

A Submission to
The Commission on Taxation

May 23, 2008

This proposal is submitted by the University of Limerick's National Centre for Taxation Studies (NCTS) on behalf of the Irish Universities Association (IUA).

The IUA, the representative body of the seven Irish universities, seeks to advance university education and research through the formulation and pursuit of collective policies and actions thereby contributing to Ireland's social, cultural and economic development.

This proposal addresses two key issues:

- 'Philanthropic Donations' to the higher education sector; and
- Tax allowances for 'on campus' higher education building and infrastructural development.

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Proposal

This submission addresses two key issues:

- 'Philanthropic Donations' to the higher education sector; and
- Tax allowances for 'on campus' higher education building/infrastructural development.

Each of these areas will be addressed within separate sections of this submission.

This submission responds to the terms of reference area (a) in the "Guidelines for Submissions to the Commission on Taxation" as follows:

- Part (a) - To consider how best the tax system can support the economic activity and promote increased employment and prosperity while providing the resources necessary to meet the cost of public services and other Government outlays in the medium and longer term.

The submission contributes to the Commission's Contextual Framework, which is based on the Programme for Government (2007), in the following areas:

- To keep the overall tax burden low and implement further changes to enhance the rewards of work while increasing the fairness of the tax system; and
- To ensure that our regulatory framework remains flexible, proportionate, and up to date.

Summary of Overall Proposal

1. The IUA supports the recommendations of the report published by the Higher Education Authority (2006) *Supporting Investment in Higher Education*¹. This report focuses on tax based and other incentives and supports the view of the important role of tax incentives in both encouraging and supporting philanthropic donations to the higher education sector.

¹ Higher Education Authority (HEA) (2006) *Supporting Investment in Higher Education. Report of the Working Group*. HEA, Dublin.

www.heai.ie/files/files/file/archive/corporate/2007/SupportingInvestment1.pdf

2. Section 848A relief should be exempt from the limitation on the amount of certain forms of relief used by certain high income individuals².
3. The method of claiming tax relief in relation Section 848A donations and the processing of tax refunds should be reviewed.
4. Donations of non-cash amounts (e.g. shares or debentures) should not give rise to Capital Gains Tax (CGT) for the donor.
5. Section 848A relief should be extended to gifts of land or buildings; this should not give rise to Capital Gains Tax (CGT) for the donor.
6. Third level institutions should be relieved from the imposition of Value Added Tax (VAT) where specific types of buildings are funded from philanthropic donations.
7. The tax incentive scheme for the provision of new student accommodation (section 50) should be re-introduced solely for ‘on campus’ developments.
8. A construction cost tax allowance should be introduced, similar to the tax allowance for private hospitals and nursing homes, to encourage investment in facilities in the higher education sector

Summary of ‘Philanthropic Donations’ Proposal

1. We support the recommendations of the report published by the Higher Education Authority (2006) *Supporting Investment in Higher Education*³. This report focuses on tax based and other incentives and supports the view of the important role of tax incentives in both encouraging and supporting philanthropic donations to the higher education sector.
2. Section 848A relief should be exempt from the limitation on the amount of certain forms of relief used by certain high income individuals.
3. The method of claiming tax relief in relation to Section 848A donations and the processing of tax refunds should be reviewed.

Rationale

The higher education sector has played a vital role in the ongoing development of Ireland’s knowledge economy and society. Ireland’s considerable economic and social progress in recent years has been underpinned by the provision of a high quality education system, responsive to the needs of individuals and of the broader society and

² Section 848A Taxes Consolidation Act 1997 (TCA 1997)

³ Higher Education Authority (HEA) (2006) *Supporting Investment in Higher Education – Report of the Working Group*. HEA, Dublin.

www.heai.ie/files/files/file/archive/corporate/2007/SupportingInvestment1.pdf

economy. This progress on human, social, cultural and intellectual capital provision has been accompanied by new challenges and new problems, particularly in the underinvestment in capital infrastructure within the higher education sector. A report from the IUA (2006) *University Infrastructure Investment* identified the need to invest €1.7 billion to enable the universities to respond to Government policies and strategies⁴. These include:

- Strategy for Science, Technology and Innovation (SSTI);
- HEA/Forfás review of national skills needs;
- Implementation of the Bologna process;
- Increasing participation in, access to and retention in third and fourth level education;
- Increased collaboration with other institutions; and
- Provision of lifelong and flexible learning options.

