Addressing the Viability and Affordability of Apartment Development in Our Cities

On behalf of Cork Chamber and the Southern Region, Construction Industry Federation

June 2021

Executive Summary

Cork Chamber and the Construction Industry Federation (CIF) have commissioned KPMG-Future Analytics to undertake research to identify solutions for issues around the viability of apartment development in Ireland. This report presents evidence-based recommendations for the Irish Government to consider in the tackling of these issues by alleviating the overall costs of new apartment construction and supporting the sustainable delivery of new apartment units.

- Ireland faces an acute housing crisis in which annual housing delivery is failing to meet national targets of 30,000 new units per annum.
- Ireland's housing sector has diversified in the last decade. In particular, the increasing importance of the Private Rental Sector (PRS) and recognition of Build-to-Rent (BTR) developments as viable options in a diversified housing market have seen an uptake in the delivery of new apartment developments in Ireland's urban centres.
- The sustainable delivery of new apartment developments is vital to meet both short-term and long-term demand and deliver objectives under the National Planning Framework for the compact spatial development and densification of Ireland's cities.
- Recent industry research and insights have highlighted an emergent issue around the viability and affordability of new apartment construction in Ireland's cities. Research commissioned by the Cork Chamber and CIF in 2019 found that the high cost of apartment delivery in Cork City resulted in a sales/rental price far above what an average buyer/renter would be able to afford.
- Similarly, research was published by the Society of Chartered Surveyors Ireland in January 2021 identifying viability and affordability issues for apartment delivery in Dublin City.
- Given these issues, the past decade has seen little private apartment development commenced or delivered outside of Dublin. This risks compromising national planning objectives for sustainable spatial development and the concentration of new residential development within the existing urban footprint of Cork City and Ireland's other major cities
- The failure to achieve adequate apartment delivery also risks compromising the economic performance of Cork and Ireland's other cities. Diverse and affordable housing options are essential to ensure that Cork City is internationally competitive in attracting new enterprise and employment opportunities.
- It is vital that the Irish Government takes swift and proactive action to tackle these issues and address the costs of new apartment delivery, in order to ensure the viable and sustainable delivery of new apartment units.
- The struggle to provide adequate new urban housing is not unique to Ireland. Across Europe, many governments and municipalities have risen to the challenge by taking proactive policy measures to support sustainable new housing delivery.
- As such, this report examines the housing sectors of three comparator cities in Europe – Brighton in the UK, Budapest in Hungary and Vienna in Austria – to identify those factors and interventions that have helped support viable new housing delivery, in particular new apartment development.

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Executive Summary

- **It is found that targeted tax interventions and competitive financing options produce clear and positive results in reducing overall costs and supporting new urban apartment development.**
- Based on this analysis, this report sets out five proposed recommendations to reduce the overall costs of new apartment development and help ensure that new apartment development in Ireland's urban centres remains viable and competitive. These recommendations are evidence-based and informed by the research set out in this report around the viability of apartment development in Cork City and factors identified in the chosen European comparator cities.
- The Irish Government is strongly urged to implement these recommendations in order to support the sustainable delivery of much needed new apartment units, address the demand for new housing and ensure the sustainable development of Ireland's cities. However a VAT reduction to 5% alone, without a combination of the other four suggested recommendations, will not address the current issues.

This report proposes the following five recommendations to support the viability and affordability of new apartment development in Ireland:

1. **Reduce the rate of VAT on residential construction activity to 5% for the period up to 2030.**
2. **Create an Urban Housing Investment Fund to invest in and secure the operation of new PRS and BTR developments.**
3. **Utilise the Urban Regeneration and Development Fund (URDF) to subsidise site enabling costs.**
4. **Provide a minimum tax depreciation of 4% per annum for apartment developments and explore accelerated capital allowances over 7 years for BTR and PRS that align to an environmental/social policy**
5. **Private investment in BTR/PRS to be recognised as businesses for gift / inheritance tax purposes.**

Contents

Chapter 1 - Introduction

The densification of new residential development within Ireland's urban centres is necessary to achieve long-term sustainable economic and community development and cater for our growing population for the next two decades. Published in 2018 the ***National Planning Framework*** (NPF) is a high-level strategy for Ireland's spatial growth and development up to 2040. It reflects lessons learned from the implementation of the previous National Spatial Strategy, and represents a shift from an uncoordinated *'business as usual'* approach to development, to the coordinated and orderly growth of Ireland's existing settlements to cater for projected **population growth of approximately 1 million people by 2040**. The NPF identifies *'Compact Growth'* as an essential **National Strategic Outcome** for Ireland and seeks to make better use of our infill and brownfield sites, as well as publicly owned lands and under-utilised derelict sites to provide higher densities of housing and employment in closer proximity to existing infrastructure and services in Ireland's five cities (Dublin City, Cork City, Limerick City, Galway City and Waterford City).

Population targets for Ireland's five cities as provided in the NPF are outlined in Table 1.1. As per National Policy Objectives 2a and 3b, the majority of this growing urban population is to be facilitated by the creation of new homes and jobs within the built up urban areas of Dublin, Cork, Limerick, Galway and Waterford.

At the last census (2016) the population of Cork City increased by 5.4%, mostly due to inward migration of persons in the household formation age range. It is vital that sufficient private accommodation is immediately available to cater for this recent population growth and for future growth targets under the NPF.

