The Consultative Committee of Accountancy Bodies-Ireland

Chartered Accountants Ireland
The Association of Chartered Certified Accountants
The Chartered Institute of Management Accountants
The Institute of Certified Public Accountants in Ireland

47/49 Pearse Street, Dublin 2

Minister Michael Noonan TD
Department of Finance
Government Buildings
Upper Merrion Street
Dublin 2

19 August 2011

Re: CCAB-I Pre Budget Submission 2012

Dear Minister

We enclose for your consideration our Pre Budget Submission.

We would be happy to discuss with you in further detail our recommendations for Budget 2012.

Yours sincerely

Liam Lynch
Chairman, CCAB-I Tax Committee

Pre Budget Submission 2012

Fairness in achieving tax yields

&

Certainty in tax policy

About CCAB-I

The Consultative Committee of Accountancy Bodies – Ireland is the representative committee for the main accountancy bodies in Ireland. It comprises Chartered Accountants Ireland, the Association of Chartered Certified Accountants, the Institute of Certified Public Accountants in Ireland, and the Chartered Institute of Management Accountants.

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Headline Items

Ireland has done well in protecting the 12.5% corporation tax rate through the current crises. However, some of the concentration on this has diverted attention from the fact that in other areas there is no certainty available to either existing taxpayers or to international investors. This is diverting investment from Ireland and is being used by competitor jurisdictions to harm our reputation in the eyes of such investors. One example is another jurisdiction using the ridiculous line that the 0.6% pension levy might be extended to international funds located in Ireland and thus persuading them to set up in their, apparently, safer jurisdiction. Another is the retrospective withdrawal of property reliefs – investment decisions are made on the facts that exist at the time and if a country gains a reputation for changing the law so that it would affect an investment decision already made, then investment will be at stake.

Ireland needs a clear policy and Ireland needs certainty as to what that policy is. Areas of uncertainty, whether in tax or other areas of Government policy, must be removed as soon as they are noticed. This is a very difficult time for both the Irish and the world economies, but striving for certainty in tax policy will pay dividends even in the short term.

CCAB-I, in this submission, recommends:

Pensions

The 0.6% pension levy is a levy on accumulated pension savings in the private sector. It would be better to temporarily suspend in part the exemptions from Corporation tax and capital gains tax on pension fund earnings. In the interests of equity, the public sector pension related deductions should be increased by a notional amount so that the burden of the pension levy is shared.

Pension policy in Ireland is in tatters – essentially there is no policy. This needs to be remedied.

Employment and Investment scheme

Investments made through the new employment and investment scheme should be removed from the list of specified reliefs for the high earners restriction. The EIS should be biased towards start-up ventures by allowing full tax relief where the investment is made in a start-up company.

Capital Tax Reliefs

While noting proposals in the four-year National Recovery Plan to curtail capital tax reliefs, it must be recognised that tax efficient transfer of a business from one generation to the next is essential to economic development. In addition, we suggest a form of rollover relief on gains accruing from business transfers provided that the disposal proceeds are invested in government bonds.

Attracting decision makers to Ireland

We can propose a form of impacted relief as an enhancement to the limited remittance basis which is not meeting its objectives. On a related issue, we propose a reordering of the charge to tax to reward innovation carried out in this country.

Stamp duties

The rate of stamp duty on commercial premises of 6% should be temporarily reduced to stimulate transactions in this market.

Introduction

The National Recovery Plan is based on growth of 2.75% over on average over the 2011 to 2014 period. The Plan will fail if this growth level is not achieved.

Tax Landscape

For the National Recovery plan arithmetic to work, the yield from income tax is essential. We see no prospect of asset values increasing in the short to medium term to an extent which will result in appreciable increases in the yields from the capital taxes – capital gains tax, capital acquisitions tax and stamp duty.

Corporation tax policy has been solid, in that every effort has been made to secure the continuance of the 12.5% rate of corporation tax. We point to developments in the United Kingdom – a promised reduction in the general corporation tax rate from 28% down to 23%, and extensive consultation taking place on a mechanism to allow a lower rate of Corporation tax to prevail in Northern Ireland – as being signal indicators of the importance of a low Corporation tax rate as an economic stimulus.

Linked with income tax yields are value added tax yields.

There are three main contributors to the value added tax yield; the exempt activities sector (banking and associated services), the public sector and the consumer sector. Tax receipts from the banking sector can be expected to remain flat for some considerable time. Likewise, with a reduction in the Exchequer spending, the public sector as an important driver of value-added tax receipts is absent from the economy. Consumer sentiment remains soft.

A very important aspect of the consumer VAT yield stemmed from the construction sector. The construction sector has recently entered its fifth year of contraction. Even if there were to be an immediate recovery, the stock of second-hand houses is such that the VAT yield applicable from the construction sector is not likely to improve in the short to medium term.

Primacy of Income Tax

There remain however risks associated with the overreliance on income tax as being the key driver of tax receipts.

We made the mistake in earlier years of becoming over reliant on one particular sector, the construction industry, to drive tax revenues. These revenues were paid in the form of capital gains tax, stamp duties, corporation tax and value added tax. This overreliance resulted in very serious consequences following the collapse of that sector.

We risk making exactly the same mistake if we are too over reliant on individual taxpayers to shoulder an excessive part of the overall tax burden for the country. Furthermore, within the grouping of income tax payers is the high earners grouping. It remains the case that a disproportionately low percentage of individual taxpayers pay the bulk of the income tax receipts. While the universal social charge has gone some way to redistributing the overall income tax burden, in our analysis, it remains the case that a mere 15% to 18% of income earners account for 75% of all income tax collected. This is simply not sustainable.