Higher education has an essential role to play in enhancing the education levels of the population to create a focus on ‘home grown’ innovation⁵ in the development of new businesses, services, processes and products - thereby contributing to economic, social and cultural development. The environment in which the universities are expected to meet these demands is becoming increasingly complex and challenging.

Competition for state funding within the higher education sector is increasing. Given the reduction in state funding in real terms in recent years, there is an increasing need to obtain funds from non-state sources to enable the universities to achieve their strategic short, medium and long term objectives. The university sector is endeavouring to find additional and new sources of income to enable the efficient management of resources and to facilitate all involved in meeting the new challenges. Taxation incentives for capital development in the higher education sector have been removed in recent Finance Acts, increasing the need to be more creative in generating revenue for capital and recurrent purposes from services provision and from philanthropy.

The HEA (2006) report *Supporting Investment in Higher Education* reviewed the use of tax based and other financial incentives for funding of Higher Education Institutions (HEIs)⁶. Philanthropic donations represent a key source of potential external funding for all HEIs, Universities and Institutes of technology (IoTs), and provide a significant source of funding in other developed countries, particularly in the United States. In this context The Irish Government ‘recognises the valuable work being carried out by organisations which promote philanthropy in Ireland and will continue to explore

⁴ IUA (2006) *University Infrastructure Investment – a National Priority*. IUA. http://www.iua.ie/media-and-events/iua-e-news/dec_06/tom_higgins.html

⁵ The HEA research strategy policy document, *Creating and Sustaining the Innovation Society* (2002) highlighted that future Irish economic development strategy can no longer afford to rely on the application of knowledge generated in other countries and that a transformation to an innovation and intellectual capital creating society is essential if Ireland is to secure its position as a prosperous and socially and culturally advanced society.

⁶ Higher Education Authority (HEA) (2006) *Supporting Investment in Higher Education – Report of the Working Group*. HEA, Dublin: www.heai.ie/files/files/file/archive/corporate/2007/SupportingInvestment1.pdf

ways to facilitate philanthropic work, strengthen and deepen a culture of philanthropy in Ireland and maximise the contribution of philanthropy to the common good.’⁷

Throughout the evolution of the Irish higher education sector, state subvention, both capital and recurrent, has been the primary source for the provision of basic teaching and research services, infrastructure and facilities. The higher education sector has been very active in securing private sector philanthropic donations to complement state subventions. For example, since 1989 the University of Limerick has secured in excess of €100 million from philanthropic donations. These additional funds have made a major contribution to the University of Limerick’s advancement and to the quality of its educational provision; this refers not only to funding buildings/infrastructure but also professorships, scholarships, research equipment and endowments.

It is important to note that the majority of these philanthropic donations to the Irish higher education sector were from a small number of U.S. donors, rather than from Irish individuals or Irish corporations. This is a space that is well capable of being expanded and there are many tangible and intangible benefits to present and future Irish societies from assisting its expansion. This leads us to the key argument of this proposal:

International evidence strongly points to the provision of tax relief to the donor as the key measure in attracting philanthropic donations, and especially so in higher education sectors.

Tax Relief for Philanthropic Donations

We support the recommendations of the HEA (2006) report relating to tax based and other incentives and we are very strongly supportive of the important role of tax incentives in encouraging and supporting philanthropic donations from donors who may be so inclined, and in encouraging other potential donors to consider doing so. We also very strongly support the HEA (2006) report’s argument that tax relief on philanthropic donations needs to be strengthened, particularly in the light of recent legislative changes which have curtailed certain forms of tax relief available to high income individuals.