Table 1.1 Population Targets for Ireland's Five Cities **under the NPF** (Source: NPF, 2018)

City Location	2016 Population	Population Growth to 2040	Minimum Population Target 2040
Dublin – City and Suburbs	1,173,000	235,000 – 293,000	1,408,000
Cork – City and Suburbs	209,000	105,000 – 125,000	314,000
Limerick – City and Suburbs	94,000	47,000 – 56,000	141,000
Galway – City and Suburbs	80,000	40,000 – 48,000	120,000
Waterford – City and Suburbs	54,000	27,000 – 32,000	81,000

Source: The National Planning Framework (2018).

National Policy Objective 2a: *A target of half (50%) of future population and employment growth will be focused in the existing five cities and their suburbs.*

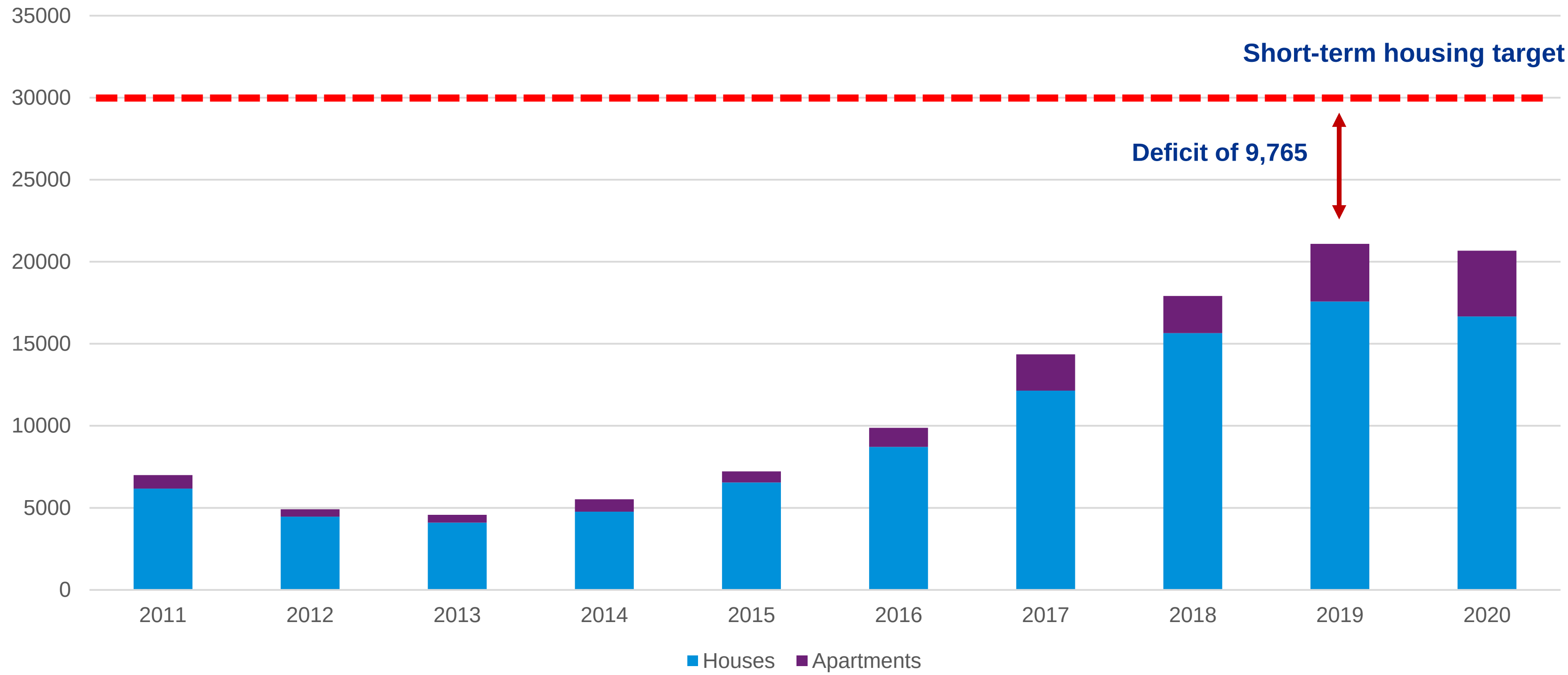
National Policy Objective 3b*: Deliver at least half (50%) of all new homes that are targeted in the five Cities and suburbs of Dublin, Cork, Limerick, Galway and Waterford, within their existing built-up footprints.*

(National Planning Framework, 2018)

Chapter 1 - Introduction

Recent rates of housing construction fall far below the output necessary to cater for Ireland's current future population. As shown below, though 2019 saw the highest number of new homes delivered in recent years (some 21,000), this is still almost 9,800 units short of the estimated short term need of approximately 30,000 units per annum.