The view of accountants who are currently preparing accounts and returns of income for preliminary tax for the 2011 tax year is that the yield from the self-employed is likely to be lower than in previous years.

For professional people, charge out rates and recovery rates have reduced across the board. Some professions, which in the past have made significant contributions to income tax yield because of the higher earnings they enjoyed, are now almost non-existent. Professionals reliant on earnings from the construction sector – surveyors, architects, civil engineers, solicitors and auctioneers - their earnings have been particularly hard-hit.

Therefore any fiscal strategy for 2012 and subsequent years which has an overreliance on additional income tax yields from high earning self-employed and PAYE taxpayers will not succeed.

Preliminary Tax Issues

We understand that preliminary tax is a necessary part of a modern tax system. However, if the payment date for preliminary tax occurs too early in the accounting period to which it relates, this causes problems not just for the individual taxpayer but also for the Exchequer.

In these recessionary times, profits in most businesses are decreasing. Seasonal businesses, retailers in particular, are increasingly dependent on income at year’s end. The indications

from accountants in practice is that preliminary tax for 2011 will have to be funded to a larger extent than ever before from borrowings.

We feel that at a time when all businesses are struggling to obtain both working capital and borrowings for longer term investment, it is counterproductive to impose tax funding requirement to satisfy imputed liabilities on unrealised profits.

In the light of this, it is essential that there are no moves (as had been proposed last year) to bring forward preliminary tax payment dates. We also recommend that preliminary tax obligations be satisfied for 2011 by the payment of 90% of the 2010 liability, rather than 100% as is currently the case.

Income Tax Rates

CCAB-I has noted recent statements by the Taoiseach that income tax rates would not increase. However, equally we are aware that this could be code for suggesting that income tax reliefs could be further reduced.

The Four Year National Recovery plan includes a further 2.5% cut in the value of tax credits, along with further curtailment of pensions tax relief in 2012. In 2011, we will see the first full impact of the changes to the High Earners Restriction which now ensure a minimum effective rate of 30% for those on incomes earning in excess of €125,000. This may seem to be a generous threshold but the reliefs which the High Earners Restriction curtail were necessary in very many cases for the funding of the expenditure creating the entitlement to tax reliefs in the first instance.

It is a reality of Irish economic life that there is now little difference between paying the Revenue Commissioners and paying one of our many State-owned banks. The High Earners Restriction forces many taxpayers to pay one or the other, without being able to afford to pay both.

Jobs Initiative

The Jobs Initiative announced in May of this year was significant not least for its recognition that tax relieving measures had to be funded and also that the relieving measures could not simply be funded by an increase in income tax from other sources.

CCAB-I does not dispute the approach taken overall to ensure that funding must be levied commensurate with reliefs granted. An unhelpful precedent though was created in that a flat levy was applied to existing pensions savings. There are, in our view, fairer and more equitable ways of achieving the funding result, and we advance a number of these later on in this submission.

The Minister for Finance has recently called on the citizens of Ireland to start spending in an act of patriotism to rescue the Irish economy. However, the citizens of Ireland have responded "*nemo dat quod non habet* "… we cannot give what we do not have, as more and more once disposable income is diverted to paying tax.

CCAB-I is mindful that revenues must be raised to fund national debt and run the country but we caution that a fine line exists between taxation policy which represses growth and taxation policy which motivates growth. In the following submission we set out necessary reforms to the taxation system which will cultivate competitive enterprise and consumer spending so vital to the recovery of the Irish economy.

Alternative Measures for raising revenue from Pensions

Recommendations:

- **maintain tax relief at the marginal rate for pension contributions,**
- **replace the pension levy with a temporary 1% tax on gains/profits of the fund,**
- **allow limited refunds of contributions to personal and occupational pension scheme**

The Pensions Context has not changed

In our Pre Budget 2011 submission, we stated that there is much merit in many of the proposals within the National Pensions Framework published in March 2010. We also commented that it would be extremely important that the Framework be taken on in its entirety, rather than cherry picking the revenue raising or revenue saving proposals for implementation without reference to the broader picture.

A pension policy is a mechanism for spreading the income earned (and the tax paid) over the lifetime of the worker, rather than merely over his or her working career. This had for years been deemed to be an admirable social aim, and the only real question should be on the amount of spreading that is equitable in a population where life expectancy in increasing as fast as it is in Ireland. In order to plan over that length of time some certainty is required. Pension policy in Ireland is currently in tatters – essentially there is no policy and people do not know how to plan for the future. This must be remedied or we will simply impose yet another burden on our children as more and more people throw themselves on the mercy of an increasingly stretched State system.

It seems to us that several of the key issues which the National Pensions Framework was designed to tackle have been at best set aside by the pensions changes in the last two Finance Acts and recent Social Welfare Acts. It is worthwhile listing these out to grasp the extent of the changes:

FA 2011: The imputed annual distribution by ARFs increased to 5% from 3%.

FA 2011: An individual must now have a guaranteed pension of €18,000 per annum (formally €12,700) or an ARMF or annuity of €120,000 (formally €63,500) until age 75 before he can transfer pension funds to an ARF.

FA 2011: The Standard Funds Threshold level is reduced from €5,418,085 to €2,300,000.