The taxation recommendations from the HEA (2006), relating to philanthropic donations, include:

- Land and buildings should be included in the scope of the donations’ income tax relief schemes;
- Notwithstanding a claim for income tax relief, a donor should not be subject to Capital Gains Tax (CGT) on assets donated under the scheme;
- The donations scheme should be removed from the list of tax incentives specified for the new annual cap on the use of tax relief;
- To help promote philanthropic giving of accumulated wealth for higher education funding, provisions should be included in tax law to facilitate the use of Charitable Remainder Trusts (CRTs)⁸, any such provisions should contain appropriate measures to guard against possible abuse;

⁷ *Towards 2016 – Ten Year Framework Social Partnership Agreement 2006–2015*, p. 72.

⁸ An arrangement in which property or money is donated to a charity, but the donor (the grantor) continues to use the property and/or receive income from it while living. The beneficiaries receive the income and the charity receives the principal after a specified period of time. The grantor avoids any capital gains tax

- Further more detailed work should be undertaken in due course to examine whether there are other Trust arrangements in the United States, Europe and the rest of the world that might be suitable for adoption in Ireland without facilitating abuse;
- In the case of highly sensitive projects a sum equivalent to the VAT effectively paid by the donor should be refunded by the Government; and
- Consideration should be given to allowing Irish higher education institutions to issue tax-exempt bonds on a pilot basis, and within an overall ceiling, as part of the development of their borrowing capacity.⁹

The Present Tax System

Ireland has recognised the dilemma faced by the higher education sector, and other similarly interested sectors such as charities, in providing tax relief on philanthropic donations. Legislation, for the main part, is now contained in Section 848A Taxes Consolidation Act 1997 (TCA 1997). Other provisions within the TCA 1997¹⁰ provide for tax relief in relation to scientific research in the case of donors carrying on a trade.

Section 848A

The existing provisions of Section 848A provide for tax relief for donors where the following broad conditions apply:

- The donation is in the form of cash or shares (or debentures) in certain Public Limited Companies (PLCs);
- The donation amounts to at least €250 in an accounting period or year of assessment as appropriate;
- The donation is not subject to repayment;
- Neither the donor nor any person connected with the donor receives, either directly or indirectly, a benefit in consequence of making the donation;
- The donation is not conditional on, or part of an arrangement involving, the acquisition of property by the charity/approved body, otherwise than by way of gift, from the donor or person connected with the donor;
- In the case of a company, the donation would not otherwise be deductible in computing the profits or gains of a trade or expense of management deductible in computing the total profits of the company.

(CGT) on the donated assets, and also gets an income tax deduction for the fair market value of the remainder that the trust earned.

⁹ See also: HEA (2006) Section 3. The Status of Philanthropy in the Third Level Sector [pp. 14-16]; Section 4 Tax Relief for Philanthropic Donations [pp. 17-20].

¹⁰ Section 764 (1)(b) TCA 1997 provides for a deduction for revenue expenditure on scientific research where a person carrying on a trade pays any sum to an approved body or an Irish University in order that the body or University may undertake scientific research.

Philanthropic donations broadly fall into two categories:

1. Donations from Income; and
2. Donations from Capital.

Donations from Income

The main tax relief is the deduction of the gift (minimum amount €250) for tax purposes at the donor's marginal tax rate. The potential donors can be high net worth individuals, or, for more modest gifts, the university's alumni, employees, friends, students, parents of current students and local communities.

How the relief applies: The application of this relief is dependent on whether the individual donor is taxed under PAYE or is self-employed.

PAYE donor: The gift of at least €250 per annum is deemed to be net of tax. On completion of the relevant tax form by the donor, the university then claims the tax relief, which is dependent on the marginal tax rate of the individual.

Self-employed donor: The gift of at least €250 is deemed to be gross. The individual claims the tax relief at their marginal tax rate.

Issues of concern

The following issues arise on the tax relief on these donations:

1. List of Specified Reliefs

The benefit of this relief is subject to restrictions introduced in the 2006 Finance Act (*Limitation on amount of certain reliefs used by certain high income individuals*)¹¹ which has the potential to significantly deplete the benefits of Section 848A. Philanthropic donations are accumulated with the allowances arising to an individual from tax favoured investments under Section 484E.

Ireland's new wealthy are the persons whom the universities (and Government) are attempting to encourage to donate and these individuals are also likely to be availing of tax favoured investments. If they have already reached the ceiling for the tax favoured investments, then only deferred relief will apply to any philanthropic donation made, which at a practical level in most instances removes the benefit and incentive from the donor.