Graph 1.1 Number of new Homes Delivered Per Annum



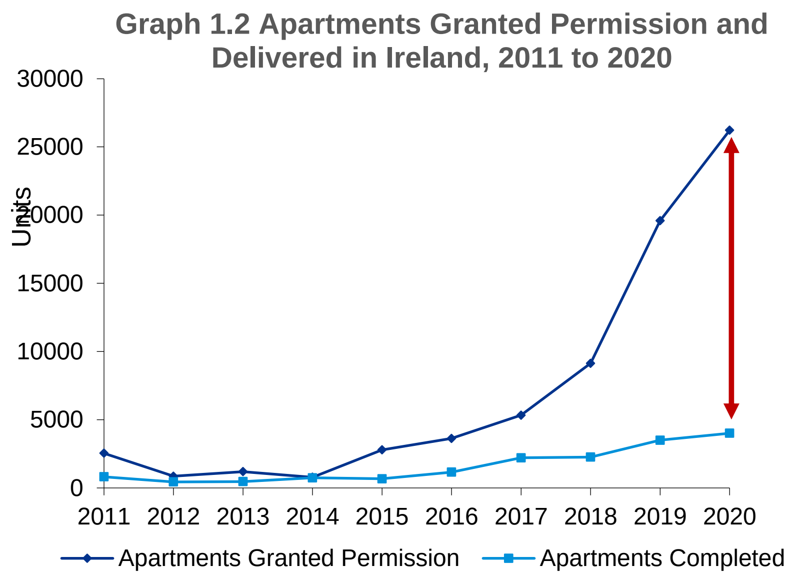
Source: on CSO Data NDA02 (last updated 04/02/2021)

Chapter 1 - Introduction

Apartment permissions granted accounted for just under 59% of the total residential planning permissions sought nationwide, outnumbering houses by some 26,200 to just over 18,300, respectively.

However, despite the growing presence of apartment units in the national planning pipeline, these planning permissions are not translating into commenced and completed units that are delivered to the market. As per Graph 1.2, a significant gap exists, and is widening, between the number of new apartments granted planning permission in recent years and those completed.

The simple case is that there are no private apartment developments of scale under construction or delivered outside of Dublin for the last 10 years at least, because it's simply not viable. Apartment construction and delivery should be viable for all sectors of housing and in all the major urban centres. The lack of viability for apartment construction is a significant threat to sustainable development initiatives in the NPF for 50% of population growth to take place in the existing urban footprint of our cities.



Source: CSO Data BHA05 (last updated 12/03/2021 and NDA02 (last updated 04/02/2021

Chapter 1 - Introduction

This report joins recent market research in reaffirming an issue in the viability of new apartment delivery, with reference to two case study examples of apartment developments at the Cork City Docklands. This report then offers realistic and concrete recommendations for action that the Irish Government can take to improve the viability and affordability for the delivery of new apartment units. These recommendations are informed by three comparator case studies, which examine how factors and measures taken in different cities across Europe have contributed to a healthy and sustainable level of new apartment delivery.

This report comprises the following sections:

- **Chapter 2: Cost Analysis –** Reference to two case study examples of apartment developments at the Cork City Docklands.
- **Chapter 3: International Comparison –** examines market factors and political measures that have supported sustainable housing delivery in three UK and European case study cities. These cities are:
  - Brighton, UK
  - Budapest, Hungary
  - Vienna, Austria
- **Chapter 4: Recommended Interventions –** sets out five recommendations for proactive policy measures that the Irish government is encouraged to implement to support the viability and affordability of new apartment delivery.

Chapter 2 - Cost Analysis

To exhibit the issue around the viability and affordability of new build apartments this report utilises details received from the CIF for two case study developments in Cork City. These developments are currently at the design stage and data relating to each development has been received in confidence. As such, the following case studies present a high-level overview of the costs and valuations of both schemes and omit sensitive information that may compromise the integrity of their future development.

Case study 1 presents the costs and valuation submitted by a developer for a **201 no. unit BTR development at Cork City Docklands**.

Case Study 2 presents the costs and valuations submitted for a **147 no. unit BTR development also situated at the Cork City Docklands**.

The following section of this report provides a breakdown of the overall costs estimated for the delivery of each proposed development, as well as a valuation of each development as submitted by CIF. It is exhibited that, based on the overall cost of delivery and valuation based on expected rents for the subject area that Case Study 1 exhibits a loss of 15% relative to its overall delivery costs and so is not considered viable. Similarly, Case Study 2 makes a loss of 18% relative to its cost of delivery and so is not considered viable. It should be noted that like all projects there are differences in location, height, car parking spaces, etc that effect the costs of development.

<u>More detailed analysis of costs can be found in the following reports:</u>

- *Viability and Affordability of Apartment Building in Cork City* (EY on behalf of Cork Chamber and CIF, 2019)
- *Dublin Residential Cost Benchmark* (Irish Institutional Property, 2020)
- *The Real Cost of New Apartment Delivery* (Society of Chartered Surveyors Ireland, 2021)

Table 2.1: Case Study 1 Details

Case Study 1	
Type of Scheme	BTR
No. of Units	201
No. of Part V Units	20
Car Parking Provision	69 spaces
Mixed-Use Element	Includes restaurant/bar and office space

Source: CIF, 2021.

Table 2.2: Case Study 2 Details

Case Study 2	
Type of scheme	BTR
Number of units	147
Part V	15
Car Parking	140 spaces

Source: CIF, 2021.

Chapter 2 - Cost Analysis

Case Study 1

Case Study 1 has a delivery cost of €106,584,772 and provides a net valuation of €90,152,960. This leads to a loss of -€16,431,812, equivalent to 15% of the overall cost of delivery. As such, the scheme is considered unviable, and the development would not be able to secure financing.