FA 2011: The earnings ceiling for employee contributions, RAC contributions and PRSA contributions is reduced from €150,000 to €115,000.

FA 2011: The maximum tax free lump sum entitlement is reduced to €200,000.

F(No 2)A 2011: Pension levy applies a temporary 0.6% on the value of a fund

The only positive measure introduced is that members of defined contribution schemes can now avail of ARF options on retirement.

While the tax treatment of pension contributions, pension funds and ARFs has undergone a radical cut, the fact that Ireland is facing a demographic winter has not altered. According to the CSO Population and Labour Force Projections 2011 – 2041, "The old population (i.e. those aged 65 years and over) is projected to increase very significantly from its 2006 level of 462,000 to around 1.4 million by 2041 under the two positive migration assumptions and to 1.3 million under the zero migration scenario. The very old population (i.e. those aged 80 years of age and over) is set to rise even more dramatically, showing a four-fold increase regardless of the scenario chosen."

Pensions Activity Tax Yields versus Pensions Savings Incentives

While we understand the need to raise revenues to meet the current national deficit, disabling the core incentive for pension savings now will give rise to an even greater funding crisis in the future. With this imminent crisis in mind, there are alternative measures for generating €700m[1] in pension related tax revenue:

Retain relief for individual contributors at their marginal rate of tax

The proposal to reduce tax relief on contributions to pension funds on a phased basis to 20% in 2014 should not be implemented. The greatest incentive to pension funding is tax relief based on the taxpayer's marginal rate of tax. If tax relief is reduced to 20% then top rate

[1] As specified in the National Recovery Plan 2011-2014

taxpayers will stop or significantly reduce their pension contributions. Per Department of Finance estimates, four out of every five taxpayers saving towards their retirement pay tax at the 41% rate.[2]

Replace the 0.6% Stamp Duty on private schemes with a temporary tax on scheme gains

The levy on private schemes has been introduced to fund a jobs initiative, but it is in danger of forcing some pension schemes to wind up in deficit. Media reports earlier this year suggested that as many as seven out of ten defined benefit schemes are in deficit, and the levy will make the funding problems worse. There are twice as many individuals in defined benefit schemes as are in defined contribution schemes[3].

The levy is inequitable as it taxes the pension contributions and any profits or gains accumulated. A more appropriate approach would be to replace the levy with a temporary Capital Gains Tax of 1% on gains made by pension funds annually for 2012, 2013 and 2014.

Exchequer Contribution Estimate

The 2009 Statistical Report of the Revenue Commissioners estimates the cost of the "Exemption of Investment Income and Gains of Approved Superannuation Funds" at €685m in 2008. There has been considerable turbulence in the investment market since then. Nevertheless, taking a conservative view that cost of the exemption, representing the non-application of taxes on yields at an average effective rate of 20%, a temporary 1% levy could yield in the order of €35m.

EU Treaties Compliance Consequences

Provided that the levy is applied to all pension fund vehicles within the charge to Irish Tax, there should be no adverse EU Treaties Compliance Consequences.

Apply a notional 0.6% charge to employees with an entitlement to public sector pensions.

There is no 0.6% Stamp Duty applied against public sector pension funding. We acknowledge that public sector pensions are by and large paid out of current expenditure. They are not funded in the same way as pensions in the private sector are funded. However, as the overall pensions restriction on public sector pensions is calculated by reference to a

[2] Report of the Commission on Taxation, at page 417

[3] The Pensions Board Annual Report and Accounts 2008, as quoted by the Report of the Commission on Taxation, at page 379.

notional capital value, a similar formula should be applied to come up with a counterbalancing levy.

As a matter of good public policy we need to move away from differentiating the tax treatment of people by virtue of whether they work in the public sector or the private sector. The worst aspect to the 0.6% levy is that it is focused solely on the private sector.

The current Public Service Pension Related deduction should be modified as follows:
First €15,000 of earnings - remain exempt
Between €15,000 and €20,000 – from 5% to 5.6%
Between €20,000 and €60,000 – from 10% to 10.6%
Above €60,000 – from 10.5% to 11.1%

This change is far less onerous on the public sector than the private sector, as in effect it only levies a notional current pension contribution. The private sector suffers a charge on "whole of career" pensions savings. Nevertheless it is an important step towards equity of treatment between the public sector and the private sector.

From 1 January 2011, the Pension Related deduction became subject to employee PRSI and the Universal Social Charge. This paralleled the reduction in relief available to the private sector in respect of pension contributions. Without prejudice to our earlier arguments, should the programme in the Four Year Plan for income tax relief curtailment for the private sector be followed, we would expect that income tax relief in respect of the Pension Related deduction should be similarly curtailed.

Exchequer Contribution Estimate

Making the Pension Related Deduction subject to employee PRSI and the Universal Social Charge (broadly 10%) was estimated to yield €60m in a full year. An additional 0.6% should therefore yield in the order of €3m - €4m.

EU Compliance Consequences

No impact. The TFEU does not extend freedom of movement to public sector employees.

Refund of Contributions

Taxpayers should also be allowed the take a refund of their pensions contributions up to the maximum of 10% of the fund encashment value. Income tax would be generated by applying income tax at the taxpayers' current marginal rate of tax on funds withdrawn, effectively reimbursing to the Exchequer the tax relief granted on the original contribution. This suggestion will generate tax revenue while at the same time allowing taxpayers to access much needed funds to service borrowings and supplement private expenditure. Taxpayers who were sufficiently prudent as to save when possible for retirement should be granted some limited access to their own contributions to help them through the downturn.

