

[4.8.8] Order of set-off between Case V capital allowances and Case V losses brought forward¹

Reviewed – July 2016

1. Introduction

Current year Case V capital allowances are set-off against current year Case V income in priority to Case V losses brought forward from a prior year. This can be less beneficial for the taxpayer because current year Case V capital allowances are set (firstly) against current year Case V income thus reducing the amount of Case V income available to absorb Case V losses brought forward. Unlike current year capital allowances such losses can only be set against Case V income.

2. Interaction of Case V capital allowances and losses

The order of set off of Case V losses and capital allowances is as follows:

1. Case V surpluses and deficiencies for the year are aggregated in arriving at the Case V profits or gains for the year of assessment
2. Capital allowances are then allowed in charging the income to tax. The amount after capital allowances is the amount assessed. The capital allowances include capital allowances brought forward from an earlier period. Capital allowances brought forward are treated as set off in precedence to capital allowances of the year of assessment.
3. Losses (deficiencies) brought forward from an earlier period are set off against the amount on which the person is assessed

3. Analysis of relevant TCA legislation

While there is no express provision in the Tax Acts setting out the priority to be given, the intended order of set off is clear from a combined examination of sections 97, 384 and 305 TCA 1997.

Section 97 is the basic Case V computation section. It is concerned with computing the profits or gains for a **particular** year (in subsection (1) “arising in any year”) and with allocating income and expenses to individual properties. The end result is that the aggregate of the surpluses for each rent is reduced by the aggregate of the deficiencies. The section is very specific in the deductions that it authorises and makes no reference to a deduction for capital allowances or for Case V losses brought forward and does not imply any sequence of deduction for these items.

¹ This issue was originally dealt with in Tax Memo 10/2003.

Section 384 provides for the carry forward of Case V losses where the aggregate of the surpluses for prior years has been exceeded by the aggregate of the deficiencies. Subsection (2) states that the losses being brought forward are to be set off against “the amount of profits or gains on which the person chargeable is **assessed** under Case V....”. Subsection (3) states that the loss should be set off against the “**assessment**” for the first subsequent year of assessment...”.

Section 305 details how Case V capital allowances are to be used when they are made in “**charging income** under Case V...” (as provided for in section 278). The ‘charging’ of a person’s income is the bringing of that income into account under Case V and the allowances are made when the income is being brought into account. Current year capital allowances are set firstly against current year Case V income and only if there is a surplus at that stage can it be set sideways against other income of the claimant and that of the claimant’s jointly-assessed spouse/civil partner.²

Sequence of events

The Case V profits or gains for a particular year are computed in accordance with section 97. The only deductions allowed in the computation are those specified in subsection (2).

By definition, capital allowances are allowances other than allowances or deductions to be made in computing income (section 2). They are, therefore, deducted from income as computed in accordance with section 97. Again, as in section 97, the focus is on a particular year – capital allowances are to be given “for any year of assessment....(and) the amount of the allowance shall be deducted from or set off against the person’s incomefor that year of assessment”. The year in question is the same one for which profits or gains have been computed in accordance with section 97.

Section 384 losses are not deductions to be made in computing section 97 profits or gains. Furthermore, they are not deductions that relate to the particular year in respect of which profits or gains are being calculated – they relate to a prior year and can only be brought into the reckoning after all deductions for the current year have first been allowed. As provided in section 384(2), they can only be deducted from or set off against the profits or gains on which a “chargeable person is assessed for any subsequent year of assessment”.

Income has to be charged, i.e. brought into account before it can be assessed to tax. Capital allowances are made in charging income under Case V. Charged income is therefore income after capital allowances have been deducted and before the income is assessed and taxed. The current year capital allowances

² In most case this sideways setoff is restricted to an annual ceiling of €31,750 (section 409A) and is subject to a 2-year election in writing. There is no sideways setoff for plant and machinery excess capital allowances as these are ringfenced to Case V income.

are therefore to be made in charging income for that year. Section 305(b)(i) specifically provides for the set off of capital allowances brought forward³ before the excess capital allowances are set off against other non-case V income for the year. It is only at that stage that the remaining Case V income is assessable and Case V losses brought forward can be deducted.

In summary, section 384 losses are not deductions that can be made in computing income or profits. Section 384 allows for a Case V loss to be brought forward to any “**subsequent year of assessment**”. Sections 97 and 305 provide for deductions in a particular/current year of assessment and therefore take precedence over deductions for items that are to be brought forward from a prior year. The losses brought forward are to be set off against the profits or gains on which the person chargeable **is assessed** under Case V. A person is assessed after the capital allowances have been given in **charging income** for a particular year.

4. Restrictions of tax relief for high income individuals

Provisions introduced in Finance Acts 2006 and 2007 (now Chapter 2A, Part 15 TCA 1997) limit the amount of “specified reliefs” that a high worth individual can use to reduce his or her tax liability in any single year. Tax Instruction [15.2A.1](#) deals with this issue. Capital allowances in respect of the various sectoral and area-based tax incentive schemes are included in the “specified reliefs” to be restricted.

Section 485C(3) TCA 1997 specifies the order in which Case V capital allowances are to be set off with effect from 2007 onwards. This order applies whether or not an individual is subject to the restriction. Relief is to be given in a particular year in respect of capital allowances that are not part of the restricted reliefs in priority to capital allowances that are restricted reliefs. The same principle applies to allowances brought forward that are attributable to both restricted and unrestricted allowances.

5. PRSI

A deduction against Case V income is allowed for capital allowances, but not Case V losses forward, in computing “reckonable income” for the purposes of PRSI and levies.

6. Some Examples

Example 1:	€
Case V profits or gains of year	4,000

³ Capital allowances brought forward always retain their identity as capital allowances and are not aggregated with losses brought forward. However, they are not aggregated with current year capital allowances and allowed to be set sideways against other income.

Case V Deficiencies brought forward	3,000
Case V Capital allowances of year of assessment	1,000
Case V Capital allowances brought forward	500

Losses and capital allowances will be set off as follows:

Case V profits or gains of year	4,000
Capital allowances	<u>1,500</u>
Income assessed under Case V	2,500
Case V Deficiencies brought forward	<u>2,500</u>
Net income assessed under Case V	Nil
Case V deficiencies carried forward	500

Example 2:

Case V Profits or gains of year	8,000
Capital allowances brought forward	1,000
Capital allowances of year	20,000
Case V Deficiencies brought forward	1,000

Losses and capital allowances will be set off as follows:

Case V profits or gains of year	8,000
Capital allowances brought forward	1,000
Capital allowances of year	<u>7,000</u>
Income assessed Case V for year	Nil
Case V deficiencies carried forward	1,000
Case V capital allowances available for set off against other income of year	13,000 (20,000 - 7,000)