Table 2.3: Case Study 1 Profit Margin Assessment

Valuation	€90,152,960
Cost	€106,584,772
Profit / (Loss)	-€16,431,812
Profit Margin	-15%

Source: CIF Member, 2021.

Case Study 2

Case Study 2 has a delivery cost of €64,859,514 and provides a net valuation of €52,559,609. This leads to a loss of €20,083,047, equivalent to 28% of the overall cost of delivery. As such, the scheme is considered unviable, and the development would not be able to secure financing.

Table 2.4: Case Study 2 Profit Margin Assessment

Valuation	€52,559,609
Cost	€64,859,514
Profit / (Loss)	-€12,299,905
Profit Margin	-18%

Source: CIF Member, 2021.

Chapter 3 - International Comparison

The delivery of sustainable levels of new urban housing is a common issue across several European cities where, like Ireland, accelerated apartment delivery is considered vital to cater for growing urban populations. Chapter 3 examines three comparator cities located in the UK, Hungary and Austria to determine what sort of policy measures have been implemented to achieve sustainable levels of new apartment delivery.

Based on the preceding analysis in Chapter 2, as well as previous research on Ireland's construction sector it is clear that there is a real issue around the viability of new apartment delivery in Cork City and Ireland's other major urban centres, with the costs of delivery significantly outweighing the expected return for new developments. Ireland is not the only country currently contending with a need for accelerated apartment delivery.

Across many European cities there is a need for accelerated delivery of accommodation to cater for growing urban populations. Many cities are achieving success in supporting the delivery of new housing, specifically new apartment units, from the private sector.

Chapter 3 provides case study reviews of the housing markets for three such cities in order to identify market factors and policy measures that have proven successful in delivering new apartment development.

The chosen comparator cities are included below:

- **Brighton, UK – 0% VAT rate on new construction ensures viability of new apartment schemes;**
- **Budapest, Hungary – A temporary reduction in the rate of VAT applied to new construction has helped regenerate a stagnant housing construction sector; and**
- **Vienna, Austria – Low interest municipal loans for private developers provided by the city municipality have supported the delivery of new affordable apartment units.**

Chapter 3 - International Comparison

Brighton, UK

The UK provides a 0% VAT for the delivery of new residential units, including houses and apartments. This helps reduce the overall cost of new housing for developers and buyers. This is clearly exhibited with reference to a proposed residential apartment development at Ellen Street in Brighton that was granted planning permission in October 2020. A development appraisal summary submitted with the planning application set out the overall cost of the scheme with it's estimated net development value, indicating that the scheme would provide a profit of £8,014,292 (i.e. a yield of 15%). This is summarised in Table 3.1.

The provision of 0% VAT for new development ensures the viability of this scheme and it is highly likely that the proposed scheme would not be viable in Ireland. To illustrate this Table 3.2 applies a VAT rate of 13.5% to the overall delivery cost for the development. This VAT charge detracts from the overall value of the development such that it would only provide £693,237 in profit (a yield 1.28%), far below what would be considered acceptable by developers or commercial financers.

As such, it is considered that the current 13.5% VAT rate charged on new housing construction is prohibitive to the viability of new apartment delivery.

Table 3.1: Costs from Development Appraisal Summary for 216 no. unit development at Ellen Street, Brighton

Total Cost	**£54,230,039**
Gross Development Value	**£66,785,763**
Purchasers Costs	-£4,541,432
Net Development Value	**£62,244,331**
Profit	**£8,014,292**

Source: Watkin Jones Group, 2020.

Table 3.2: Application of 13.5% VAT rate for 216 no. unit BTR Development at Ellen Street, Brighton

Total Cost	**£54,230,039**
Gross Development Value	**£66,785,763**
Purchases Costs	£4,541,432
VAT at 13.5% on total cost	£7,321,055
Net Development Value	**£54,923,276**
Profit	**£693,237**