It is inappropriate, in our view, to pool Section 848A donations and capital allowances on tax based properly investments for application of the restriction.

Section 848A donors do not envisage nor indeed are permitted under the TCA 1997 to receive any benefit in return for their donations. They are entitled to a tax refund equal to the level of donation at their marginal rate of tax. In contrast, an investor in a tax based

¹¹ Sections 485C to 485G TCA 1997 – see Reference no. 52 Schedule 25B TCA 1997

property investment (e.g. nursing home or crèche investment) expects a return well in excess of their investment in addition to the tax break. Other tax based property investors (e.g. investing in a Section 23 type property investment) would expect, in addition to the property's tax break, a rental yield and capital appreciation from their investments.

Recommendation:

We recommend that the current pooling of the investor relief with the philanthropic gifts, under Section 484E be reviewed with a view to the removal of philanthropic donations from the restrictions introduced in the 2006 Finance Act.

2. Method of granting tax relief to the PAYE donor (particularly for small regular donations)

The second issue is the method of granting tax relief to the PAYE donor. While it appears to remove the burden from the individual, it has two distinct disadvantages:

- The perceived tax advantage of giving a gift is not appreciated by the donor; and
- The institution has to receive the relevant forms each tax year (for a recurring gift) from the donor. Some donors ignore the request for completion of these forms as they perceive no incentive in completing them. In this event the matching tax relief to the Irish university/HEI is lost.

Recommendation:

We recommend that the method of granting tax relief on donations from the PAYE donor should be reviewed to make the tax relief more attractive to such donors. This is also an important relief for Irish charities and we appreciate that it will require wide consultation and careful review to address the current deficiencies. Among the number of methods available the following could be considered:

1. PAYE taxpayers could be treated on an identical basis to chargeable persons – *viz* allowed relief at their marginal tax rate on foot of a claim by the individual in their annual tax return. The minimum gift would need to be reviewed in the light of this recommendation. This would have the advantage of treating all taxpayers equally and the system would be simpler to operate.

or

2. All donations above a certain amount would carry a standard rate (20%) tax credit. The university/HEI would automatically receive the credit from Revenue on filing of regular returns. One disadvantage of this proposal would be a loss from those top-rate employed taxpayers who actually complete and mail the appropriate returns. However, we suspect that this loss would be more than outweighed by the tax credits received in respect of the other cohorts. In any event, a qualifying organisation might be given the choice as to whether to adopt the recommendation or to remain with the status quo for all donations - this would

overcome objections of organisations which have a high recovery rate on the top-rate tax credits.

Donations from Accumulated Wealth

There are currently no tax incentives for donations from accumulated wealth (other than as outlined in Section 848A above). However, there are perceived tax disincentives that need to be examined.

1. Capital Gains Tax (CGT).

A gift of assets, such as land or buildings, will normally not give rise to a CGT liability on the donor.

However, in the case of a gift of shares or debentures qualifying for relief under Section 848A the donor will be deemed to have disposed of the asset at open market value and be liable to pay CGT on the gift.

This significantly undermines the tax relief and can be perceived by the donor as a penalty for philanthropic giving.

2. Other Non Cash Gifts.

Where an individual gifts land or buildings or assets not specified in Section 848A then no income tax relief applies.

3. Value Added Tax (VAT).

Where a gift is given to fund a project that has an embedded VAT liability in its costs (typically a building), the funding can be perceived by the donor as partly funding VAT to the exchequer¹².

Recommendation:

We recommend that gifts of shares and debentures qualifying for relief under Section 848A should not give rise to a CGT liability on the donor. This has been successfully implemented in the United Kingdom without adverse impact on taxation revenues.

We recommend that philanthropic gifts of assets, such as land or buildings also qualify for relief under Section 848A and also carry an exemption from a CGT liability for the donor. These gifts would give rise to a 'no loss / no gain' situation, similar to other non cash donations to charities.

We fully support the HEA (2006, p. 38) recommendation that embedded VAT payments costs funded by philanthropic donations be refunded to the University/HEI either by means of a VAT Recovery Order or through a dedicated Matching Fund.

¹² See HEA (2006, pp. 37-38.)

