

Plant in Leased Buildings – Treatment of leasing income and capital allowances

Part 09-02-03

Document last reviewed April 2022

Does not reflect current Revenue position.

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1 Introduction

Buildings are often let fully fitted out. The fit out will involve expenditure on plant. These lettings raise issues in relation to:

- the manner of charging the income from the letting of the plant to tax
- the entitlement to capital allowances in respect of the expenditure incurred by the lessor on plant
- how the allowances are used.

This manual deals with buildings that are situated in the State. It deals mainly with the letting of commercial buildings. [Section 8](#) deals with residential lettings. References to plant include machinery. The relevant TCA references are listed in [section 9](#).

2 Charging of income from the letting of plant

2.1 Case V

Where a composite payment made under a lease relates partly to premises and partly to items of plant the full payment is regarded as rent for the tax purposes and is chargeable under Case V. This applies whether or not the plant is integral to the building.

2.2 Case IV or Case 1

Where the plant is let under a separate lease a separate tax charge is made in respect of the income from the letting of plant. Income from leasing in the course of a trade is chargeable under Case 1. It is a question of fact whether a trade of leasing is being carried on in any particular situation. Income from leasing plant that is not chargeable under Case 1 or Case V is chargeable under Case IV.

3 How capital allowances are given

The following is a brief outline of how capital allowances are given depending on what is being leased.

3.1 Buildings

Where a building is let, industrial buildings allowances¹ are given in charging income under Case V and are available primarily against Case V. Any excess allowances arising in a particular year can be set sideways against other income, subject in most cases to an annual limit of €31,750,² with any unused allowances available for carry forward against future Case V income only.

3.2 Plant

In relation to plant it is necessary to ascertain from the lease if the plant is let in the first place, and if it is, how the lessor is entitled to the capital allowances. The following situations can occur:

- Where the plant is let in the course of a leasing trade the wear and tear allowances are given under section 284(1) against the Case 1 trading income.
- In the absence of a leasing trade the lessor is required to let the plant on such terms that he or she bears the burden of wear and tear of the plant. In this situation the wear and tear allowances are given against the income from the plant under section 298(1), that is, against Case IV income.
- Where a furnished residential building is let the wear and tear allowances are given against Case V income.

3.3 Combined letting of plant and building

Where there is a combined letting³ of plant and building, wear and tear allowances for plant are given against Case V income. Where the entitlement to the allowances arises because the landlord bears the burden of wear and tear of the let plant, the wear and tear allowances are given against the income from the letting of the plant. Such wear and tear allowances are ring-fenced to income from the letting of the plant and cannot be set sideways against other income. This is because section 403(5) disapplies the section 305(1)(b) provisions for sideways set off where expenditure is incurred on the provision of plant.

¹ Used as a generic term here to refer to all capital allowances on buildings.

² There is no annual limit on sideways set off against other income in the case of 3*** plus hotels in certain counties of the BMW region (section 409B).

³ Where the letting of the plant is provided for in the lease or otherwise associated with the rental of the building.

4 Plant integral to industrial building

4.1 Revenue practice

How capital allowances in respect of expenditure incurred on plant located in a building which qualifies for industrial buildings allowances are used may differ depending on whether the plant is integral to the building or not. Revenue practice is to allow taxpayers to elect to treat expenditure on plant that is an integral part of an industrial or commercial building⁴ as part of the construction cost of the building instead of as expenditure on plant. The effect of the election is that the expenditure on plant qualifies for industrial buildings allowances rather than for wear and tear allowances. The practice applies to expenditure incurred after 6 April 1997 on a limited number of items of plant (listed below).

Where an election is made by a person to include expenditure on a permitted item of plant in a claim to industrial buildings allowances, that person, or any other succeeding claimant, cannot subsequently elect to treat the particular item as plant.