Source: Watkin Jones Group 2020 and KPMG Future Analytics, 2021

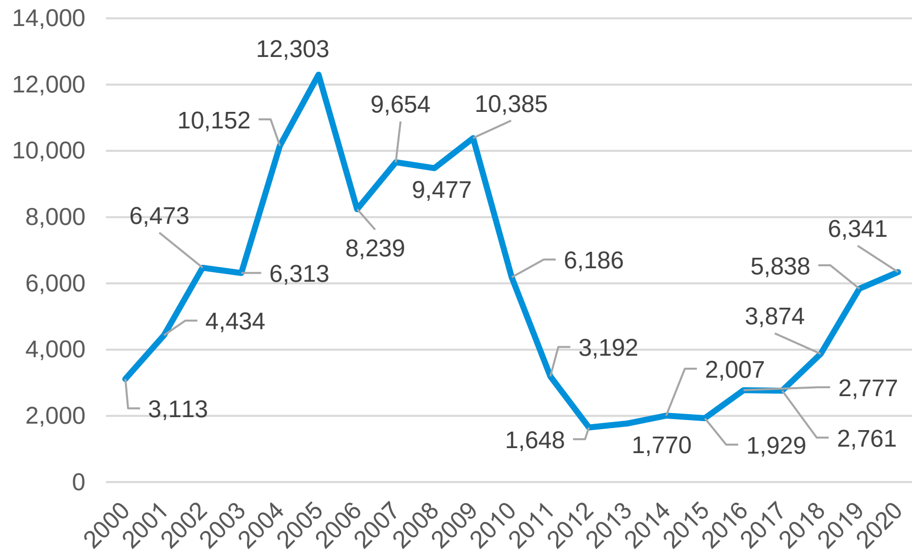
Chapter 3 - International Comparison

Budapest, Hungary

In a bid to combat acute sluggishness in housing delivery caused by labour shortages and economic recession, in 2015 the Hungarian government announced new regulations for the tax treatment of new home construction, reducing the rate of VAT applied to the supply of new housing from the standard national rate of 27% down to 5%. Under this measure residential buildings that received planning permission by the end of 2018 could be sold at this reduced VAT rate of 5%. It was also required that eligible units be sold by the end of 2023 in order to avail of this reduced VAT rate, in order to prevent speculation and encourage short term activity.

This reduced VAT rate has had a clear impact on the delivery of new housing units in the city of Budapest, with the number of new units delivered per annum rising from 1,929 in 2015 to 6,341 in 2020 (see Graph 3.2).

Graph 3.2: Housing Completions in Budapest



Source: Hungarian Central Statistics Office, 2021.

Vienna, Austria

First introduced in 2011 and extended in 2015, the Wohnbauinitiative (WBI) is a subsidy scheme that provides medium-term, low-interest loans and low cost building land to support new housing construction. Explicitly aimed at private developers, the WBI is intended to support the delivery of new middle-range apartment units at rents that are affordable for residents that do not qualify for social housing support but find themselves under pressure at market rental rates.

Under the WBI the City of Vienna provides bullet loans to developers to finance new housing construction, at a rate of €800 per sq.m of usable floor space. A bullet loan is one that defers the majority of payment until the maturity of the loan term, with payment on the loan value and interest accrued generally paid in a lump sum at the end of the loan period. As such, it offers greater financial flexibility for the borrower.

Initially lent at an interest rate of 3.9% for ten years, this interest rate was reduced to 2.5% in 2015. By providing low-interest loans for which payment can be deferred until the end of the loan term, the WBI provides a cheap financing option for developers. Also as part of the WBI, the City of Vienna can provide urban building plots at a below-market rate to developers. These plots are typically ancillary in nature and are outside of the major public land holdings intended for social housing construction. By providing them to developers at reduced rates, the intention is to ensure that they are brought into productive use.

In exchange for these subsidies developers are required to provide their own equity at a minimum rate of €350 per sq.m of usable floor space. 50% of the completed units are to be allocated by the City of Vienna to residents that have previously applied for subsidised housing provision.

Further, during the term of the loan repayment, rents for the proposed development are to be agreed at an affordable rate. The implementation of the WBI has been considered successful, with 6,300 new units delivered under it's first call and a further estimated 1,800 units to be delivered under it's current iteration (Mudnt and Amann, 2018).

The impact of the WBI on the cost of new apartment delivery is estimated in ***Affordable Housing Governance and Finance*** (2018) based on interviews conducted by the authors and construction industry actors. This estimated impact is exhibited in Table 3.3, which includes the building and finance costs of an example WBI projected compared to a project purely financed by the private market. It was found that the build costs and financing costs for a typical WBI project was lower than that of a purely private development, which had to pay the market-rate for the development site and turn to commercial loans with higher interest rates for financing.

Table 3.3: Comparison of Costs for WBI Project and Market Financed Project

	Example WBI Project	Example Market Financed Project
Building plot (including site works)	350	900
Construction costs	1,750	2,300
Overall Costs	2,100	3,200
Own equity developer	350	900
WBI loan	800	0
Tenants' capital contribution	400	500
Other loans (banks	550	1,800
Overall finance	2100	3,200

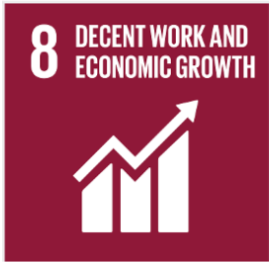
Source: "Wiener Wohnbauinitiative": a new financing vehicle for affordable housing in Vienna, Austria. From: *Affordable Housing Governance and Finance* by Alexis Mundt and Wolfgang Amann, 2018.

Chapter 4 - Recommended Interventions

As set out in Chapter 3 various factors and measures have contributed to the ability of other cities in the UK, Hungary and Austria to achieve a healthy and functioning housing market that is able to ensure viable and sustainable apartment delivery. Given the exhibited issue around the viability of apartment delivery in Ireland and the failure of the market to deliver on national housing targets, swift and affirmative action is required at policy level to improve the viability and delivery of apartments within our urban centres. Chapter 4 sets out five key recommendations, informed by the preceding cost analysis and comparator studies of European cities, to improve the viability of apartment development in Ireland and help ensure that Ireland is able to meet its short and long term targets for new housing delivery.

The NPF places an overarching focus on the sustainable and compact growth of Ireland's cities, calling for the majority of new housing to be delivered within the existing built-up area of our urban centres. In doing so the NPF aligns with wider principles of sustainability as established under the **UN's 17 Sustainable Development Goals (SDGs)**. Of particular relevance are Goal 8 and Goal 11, which seek to achieve economic and employment growth and the creation of sustainable cities, respectively.