Currently for occupational pension schemes, an individual is entitled to a take a refund of contributions when he/she withdraws from service. A flat tax of 20% must be applied by the pension fund manager on the contributions withdrawn. We are not suggesting that this arrangement change – our suggestion relates to the expansion of this withdrawal option to allow an individual withdraw a maximum of 10% of their contributions, while remaining in service and still retain the employer contribution on the fund.

Employer contributions would not be refundable and pension funding regulations should be amended to facilitate the re-contribution of withdrawn funds at a later date by the taxpayer.

In addition to this measure, it is noted that if a person exceeds their PFT that the excess is taxed at an effective rate of over 70% when the person retires. On the basis that no one would plan into such a situation the only people that this penalises are those who have been lucky enough to invest in outperforming assets and those who have been caught as a consequence of the various reductions in the PFT. In any event, the excess tax is a long term potential revenue event for the Exchequer and does nothing significant to fund current expenditure or encourage spending behaviour that would help us in our current difficulties. We propose that where the PFT is exceeded at any particular time (say 31 December annually) that the beneficiary of the pension scheme would have a period of six months within which to withdraw the excess and have it subject to income tax (and not the USC) in that particular year of assessment. If the amount is not withdrawn it will continue within the pension fund until retirement and the current rules would continue to apply. This would have the dual impact of raising funds earlier for the exchequer and also releasing funds that will help stimulate activity in the economy.

Exchequer Contribution Estimate

The 0.6% levy is expected to generate €470m, suggesting relevant pension fund valuations in the order of €80bn. Assuming the 80:20 ratio of 41% taxpayers to standard rate taxpayers, €1bn would have to be drawn down to approximate this tax yield. There would also be positive Exchequer consequences from the release of €530m into the economy.

Recent media reports suggest that the average value of the first 500 of the 1,200 PFT notification forms submitted in June 2011 show an average fund value of €3,200,000. If this average is indicative of fund values going forward, then the excess over the reduced PFT will be €900,000. Tax revenues of €369,000 could be generated under the suggested excess PFT drawdown option along with the re-introduction of €531,000 for spending into the economy per fund.

EU Compliance Consequences

No impact.

Expanding tax relief for Employment and Investment Schemes

Recommendations:

- **remove the EIS from the list of tax reliefs subject to the High Income Earners Restriction**
- **allow upfront tax relief at 41% for investments in start-up companies**
- **tailor a facility for company owner/managers to investment in their company by way of loans and benefit from the EIS**

EIS and the High Earners Restriction

CCAB-I welcomes the replacement of the BES and Seed Capital Scheme with the Employment and Investment Scheme (EIS). We recognise a number of improvements provided for in the EIS such as the extension of the definition of trading activities, the reduced holding period for investors, and the increased lifetime and annual funding limits for the beneficiary company.

However, the tax benefit of 30% for rewarding the investor to make a high risk investment is inadequate when coupled with the High Income Earners Restriction.

There is strong competition for an investor's limited resources and a genuine Government initiative to encourage investment in Irish companies must be matched with a worthwhile tax relief.

The curtailment of tax reliefs for pension and other forms of investment will create a demand for tax efficient investment vehicles. The EIS will not realise its full potential as long as its tax relief is curtailed by the High Earners Restriction.

Bias towards Start-Ups is required

We note that an additional 11% tax relief is available at the end of the holding period if the company concerned increases the number of employees over the term of the investment, or has increased its expenditure on research and development. In effect, this is a success bonus for the investor. In practice that could channel money away from riskier, start-up ventures which could have greater employment potential should they succeed.

A tax incentive for investment should be biased towards investment in new start-up companies. New companies in the SME sector find it difficult to attract investment and

currently few if any BES investment fund promoters sell EIS equivalent tax relief investment in start-up companies.

Tax incentivised Risk Capital, which is what the EIS is designed to provide, should fill the funding gaps identified in the recent CSO Study – Access To Finance 2007 and 2010[4]. That study noted that enterprises that applied for loan finance had a success rate of 90% in 2007, compared with 50% in 2010. Enterprises applying to banks for loan finance were successful in 95% of cases in 2007, while in 2010 the success rate dropped to 55%. The main reasons given by banks for wholly or partially refusing loans in 2007 were lack of capital and insufficient or risky potential. However, in 2010 the most common reason identified was that enterprises had too much debt.

Start-up companies must compete with established companies for limited investment and the investor will obviously favour the established company due to lower risk. The start-up company is directly creating new jobs. As new enterprise is a vital component to economic growth and corresponding recovery, the investor to a new EIS start-up company should get tax relief of 41% up front on his investment.

Funding outside of Share Capital

The EIS is predicated on the requirement for the investor to purchase shares in the company and hold those shares for a three year period. While this requirement is commercially appropriate for investments aimed at third party investors, it is not a tax efficient or a commercially appropriate means for the owner/manager to invest in his company. The exit mechanism of share sale does not support his/her long term involvement with the business.

In general, owner/managers of SMEs make a personal investment in his/her business by way of a loan to the company. If a share investment is made then he/she must either liquidate or sell the shares in order to realise a return on their investment. The EIS rules for owner/managers of SMEs therefore require such individuals to dispose of the business they have worked hard to build up in order to get a return on their investment.

