Should Pay More. Publicpolicy.ie, January 2013 available at: http://www.publicpolicy.ie/wp-content/uploads/Property-Tax-Why-Dubliners-Should-Pay-More.pdf