The following five recommendations aim to advance the sustainable development of Ireland's cities, as provided for under the NPF and the UN's SDGs. Informed by the housing and economic context both at home and abroad, they aim to help secure the viability of new apartment development in Ireland to accelerate delivery and help achieve national housing targets of 30,000 new homes per annum. Their implementation is considered vital to help address Ireland's current housing shortage and to support the wider regeneration and sustainable development of Ireland's five cities. As such, the Irish Government is urged to consider the following recommendations and provide for their swift implementation, taking into account that **a VAT reduction to 5% alone, without a combination of the other four suggested recommendations, will not address the current issues**.



This report proposes the following five recommendations to support the viability and affordability of new apartment development in Ireland:

1. **Reduce the rate of VAT on residential construction activity to 5% for the period up to 2030.**
2. **Create an Urban Housing Investment Fund to invest in and secure the operation of new PRS and BTR developments.**
3. **Utilise the Urban Regeneration and Development Fund (URDF) to subsidise site enabling costs.**
4. **Provide a minimum tax depreciation of 4% per annum for apartment developments and explore accelerated capital allowances over 7 years for BTR and PRS that align to a environmental/social policy**
5. **Private investment in BTR/PRS to be recognised as businesses for gift / inheritance tax purposes.**

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Chapter 4 - Recommended Interventions

Recommendation 1: Reduce the rate of VAT on residential construction activity to 5% for the period up to 2030

Construction activity in Ireland is currently subject to a VAT rate of 13.5%. There is potential for a reduced VAT rate on residential construction activity to help reduce the cost of construction and support the delivery of new apartments. In November 2020, the Irish government applied a timed reduction to the VAT rate for the hospitality sector, with the rate of VAT applied to associated goods and services reduced to 9% for the period up to December 2021 in order to support this sector in surviving and recovering from the impact of the COVID-19 crisis. Given the impact of COVID-19 on Ireland's construction sector, with activity subject to various suspensions throughout 2020 and 2021, it is argued that similar affirmative action must be taken in order to help support the construction sector's recovery and encourage new residential development to help meet national housing targets of 30,000 units per annum.

It is understood that compliance with the European VAT Directive (European Council Directive 2006/112/EC) entails some constraints on possible reductions in VAT rates for Member States. Member States must apply a standard VAT rate at no lower than 15% and may apply two reduced rates of between 5% and 15% to certain goods and services. Currently the standard rate of VAT in Ireland is 23%, with construction activity availing of a reduced rate of 13.5%. As above, a second reduced rate of 9% has been applied to help boost activity in the hospitality sector.

Ideally, a 0% rate on residential construction would be preferable, however, we acknowledge that current EU VAT rules make such a recommendation non viable. **At a minimum, it is suggested that the second reduced VAT rate is further reduced to 5% and extended to residential construction activity in order to help alleviate the impact of COVID-19 on the residential construction sector and help support new residential construction and delivery**.

Based on the case study examples examined in Chapter 3, reducing the VAT rate on construction will help ease the cost of new apartment delivery at both supply side and purchaser side and will help developers implement planning permissions for developments that have yet to commence.

As noted in Chapter 3, Hungary took the ambitious measure of reducing the VAT rate on new residential construction to 5%. In Portugal a reduced VAT rate of 6% is applied for the construction of new social and affordable housing, which is consistent with allowances under the VAT Directive for additional VAT reductions as a means to achieve broader social policies. As such, a VAT rate as low as 5% may ultimately be permitted if part of a broader political effort to leverage the private construction sector to deliver new social and affordable housing.

Therefore, a further reduction of the second reduced VAT rate to 5% and extended to Ireland's residential construction sector will help support recovery from the impacts of COVID-19 and support the delivery of much-needed new apartments. Though of benefit to the sector as a whole, this measure will have a concrete impact on new apartment development in Ireland, **helping to reduce overall costs and improve the viability and affordability of new residential units**.

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Chapter 4 - Recommended Interventions

Recommendation 2: Create an Urban Housing Investment Fund to invest in and secure the operation of new PRS and BTR developments

As the case study examples in Chapter 2 show, the expected return for new PRS and BTR developments is not necessarily enough to ensure their commercial viability. Furthermore, with recent Government efforts to curb the ability of institutional investors to purchase large swathes of housing from new developments by way of increased stamp duty rates, there is a need in the current economic climate to ensure that there are suitable long-term investors that will take over the operation and management of new PRS apartment developments. It is suggested that there is scope for the Irish state to play a role by becoming a primary investor in a dedicated fund/platform whose remit is to invest in new BTR and PRS developments in urban areas that meet specific environmental credentials. This fund could also attract other institutional investment and be professionally manged by an experienced asset manager.

A dedicated State-backed Urban Housing Investment Fund can step in as a long-term buyer and investor for new PRS and BTR developments. Such a fund, with a view to securing long-term returns, can bear the likely yields estimated to arise from such developments given Ireland's current economic context. In doing so, it will help ensure the viability of new apartment developments and secure the delivery of new apartment units at a rate required to meet current housing targets. This State-backed fund would occupy a similar role to that of large institutional housing investors that are present in many European countries but are not active in the Irish market.