The EIS is the only tax relief option open to the owner/manager since FA 2011 abolished income tax relief for loans used to invest in companies. We strongly recommend that the rules for investments by the owner/manager under the EIS should allow for investment by

[4] Published 23 May 2011

way of loan to facilitate the long term development of the business and involvement of the entrepreneur.

Exchequer Contribution Estimate

Refinements as suggested to the EIS should be revenue neutral. There may be a small cash flow benefit as PAYE receipts from new employments may predate the granting of relief to investors.

EU Compliance Consequences

The delay in securing EU Approval under the State Aid rules for the EIS as currently constituted is of major concern. It is in fact counterproductive to introduce a relief with an inordinately delayed effective date.

EU guidelines on State Aid clearances for risk capital measures refer to measures designed to provide or promote risk equity and/or quasi-equity financing to enterprises in their start-up and expansion phases. We understand the Commission will regard in a positive light existence and evidence of market failure, appropriateness, incentive effect and necessity of aid. It is not surprising that a scheme as unnecessarily convoluted as EIS is encountering EU clearance delays. The suggestions made here will simplify clearance procedures.

Attracting Decision Makers Back to Ireland

Recommendation:

- **introduce an "impatriate regime" to encourage key international executives to re-locate to Ireland**
- **abolish the domicile levy**

Importance for Foreign Direct Investment

Long term Foreign Direct Investment involves the re-location of the key executives and decision makers to Ireland. When the top executive is working on the ground in Ireland then he/she is more likely to make long term commitments to building business resources in Ireland such as job creation, infrastructural investment and marketing Ireland as a key place of business.

In recent years we have remodelled mechanisms which worked very well in encouraging the decision makers to locate in Ireland, but with mixed results. The existing incentive regime is uncompetitive with other jurisdictions because:

- Relief is restricted to 50% of an excess, rather than the full amount, of earnings
- Relief is on a refund basis

Specific refinements to make the current relief useful

The relief, as currently constituted under Section 825B TCA 1997, is being found in practice as being too narrow in scope. It cannot be marketed.

Based on our practical experience of implementing the relief, there are three specific issues which could be re-examined to promote the relief as an incentive towards its economic purpose; the relocation of skilled expatriates to Ireland in support of FDI. These are:

- The exclusion of Irish nationals
- The income threshold of €100,000
- The granting of the relief by way of refund

Restrictions on the origin of the employee

Under section 825B, relief is denied to individuals domiciled in Ireland. The old remittance basis regime applied to non domiciled individuals and also citizens of Ireland not ordinarily resident. This allowed for relief in respect of employment earnings for a limited period from when the individual returned to Ireland. The old regime acted as an incentive to repatriate home grown talent. There is no similar incentive for Irish citizens under the current system. In addition, Irish citizens working abroad for many years, who satisfy all other conditions, cannot avail of the relief. On the other hand, their foreign domiciled colleague, in the same circumstances, can claim the relief.

Income Threshold

Relief is only beneficial if the greater of remittance of employment earnings and an amount equal to an income threshold of €100,000 plus 50% of the excess, is less than income attributable to Irish workdays. Salary levels worldwide have reduced since the relief was first framed. It is now unlikely that the relief would be of benefit or even provide a significant tax saving for many foreign employees relocating to Ireland.

We recommend that both thresholds be reduced to €50,000 and 25% respectively.

Relief by way of refund

Again, this aspect of the relief was framed at a time when there was less sensitivity to the upfront costs of international assignments. In practice, it is the multinational employer, through a process of tax equalisation, which bears any additional income tax costs associated with their international secondment programme. We need to devise a mechanism whereby effective relief can be granted through the normal payroll process – perhaps by way of an allowance computed to the value of the anticipated tax refund, but subject to adjustment on the filing of the return of income.

Alternatives – the Impatriate Model

While the existing arrangement might be attractive for an individual, in practice, multinational assignments are arranged on a “hypo tax” basis, where a net sum is agreed by way of remuneration, and then worked back, depending on the country where he or she is based, to arrive at the taxable gross amount. Unfortunately this leaves us as a poor comparison to other jurisdictions.

We have in the past advocated an approach similar to the French Impatriate model, and put it forward for consideration again. This “impatriate regime” is aimed at managers and employers sent to work in France by a non-French employer to perform a professional activity for a limited period of time. The impatriate must take up French tax residence and not have been a French tax resident during the five-year period preceding the start of his duty in France. The tax incentive takes the form of a partial exemption from income tax for the portion of the impatriate’s salary compensating him/her for the transfer to France or an exemption on 30% of the global remuneration of the impatriate.

The Domiciles Levy

From 1 January 2010 certain individuals who are Irish citizens and Irish domiciled in a tax year pay a levy of €200,000. Specifically the levy applies where the individual has:

- Irish located property greater than €5 million,
- worldwide income in excess of €1 million and
- an Irish income tax liability less than €200,000,

The levy applies irrespective of where the individual lives or where they are tax resident. This levy is unenforceable if the individual is non-tax resident and otherwise not in the Irish tax system.

Given Ireland’s current high standing[5] as a transparent and effective tax authority, it is a paradox that Ireland should attempt to operate a tax which depends on voluntary payment of a substantial tax by an individual not living in Ireland. The basis for applying the levy is also at odds with Article 4 of the OECD’s Model Convention on double taxation agreements as it seeks to apply tax even where an individual is not Irish resident and whose centre of vital interests (family and social relations, occupations, political, cultural or other activities, place of business) are located outside the State.