4.2 Benefits of practice

Depending on the particular circumstances involved, there are advantages to electing to claim industrial buildings allowances instead of wear and tear allowances (but see [section 7](#)). Because the expenditure is not regarded as being incurred on the provision of plant, section 403(5) TCA, 1997 does not apply. Thus, there is greater flexibility in how the allowances can be used so that instead of being restricted to the income from the leasing of the plant, the capital allowances can be set sideways against all Case V income and any excess allowances can be set against other income up to an annual maximum of €31,750.⁵ Depending on the applicable rate of industrial buildings allowances, it may be possible to claim the capital allowances at a faster rate than the standard 8-year write-off period for plant.⁶ Another consequence of the election is that the lessor does not have to satisfy any 'burden of wear and tear' test in relation to the plant.

⁴ Building must qualify for industrial building allowances, that is, buildings included in section 268 TCA 1997, commercial buildings under the area-based incentive schemes and childcare (section 843A) and third level education buildings (section 843).

⁵ There is no annual limit on sideways set off against other income in the case of 3*** plus hotels in certain counties of the BMW region (section 409B).

⁶ Certain buildings can be written off over 7 years (15% for 6 years and 10% year 7). Accelerated allowances such as initial allowance and free depreciation may also be available.

4.3 Permitted items of plant

The practice applies to the following items of plant:

- lifts
- heating systems
- air-conditioning systems
- electricity or gas distribution systems
- water and waste services
- alarm and security systems
- fire fighting or prevention systems
- wiring associated with or ancillary to any of the above.

These are the types of integral items that would not be removed by the owner if the building is sold. They are necessary for the functioning of the building, regardless of the trade being carried on in the building. They have effectively become part of the fabric of the building and can be distinguished from other items that, while attached to the building, might be removed were the building to be converted to a different use. For example, items of fixed plant in a reception area of a hotel would probably be removed if the building were to be converted for use as a nursing home.

To qualify for the practice the listed items must actually be plant given the particular circumstances of the trade being carried on in the building.⁷

5 Treatment where Revenue practice does not apply

The Revenue practice outlined in [section 4](#) does not apply where:

- plant is integral to an industrial building but the claimant does not elect for the practice to apply
- plant is not integral to an industrial building
- plant is integral to a non-industrial building
- plant is not integral to a non-industrial building.

5.1 Combined letting of plant and building

As outlined in [section 2](#), where there is a combined letting of plant and building in the above scenarios the income is chargeable under Case V. Because the Revenue practice does not apply, capital allowances for plant must be given in the form of wear and tear allowances rather than as industrial building allowances. While the plant has to be separately identified for the purposes of ascertaining the wear and tear allowances, the allowances are given in charging the Case V income.

⁷ There is no definition of plant in the Tax Acts. Instead, its meaning comes from a large body of case law and on a 'facts and circumstances' basis. What is plant depends on the particular trade being carried on and on how the item is used in that trade. Thus, what is plant in one situation may not be plant in another situation.

Where entitlement to the wear and tear allowances arises under section 298 (lessor bears burden of wear and tear) the strict position is that the allowances should be given against the income from the letting of the plant. However, to avoid unnecessary apportioning of the income between plant and building, Revenue allows the entire income to be regarded as income from the letting of the building. The wear and tear allowances can therefore be set against the composite Case V income, but without the option to set any excess allowances sideways against other income. This is because the capital expenditure is incurred on the provision of plant (and not the building) and, in such circumstances, section 403(5) disappplies section 305(1)(b), the provision that allows excess Case V capital allowances to be set sideways against other income.

5.2 Order of set off of capital allowances

In the case of a combined letting of plant and building both the wear and tear allowances and the industrial buildings allowances are given in charging Case V income. As the Tax Acts do not provide for any particular order for setting off the allowances, the order of set off is at the discretion of the claimant. However, it should be noted that any excess allowances arising from the use of wear and tear allowances, as opposed to industrial buildings allowances, cannot be set off sideways against other income in the year in which they arise.

5.3 Separate lettings of plant and building

Where the plant and building are let separately, the income from the letting of the plant is not chargeable as Case V. The wear and tear allowances are given in taxing the Case 1 trade or in charging income under Case IV as appropriate. Section 403(5) operates to ring-fence the allowances to the income from the letting of the plant.