For instance, Vonovia is a German residential landlord that is active in German, Sweden and Austria. In Berlin alone Vonovia owns and lets 43,000 apartment units, with this number expected to increased to 150,000 subject to the acquisition of the rival Deutsche Wohnen organisation, which is currently under negotiation. With a focus on long-term profitability and market sustainability, Vonovia are able to control their rental costs to reflect market conditions. In May 2021 Vonovia indicated that they will limit rent increases for their units up to 2026, capping rent increases at 1% up to 2024 and adjusting increases beyond up to 2026 to reflect inflation. A State-based Urban Housing Investment Fund could occupy a similar position in the market, ensuring that new apartments are managed and rented at a viable and affordable price.

In occupying such a role, an **Urban Housing Investment Fund provides the opportunity for the State to help influence the provision of rental accommodation at affordable and sustainable rates and provide security for tenants**.

Such efforts would also be consistent with and further support the emergence of cost rental housing as a viable form of housing tenure in Ireland. Under a cost rental housing model, tenants pay rent that covers the cost of delivering, managing and maintaining a home only. Under the 2021 Budget, €35 million has been made available to Approved Housing Bodies (AHBs) to deliver approximately 350 cost rental homes in 2021. These cost rental homes are to be rented at rates which are a minimum of 25% below open market values, and are aimed at providing secure and stable housing for middle-income households that are facing financial pressure under current housing market conditions. **By taking a role in the ownership and management of new PRS apartment developments there is potential to support the wider roll-out of the cost rental housing model in the future and help provide security and sustainability in Ireland's housing market.**

Chapter 4 - Recommended Interventions

Recommendation 3: Utilise the URDF to subsidise site enabling costs

The support of urban regeneration projects are welcome and indeed are vital to achieve objectives under the NPF and wider sustainable development goals. However, to achieve national objectives under the NPF around compact urban growth and urban residential development, there is a need for specific support to be given to the provision of new urban apartments. **It is suggested that further funding under the Urban Regeneration and Development Fund (URDF) be ringfenced to help subsidise site enabling costs for new apartment delivery in our urban centres.**

The subsidisation of site enabling costs for urban apartments can be modelled on the current Site Services Fund which serves as a precedent. The Site Services Fund is a state subsidy that supports the construction of public affordable and cost rental homes. It supports the provision of key enabling infrastructure on local authority land to unlock the potential for new housing by subsidizing up to €50,000 for the cost of new homes through enabling works.

This approach to unlocking new housing opportunities should be extended beyond publicly-owned lands to help unlock further opportunities for the provision of much needed housing in Ireland's five cities. It will help deliver new housing units to the market for purchasers and tenants and, in the context of the Affordable Housing Bill 2021 approved by Cabinet in May 2021, will support the delivery of new social and affordable housing. Currently under Part V of the Planning and Development Act 2000, in residential developments of ten or more units 10% of units are to be reserved for social housing provision. However, the Affordable Housing Bill 2021 includes a provision for the extension of Part V requirements to a minimum 20% for social and affordable housing provision. Under this new provision the subsidisation of site enabling works for urban housing would help deliver new housing types to cater for purchasers and tenants of all needs.

An appropriate rate of subsidisation for site enabling costs for eligible developments can be agreed based on locational and site-specific factors and constraints. For instance, in January 2021 Dublin City Council indicated that the standard allowance of €50,000 per unit available under the Site Services Fund was not enough to make a requisite impact given the higher construction costs associated with building new housing in Dublin. As such, it is considered that the provision of future subsidies for site enabling costs must be evidence-based and properly reflect the real cost of apartment construction in Ireland's cities.

Chapter 4 - Recommended Interventions

Recommendation 4: Provide tax depreciation of 4% per annum for apartment developments

Tax deprecation allows for a taxpaying enterprise to write off capital expenditure on certain costs against its annual profits, thus reducing the amount of tax paid. It results in the taxable profits of the enterprise being more closely aligned to accounting profits. Claims for tax deprecation are generally referred to as capital allowances. By allowing for capital allowances against certain expenditures an enterprise is essentially able to write-off the cost of an asset over an extended period of time.

In Ireland, enterprises can currently claim capital allowance against plant and machinery that will be used as part of a commercial business. The permitted rate of capital allowance is 12.5% of the expenditure cost, over a period of 8 years. Ireland also permits Industrial Buildings Allowances (IBAs) of 4% to be claimed against qualifying construction expenditure incurred on the provision of industrial buildings (i.e. factories and mills). Accelerated capital allowances of 15% over 6 years and 10% in year 7 were introduced in 2019 in respect of qualifying capital expenditure on childcare and fitness centre facilities provided by employers. However, there are no similar allowances provided for the costs of constructing or acquiring new housing or apartment developments which are used in PRS/BTR businesses. Tax depreciation of a building, provided over a reasonable period of time and/or as part of social policy, should not fall foul of State Aid rules. Moreover, during the Covid pandemic a Temporary Framework was introduced to ensure State supports did not breach State Aid rules.

We recommend that the Irish Government should explore with EU partners whether additional measures can be introduced to allow for certain more expansive incentives to encourage investment in capital projects including for example PRS/BTR investments.