Nor is it helpful to Ireland’s international standing that the levy cannot be offset against taxes other than Irish income tax. We have evidence to suggest that capital has already left the

[5] OECD Forum on Tax Transparency

country to avoid the imposition of the levy in advance of its first payment date of 31 October 2011.

On the basis that this levy contradicts internationally recognised best practices on double taxation policy and is unenforceable, we call for the abolition of this levy to protect Ireland's standing as a credible tax authority. If this is not possible, it should at the very least be clarified that the levy can be reduced by reference to income tax and social insurance paid by the individual in their country of residence – the absence of such relief would seem in any event to be contrary to EU rules and at least the spirit if not the word of most of our double tax agreements. It goes against even the tenuous reasoning for the introduction of this levy not to allow such offsets, as people who are paying such substantial taxes as they live and work in other jurisdictions can hardly be termed "tax exiles".

Exchequer Contribution Estimate

Refinements as suggested to the limited remittance basis should be revenue neutral, or revenue positive in that they will attract in new taxpayers. Please note that under no circumstances are we advocating tax exemptions.

No money has been collected under the domiciles levy rules as of yet. Given the relatively small constituency of potential domiciles levy payers, we doubt that the abolition of the levy would result in anything more than €10m in revenue foregone.

EU Compliance Consequences

EU Approval under the State Aid rules for significant amendments to the limited expatriate regime would be necessary.

Re-Introduction of Tax Relief for Patents

Recommendation:

- **introduce a 10% corporation tax rate for profits generated from patents**
- **employees working in innovation should be subject to tax at 12.5% on dividends from Intellectual Property development**

An Irish "Patent Box"

FA 2011 abolished tax exemptions for patent royalties and dividends from a qualifying patent from 24 November 2010. This is a counter-productive move in light of the fact that many countries are increasing tax incentives to encourage the location of innovation in their particular jurisdictions because jobs and enterprise generated by innovation is recognised and valued.

We recommend the introduction of a reduced tax rate for companies on profits generated from patents similar to the UK's proposed "Patent Box"[6]. Ireland must move fast to ensure that we remain competitive as a location of choice for international and indigenous innovators. As the rate proposed in the UK is 10%, a similar rate in Ireland is necessary. Tax relief to the Irish equivalent of the "Patent Box" should be broad and inclusive regime for the purpose of encouraging businesses across a wide range of sectors to invest in the Ireland, generating growth and jobs. Ensuring that the tax measures are inclusive will also assist in ensuring that this relief does not fall foul of EU State Aid rules.

Ireland already has the infrastructure to implement this relief:

- A legal authority to validate the patent (the Patents Office)
- Expertise within in the R&D sections of Revenue and legal powers to secure specialist expertise.

[6] Per the HM Treasury consultation document *The Taxation of Innovation and Intellectual Property* 29 November 2010, "The Government intends to introduce a preferential regime for profits arising from patents, known as a Patent Box. Encouraging innovative business to invest in the UK will play a key part in supporting a strong, growing private sector. The Patent Box will encourage companies to locate the high-value jobs and activity associated with the development, manufacture and exploitation of patents in the UK. It will also enhance the competitiveness of the UK tax system for high-tech companies that obtain profits from patents".

Rewarding the Innovators

It remains important to recognise the input and involvement of employees who contribute to the nation's bank of Intellectual Property. In addition to the introduction of a special 10% rate of tax on corporate patent income, any dividends paid to shareholders directly involved in the innovation process should be subject to a 12.5% withholding tax rate, with that tax constituting the final liability.

This approach will be attractive in the commercial environment where the remuneration for an innovator and their team can be directly linked to the commercial return being made from their underlying work. However it would not be sufficient to implement this measure on its own, as this would be to the detriment of innovation within the public, and in particular, to the university sector. Therefore, the same rate of tax should apply to income earned from innovative patents held by any person in Ireland and in respect of which they carried out actual innovative technical development, and the same tax should apply to a bonus paid to an employee out of such income received by an employer.

In addition to the immediate benefits of this regime, this would send a clear message to people still in education of the types of activity that are in somewhat short supply but are valued by society and which will be supported by the State.

Exchequer Contribution Estimate

The abolition of the Patent Exemption was estimated to raise €50m in a full year. The introduction of a reduced rate of Corporation Tax instead will have a tax cost, but based on on this figure, the cost will be unlikely to exceed €10m.

A special income tax regime on patent dividends for innovators will also have a tax cost, but this would be offset in part by greater activity in the area. While this figure is difficult to estimate, again based on the 2011 Budget figures, we believe a cost estimate of a further €10m is also reasonable.

EU Compliance Consequences

EU Approval under the State Aid rules may be necessary. We recommend that the initiatives be linked to the suggested enhancements to the R&D regime offered below to ensure the Commission is aware of the overall strategy involved, rather than looking at specific measures in isolation.

Research and Development Tax Credit Accessibility

Recommendation:

- **replace the 2003 base year approach with a volume based approach for claiming the R&D credit**
- **launch a cohesive initiative to promote the R&D credit**

Limitations of the Incremental Approach

We welcome measures introduced by F(No2)A 2011 which provide an option for a refund of R&D tax credits based on the current payroll costs and prior year costs. This measure will certainly assist Ireland in competing with other jurisdictions and will attract international R&D companies to locate here.

However, we also need to look at ways of encouraging R&D expenditure within a company with internally competing expenditure needs.