We would also recommend that the Commission consider other forms of support to encourage increased philanthropic donations from Irish individuals and companies.

Summary of ‘Tax Allowances for ‘On Campus’ Building Development’ Proposal

1. We fully support the recommendations of the 2006 HEA report *Supporting Investment in Higher Education* relating to tax based incentives to support the continued and necessary development of ‘on campus’ facilities in the Irish Higher Education Sector.
2. The Section 50 Student Accommodation scheme should be re-introduced strictly for ‘on campus’ developments.
3. A tax allowance scheme, similar to the private hospital capital allowance scheme¹³, should be introduced to encourage investment in facilities that support the teaching, research and community support agendas of the higher education sector.

Rationale

As noted above, the HEA (2006) report reviewed the use of tax based incentives for funding of Higher Education Institutions (HEIs)¹⁴. Sections 6 and 7 of the HEA report specifically relate to ‘on campus’ based investment and clearly outline the benefits that were provided by the availability of tax allowances in enabling capital infrastructure development in the higher education sector.

In relation to Section 50 student accommodation, the Indecon report¹⁵ recommended the removal of the Section 50 scheme based on the view that the objectives of Section 50 had been met and was no longer needed. We do not agree with this conclusion of the Indecon report. The following very relevant factors also need serious consideration:

- The continuing shortage of third level accommodation in some areas, particularly Dublin and its surrounds;
- Withdrawal of off-campus Section 50 accommodation from the student market when the 10 year time frame expires;
- Evidence from the 2003/04 report on student living conditions which highlights the dependence on off-campus private rented accommodation; and
- The pressure on the existing supply of the projected growth in undergraduate student numbers, as well as the objective of doubling the number of PhD graduates outlined in the SSTI.

¹³ Section 268(1)(J) TCA 1997

¹⁴ Higher Education Authority (2006) *Supporting Investment in Higher Education. Report of the Working Group*, HEA, Dublin.

¹⁵ Department of Finance (2006) *Budget 2006: Review of Tax Schemes [Volume 1.] Indecon Review of Property-based Tax Incentive Schemes*, Department of Finance.

<http://www.finance.gov.ie/documents/publications/other/Taxreview2006Vol1.pdf>

Higher education institution residential developments must be self-financing, with a reliance on older schemes financing newer schemes as the debt on the older schemes is retired. As a result, financing and construction of development projects must be carried out over an extended period of time to avoid the risk of exposure to high levels of debt. The Section 50 scheme should be seen in this light and not merely as a short-term tax incentive.

The private hospital and nursing home capital allowance schemes were retained as the schemes would encourage the provision of facilities that would assist in meeting national policy objectives. We believe that a similar scheme would enable the higher education sector meet its national policy objectives with the risk being transferred to the investor/private operator while providing key facilities for the higher education institutions. The key facilities that could benefit from this scheme are outlined in Section 7 of the HEA (2006) report and include:

- Research facilities in line with SSTI objectives;
- Teaching facilities; and
- Conference, Sporting, Cultural, and Recreational facilities.

Section 50 Recommendation:

We recommend that the Section 50 tax allowance scheme should be re-introduced with the following restrictions:

- The scheme should be restricted to university/HEI owned on-campus residences to eliminate the risk of the accommodation reverting to private rented accommodation;
- The qualifying period should be extended to twenty years; and
- Any further measures necessary to eliminate potential abuses of the scheme.

Tax Allowance Scheme Recommendation:

We recommend that a tax allowance scheme, similar to the private hospital capital allowance scheme¹⁶, should be introduced to encourage investment in facilities that support the progressive agendas, moral and intellectual visions, and growth strategies of the Irish higher education sector. The scheme could be re-introduced with the following restrictions:-

- On the basis that the facility is made available to the third level institution on agreed terms;
- Long-term ownership of the facility rests with the higher education institution;
- The facility operates for a minimum of 20 years after which it reverts to management by the higher education institution; and
- Any further measures necessary to eliminate potential abuses of the scheme.

¹⁶ Section 268(1)(j) TCA 1997

We will be happy to respond to any of the points raised in this submission, and we wish the members of the Commission on Taxation success in their deliberations.

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