6 Multi-tenanted building

The common areas of commercial centres and office blocks are generally retained by the landlord. These areas contain items of plant such as lifts, heating, air conditioning and sprinkler systems. The landlord charges the tenant for the use of such plant by way of a service charge. Where the building qualifies for industrial building allowances such plant will generally be included in the industrial building allowances claim as being integral to the building in accordance with the Revenue practice.

Where the Revenue practice does not apply, the strict position is that no capital allowances are due as the plant is not in use for the purposes of a Case 1 trade and is not let. However, Revenue regards such plant as coming within section 298 if the burden of wear and tear is borne by the landlord and the building is in use for the purpose of a trade or profession carried on by the lessee. In such circumstances, the payment from the tenants for the use of the plant is chargeable under Case IV and the wear and tear allowances are given against this income without any sideways set off against other income.

7 Termination of incentive schemes – cap on allowable construction expenditure

In certain circumstances there can be a downside to electing for the Revenue practice outlined in [section 4](#). This is because the expenditure on the provision of plant is treated as expenditure on the construction of the building and as a consequence becomes subject to other provisions that apply to expenditure on the construction of buildings. The provisions in question include the transitional arrangements that were contained in Finance Act, 2006 for the phasing out of capital allowances for certain industrial and commercial buildings (see Tax and Duty Manual [Part 09-01-04](#)). As part of these transitional arrangements, the amount of construction expenditure that can qualify for capital allowances is reduced depending on when the expenditure was incurred. Thus, while there is no restriction on the amount of qualifying construction expenditure incurred in 2006, qualifying expenditure incurred during 2007 and in the period 1 January 2008 to 31 July 2008 is restricted to 75% and 50%, respectively, of the expenditure incurred. Where an election is made to treat expenditure on the provision of integral items of plant as expenditure on the construction of the building, such expenditure is also subject to the 75% and 50% caps on the amount of qualifying expenditure.

Claimants can elect to treat expenditure on the provision of integral plant that is incurred by 31 December 2006 as expenditure on the construction of the building and to treat such expenditure incurred after that date as expenditure on the provision of plant.

8 Plant that is leased with residential premises

A wear and tear allowance is available in respect of capital expenditure incurred on the provision of plant in a house which is let furnished and the income from which is chargeable under Case V.⁸ The allowance is made in charging a person's income under Case V. Accordingly, the allowance may be set off against all rental income chargeable under Case V. Unlike the position with commercial buildings, there is no requirement that the lessor bear the burden of wear and tear of the plant to qualify for the allowances.

9 Relevant TCA 1997 references

Section 96(1) – contains definition of “rent” for Case V purposes that allows for payment for goods and services to be included in payment for premises.

Section 278 – industrial buildings allowances are given in taxing Case 1 trades or in charging income under Case V.

⁸ This wear and tear allowance is available wef year of assessment 1997/98. Prior to that it was available by concession.

Section 284 – subsection (1) provides for Case 1 wear and tear allowances. Subsections (6) and (7) provides for wear and tear allowances for furnished residential lettings where the income from the letting is chargeable under Case V.

Section 298(1) – gives wear and tear allowances to lessors who bear the burden of wear and tear of the let plant.

Section 300 – wear and tear allowances are given against Case 1 income (leasing trade), against the income from the letting of plant (burden of wear and tear) or against Case V income (furnished residential lettings).

Section 305(1) – even though capital allowances (both plant and buildings) are given primarily against a particular class of income, there is provision for sideways set off of any excess allowances against other income.

Section 403 – ring-fences wear and tear allowances relating to leased assets to the income from those leased assets. Subsection (5) disapplies section 305(1)(b) and the sideways set off of excess allowances against other income where the relevant expenditure has been incurred on the provision of plant.

Section 409A – notwithstanding section 305(1)(b) imposes an annual cap of €31,750 on the amount of excess allowances that can be set sideways against other income in the case of most industrial buildings. Section 409B provides an exemption in the case of 3***plus hotels in certain BMW counties.

Does not reflect current Revenue position.