Currently the R&D credit is a function of increases in expenditure using 2003 as the base year of comparison. While the incremental approach was a fair means of encouraging year on year increased R&D expenditure, it is not appropriate in a recession. A volume based test allows every cent spent on R&D to qualify. In these difficult times, expenditure is not taken lightly by any business and therefore the volume based approach offers a direct correlation with tax relief and dedicated expenditure on R&D. Industry consensus supports the expenditure approach as outlined in KMPG 2010/11 survey on Research & Development in Ireland with 42% of companies surveyed favouring the volume based approach.

For practical purposes, the 2003 base year approach requires companies to retain records for close to a nine year period. This period of retention of records is too long and cumbersome and penalises those companies who have invested in Ireland over the long term. The volume based approach removes the practical problems associated with retaining records going back to 2003 and optimises the incentive to spend in a time when all expenditure on R&D must be rewarded given the funding difficulties faced by Irish businesses.

Marketing R&D Incentives

As outlined in previous submissions, many Irish businesses are not aware of the R&D tax credit relief or are unaware of how to go about successfully claiming the relief. KPMG's 2010/11 survey on R&D activities in Ireland shows that 18% of companies surveyed had not even heard of the R&D tax credit. Therefore, further work is needed to promote and educate

SME on possible entitlement to claim the R&D credit. We suggest that Revenue and Enterprise Ireland should actively target the Irish SME sector to first make it known that R&D relief exists. It should then provide user friendly information guides supported by expert advice within Revenue on how the relief works to improve the take up of R&D relief in Ireland.

The R&D tax credit is an extremely positive tax measure and every relevant company in Ireland should be aware of how it can access the credit.

Exchequer Contribution Estimate

The only reliable way to establish the cost of moving to a volume basis is to introduce the measure for a limited time period, say two years. The cost benefit can then be assessed.

EU Compliance Consequences

Generally, R&D incentive activities need only be notified to the Commission. EU Approval under the State Aid rules will not be necessary.

Remove the Close Company Surcharge on Professional Services

Recommendation: remove tax discrimination against professional service companies

Impact of the Surcharge

The CCAB-I has long been a proponent of the removal of the surcharge applied to professional service companies. The Commission on Taxation supports this view in its 2009 report:

> *"Our investigation of ways to support economic activity and grow employment is based on a pro-business ethos. The close company surcharge on professional services companies inhibits such companies from re-investing their trading income. Similar restrictions do not apply to other trading companies. We cannot see an objective rationale for distinguishing between professional services companies and other trading companies and we therefore recommend the abolition of the surcharge for professional services companies."* [7]

Professionals, including member firms of CCAB-I, are incorporating for the purposes of limited liability and debt structuring. The decision to incorporate is not a life style choice for the purposes of income accumulation and tax avoidance. The sole trader/partner will expect (and need) to drawn down the same level of income out of an incorporated business as he/she took out of the sole trade/partnership. Therefore, income tax will be paid on the same income levels and corporation tax will also be applied on net corporate profits. The imposition of another layer of tax on professional service companies has no basis in 2012 and constitutes discrimination.

Retaining the surcharge presents particular dangers for Foreign Direct Investment, particularly in the IFSC. It is by no means clearcut the extent to which Revenue will seek to impute close status, and then professional services activities on certain fund vehicles. With the advent of the USITS IV Directive, funds management becomes more mobile within the European Union than ever before. We need to have available every reason for this business

[7] At page 198

to come to Ireland. Uncertainties surrounding the application of the surcharge are profoundly unhelpful.

The surcharge and the EIS

Professional service companies are equally capable of providing job opportunities but are excluded from the EIS. The financial model of professional service companies is currently based on running the business on an overdraft or loan. These companies have many uses for outside investment which would be used for equally worthy purposes as with other trading companies who can benefit from the EIS. The EIS should be expanded to allow for investment in professional service companies.

Exchequer Contribution Estimate

Usually dividends are paid out to avoid the consequences of the Professional Services surcharge. There will therefore be no immediate cost to the Exchequer.

EU Compliance Consequences

None in our estimation.

Reform of Capital Tax

Recommendation:

- **offer a form of roll over relief on tax arising on family business succession**
- **temporary reduction of stamp duty on commercial property**

Context – Capital Reliefs serve a purpose

The National Recovery Plan 2011-2014 indicates that the base for taxation under the heads of CAT, CGT and stamp duty will be broadened by abolishing or restricting tax reliefs. Many stamp duty reliefs were abolished under FA 2011.

Moves to abolish or restrict capital tax reliefs which allow for the tax efficient succession of Irish businesses from generation to generation would be detrimental to the survival of Irish business. Reliefs such as Retirement relief, Business and Agricultural relief are in place for the purposes of encouraging business men and women to grow their businesses to the best of their abilities with the end sight of passing the business on to the next generation of entrepreneur be it their own children or an unrelated party.

Many businesses are being run at a loss today. For many business people, effort will only be rewarded by the future realisation of value through the sale or succession of the business. A punitive capital taxes regime has immediate consequences for the current sustainability of a business.

The National Recovery Plan is vague as to the Exchequer benefits if the capital tax base is broadened. The Plan acknowledges the difficulties for capital tax yield which result from the deterioration in underlying asset values. Rate increases and the elimination of reliefs might not result in worthwhile revenue yields while doing significant damage to the business environment.