Internationally, Germany provides for an annual straight line depreciation rate of 2% for buildings used for accommodation purposes. For newly constructed rented property, based on building permissions granted between 1 September 2019 and 31 December 2021, a temporary additional depreciation of up to 5% of the acquisition or construction cost is available in addition to the regular straight-line depreciation, as a means to boost the delivery of new apartment developments. The additional depreciation is only available if the acquisition or construction cost does not exceed €3,000 per sq.m and the rental property is rented out in the year of acquisition/construction and for the subsequent 9 years. Similarly in Hungary a depreciation rate of 5% is permitted for rented property and Greece provides a depreciation rate of 4% for all office and residential buildings

Permitting a tax depreciation deduction for the cost of construction of PRS and BTR developments is recommended. A rate akin to that of the IBAs i.e. 4% per annum, would be considered competitive and in line with European standards. Indeed an accelerated capital allowance regime over 7 years for BTR and PRS schemes that aligns with social and environmental objectives warrants strong consideration. The introduction of such a measure would allow Ireland to compete equally with other European locations for investment in PRS and BTR apartment developments. The availability of such depreciation should encourage domestic and international investment by offering investors a tax deduction for their investment in qualifying properties over an extended period of time and will provide greater certainty to investors that the profits on which they pay tax is aligned to the profits actually realised. This increased certainty should lead to the improved viability of new apartment developments.

Chapter 4 - Recommended Interventions

Recommendation 5: Private investment in BTR/PRS to be recognised as business asset for gift / inheritance tax purposes

Nationwide there is a weak supply of suitable rental accommodation. The private residential market in Ireland has been dominated for many decades by landlords, the majority of whom own one or two properties. Per the 2019 Department of Finance paper titled *Institutional Investment in the Housing Market* 70% of landlords (121,481) registered a single rental property. In more recent times increased regulation (often introduced to properly protect the rights of tenants) and taxes have led to a decline in the numbers of "one property" landlords. In more recent times we have also seen investment from funds in certain PRS and BTR schemes. However, this investment has been targeted almost exclusively in the Dublin marketplace. Investment in PRS and BTR schemes has not yet extended to the regions and this need to change Moreover there is a lack of Irish sourced investment capital to support such developments.

The above mentioned Department of Finance paper also notes that managed PRS and BTR schemes have a major advantage in that they can provide professionally managed housing, often with newer stock. Expanding the BTR sector is a specific objective of the Government's *Rebuilding Ireland: An Action Plan for Housing and Homelessness.*

In order to support and achieve these policy objectives it is recommended that targeted tax measures are introduced to encourage participation in such schemes by individual Irish investors.

These tax measures should do no more than recognise the reality that PRS and BTR schemes are active businesses which require professional management and active oversight.

We would recommend an extension of Business Property Relief for gift and inheritance tax purposes to include qualifying BTR and PRS schemes.

This measure can encourage private long term investment into the construction of PRS and BTR developments. It would support such developments source funding from private Irish individuals (or a collective of private individuals) who would agree to invest in BTR/PRS schemes with an objective to hold same for a longer term period.

Summary of International Measures to Aid Apartment Delivery and Affordability

The preceding recommendations are informed by international measures that have been implemented by cities across Europe to aid the viability of new apartment and housing delivery. The below summarises the measures previously detailed in Chapter 3, as well as a number of additional measures employed in other European cities.

- The construction industry in the city of Brighton benefits from the UK's competitive 0% VAT rate on the delivery of new housing, which helps reduce overall costs for developers and purchasers/tenants and helps ensure that new development achieves a viable level of return.
- In the city of Budapest in Hungary the timed reduction of the VAT rate for new housing delivery from 27% to 5% helped revitalise a housing market, incentivising developers to commence and deliver new units in a timely fashion in order to benefit from the reduced rate.
- The city of Vienna in Austria made competitive low-interest loans and affordable land available to developers to help reduce overall development costs and ensure the viability of affordable new apartment units that could be viably let at below-market rates.
- Uppsala in Sweden employ a competitive tendering process for the development of public lands in order to stimulate development and help address specific gaps in the housing market. The Municipality specifies the desired quantum of residential development for a site and developers then compete for the right to deliver the proposed development, with the successful developer granted two years to deliver the proposed development to ensure commencement. Throughout the tendering process developers are encouraged to provide innovative design and construction solutions in order to reduce costs and improve the amenity of the final development.
- Germany allows for an annual straight line depreciation rate of 2% for buildings used for accommodation purposes. Further, for newly constructed rented property, based on building permissions granted between 1 September 2019 and 31 December 2021, a temporary additional depreciation of up to 5% of the acquisition or construction cost is available.
- In Luxembourg the State provides financial support accessible to municipal authorities and private developers to subsidise the construction cost of new affordable housing units. These subsidies are administered by the Ministry of Housing and assist with costs associated with site acquisition and the planning and construction of new dwellings. Subsidies can range from 50% to 100% of the overall costs for individual projects, and in return subsidised dwellings must be sold or rented at below-market rates.
- In Iceland the Housing Financing Fund (HFF) is an independent government institution that provides and manages loans with the aim of supporting sustainable housing delivery and housing security. The HFF provides mortgages to individual homebuyers, as well as public and private developers to support the construction of new housing units. Dwellings built with the support of the fund are subject to maximum price limits in order to ensure affordability.

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