Capital Tax Bonds

If moves to restrict CAT and CGT are indeed to go ahead, then we propose that a form of roll-over relief of tax should be introduced linked to investment in Government Bonds.

For example, an individual could defer his/her tax liability arising on the disposal of his/her business/farm to a family member or third party by investing in a government bond for a period of not less than 5years. The bond yield would be tied to the capital gains tax liability. The capital gains tax due on the original transaction would crystallise on the encashment of the bond. The Exchequer would have the use of the full proceeds; from the taxpayer perspective the CGT arising would ultimately be extinguished at least in part by the bond yield on maturity.

Stamp Duties on Commercial Property

CCAB-I welcomes the reduction of stamp duty to 1%/2% on transfers of residential property in FA 2011. This is the first step in the process of encouraging the stabilisation of falling house prices.

A temporary reduction in stamp duty rates is also necessary to aid stabilisation in commercial property market. The top rate of stamp duty of 6% should be reduced to a maximum of 4% (as in the UK) and the stamp duty threshold for exempt transactions should be increased from €80,000 to €150,000. We suggest that this reduction apply for a period of two years.

Exchequer Contribution Estimate

We share the uncertainty of the Four Year Plan in assessing the cost of capital reliefs. The proposals made will have a cash flow cost, but the value of additional lending to the Exchequer should be recognised.

The Stamp Duty yield from commercial transactions is totally flat. A temporary reduction in commercial Stamp Duty rates will undoubtedly raise additional revenue.

EU Compliance Consequences

None in our estimation.

Legal Professional Privilege

Recommendation: CCAB-I calls for public debate on the appropriateness of LPP exemptions within the tax system

Mandatory Reporting

Significant powers of information gathering have been granted to Revenue on introduction of the Mandatory Reporting Regime. We have no issue in regard to Revenue being granted powers provided that any such powers are proportionate and subject to appropriate checks and balances.

However specific exclusions from compliance are specified in the legislation where the information which Revenue might request is subject to Legal Professional Privilege (LPP). This provides an unacceptable commercial advantage to law firms providing tax services.

In the UK court case, Prudential PLC & Anor v Special Commissioner of Income Tax & Anor [2009] EWHC 2494, LPP was described as "where legal advice is sought in confidence from a qualified legal adviser in his professional capacity, privilege may be claimed for the communications made for that purpose."

The idea behind LPP was to ensure that any person can feel confident in seeking advice about their legal rights and obligations and in particular advice about litigation or potential litigation. Equally, Revenue need information about taxpayers to ensure that they are paying the right amount of tax. It is quite right that there should be a balance between the right of Revenue to know and the right of the taxpayer to privacy. It is not right that this balance can be skewed when the taxpayer uses a legal adviser to deal with his tax affairs.

Discrimination between Tax Practitioner Firms

Firms of accountants and law firms are not treated equally when it comes to providing information to Revenue. While providing for the Mandatory Disclosure of Certain Transactions Chapter within TCA97, s817J states that "Nothing in this Chapter shall be construed as requiring a promoter to disclose to the Revenue Commissioners information with respect to which a claim to legal professional privilege could be maintained by that promoter in legal proceedings." Case law has established that only legal firms can avail of this protection.

It is clearly in the public interest to have a fair, robust tax system within which taxpayers can know with certainty how they will be taxed. We suggest that LPP exemptions within the Taxes Acts will result in their sufficient prevalence as to be discriminatory – affording some taxpayers greater protection under the law by virtue of the kind of firm they choose to handle their affairs.

By extension this leads to an inference that advisors who qualify for the LPP exception are preferred from an official policy perspective, even though they provide exactly the same service as those that do not qualify for the exception. This is clearly anti-competitive and of extreme concern to our members. Equally, the appearance of specific LPP provisions in the legislation is very new, and can only be interpreted as an enhancement of the LPP already claimed by legal firms in respect of all advice that they provide and a recognition that this is accepted and will not be challenged by the State.

Suspension of Legal Professional Privilege for Mandatory Reporting matters

We believe that a public debate needs to be conducted on the appropriateness of LPP exemptions within the tax system, the enshrining of such exemptions in the legislation itself as an enhancement of the fundamental legal principle and the preferential treatment of one set of advisers in this regard even where they provide the same service as those with the officially preferred qualification. Until this can be resolved we would suggest that the existing exclusions in the legislation be suspended and allowed to rest on the basic legal principle, and that no further legal enhancements to the LPP principle as it applies to those with a legal qualification be introduced until the basis for the preference being conferred is fully aired and understood.

The Australian Government has issued a discussion paper entitled ***Privilege in relation to Tax Advice*** to consider whether legal professional privilege ought to be extended to accountants and other tax advisers. The Australian Government notes the wide ranging powers of the Australian tax authorities to obtain information from taxpayers. The discussion paper notes the current operation of legal professional privilege in the Australian context. As Australia operates a common law system, comparable to Ireland and the United Kingdom, many of the observations in the discussion paper are relevant here.

Concerns in relation to how the mandatory disclosure regime operates in the Irish context surround legal professional privilege. Revenue apparently felt constrained, because of their interpretation of the legal professional privilege requirement, to operate carve-outs for legal firms offering tax advice which might otherwise be subject to mandatory reporting.

Such a distortion of the agent market, where its unbiased operation is essential in a modern self-assessed tax regime, is not appropriate.

Exchequer Contribution Estimate

None in our estimation.

EU Compliance Consequences

There are both Competition and Regulation issues which will require closer examination if the current situation persists.