Broadening the Irish Tax Base in 2013

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IRISH GOVERNMENT SPENDING THROUGHOUT THE 'CELTIC TIGER' YEARS was funded to a certain extent by tax receipts linked to buoyant property prices. The flood of revenue into the Exchequer from the construction and property sector gave Irish Governments the opportunity to reduce the traditional tax burdens on income, and over the 'Celtic Tiger' years income tax and CGT rates were cut, tax credits were increased and the standard 20 per cent band was increased, reducing the overall tax take from income.

Property sales resulted in tax on the vendor's profits and stamp duty and VAT costs for the purchaser, so both sides of each transaction were taxed. In a rising property market, with frequent transactions the 'tax take' was high, but when the market began to falter late in 2006 and early in 2007 (so the level of transactions fell) the disadvantages of a tax base which was focused on transaction taxes became apparent.

Steps had to be taken to increase the tax take from income, and discussions on the Irish economy began to centre on how to broaden the tax base. The first port of call in increasing tax take is to consider increasing the tax paid by existing taxpayers.

Throughout the economic downturn successive Governments have underlined their commitment to Ireland's 12.5 per cent rate of corporation tax (seen as the corner stone of Ireland's economic policy). In addition successive governments have stated that they will not raise the rate of income tax (which has remained at 41 per cent since 2007), however, a new tax on income (the Universal Social Charge or USC) was introduced which has resulted in an additional tax flow from income.

Since 2007 Irish Governments have taken other steps in their budgets to steadily increase taxes on income, without raising rates, by reducing the level of income tax credits, reducing the lower 20 per cent income tax band, preventing a high level of tax reliefs being used by capping the level of reliefs that can be claimed by high earners, and phasing out tax benefits such as the rent credit, and mortgage interest relief.

Given the relatively small population (4.588 million according to the 2011 census) the number of taxpayers who can carry an income tax burden is not high. The last set of income tax statistics released by Revenue show that the number of income tax cases is only 46 per cent of the population and of those just under half (45 per cent) have income levels too low to pay any income tax at all. High earners are often seen as a target but fewer than 10,000 Irish taxpayers (less than 0.5 per cent of all cases) have income of €275,000 or over. It follows that the scope for simply increasing income taxes is limited.

The Government has taken a number of steps to broaden the tax base, including the introduction of charges on properties (such as the Non Principal Private Residence charge or 'NPPR', and the Household Charge), pension levies, a parking levy for employees in urban areas using parking supplied by employers, and the proposed

introduction of water charges.

A non domiciliary tax of €200,000 was introduced which was aimed at wealthy Irish citizens who are non resident (but remain domiciled here), and who have worldwide income of over €1million and Irish assets of over €5million. This tax also applies to Irish residents but a credit for Irish income tax paid effectively offsets the domicile levy. However, the success of this tax has been limited with Revenue figures for 2010 show 10 returns filed, and only €1.4million collected from the levy.

Pension funds were also targeted by capping reliefs, the imposition of a pension levy and the introduction of a provision deeming five per cent of the value of pension funds which have vested in the pensioner to have been distributed each year, so that it is treated as income for tax purposes.

New Tax Legislation – Broadening the Tax Base

On 13 February 2013 the Finance Bill 2013 was published, implementing the measures announced in the 2013 Budget, and including some additional measures. The consensus from commentators before the Budget was published was that the 'low hanging fruit' had been picked and that the Minister would need to be creative to increase tax revenues without touching the key tax rates (such as VAT, income tax, and corporation tax).

The Minister did bring in 'across the board' increases in ancillary tax rates, increasing the rates of CAT (Irish inheritance tax), CGT, DIRT (tax operated on deposit interest) and exit taxes on 'unit fund' type investments from 30 per cent to 33 per cent. Reduced rates of USC that applied to individuals over 70 years of age, or holding a medical card and earning more that €60,000 were abolished, bringing those taxpayers up to the standard USC rates.

The most talked about measure to broaden the tax base is the introduction of Local Property Tax or LPT on residential properties. The draft legislation was published in the Finance (Local Property Tax) Bill 2012, and amended by Finance (Local Property Tax) Amendment Bill 2013. LPT is to be payable by the owner of a property, and based on the market value of residential properties, which will be determined for a period of three years.

LPT will be applied using a banded system with the first band being €0 to €100,000 and bands increasing in increments of €50,000 thereafter up to €1m. LPT will apply at a rate of 0.18 per cent on properties valued at €1m or under, will be charged at a rate of 0.25 per cent on any market value in excess of €1m. In the first year, 2013, the impact of the tax will be mitigated by the fact that the tax will only be in force for six months of the year (halving the cost to the taxpayer) so the full impact of the new tax will not be felt until 2014.

Encouraging Recovery - The Small & Medium Enterprise Sector

The SME sector incorporates nearly 70 per cent of people engaged in the business economy and accounts for just over half of the country's turnover. In 2012 the Irish Central Statistics Office issued a report entitled *'Business in Ireland 2010'*, which looked at the role of the SME sector in Ireland and noted that:

"SMEs accounted for almost 99.8 per cent of active enterprises, 69.1 per cent of persons engaged, 51.5 per cent of turnover and 46.8 per cent of gross value added (GVA)....It is noticeable that while SMEs employed almost seven in every ten persons in the business economy, they accounted for lower proportions of turnover and GVA".

In 2013 the Irish Government has focused on encouraging entrepreneurial activity and the Minister for Finance announced an initiative to assist SMEs, which involves:-

- Increasing the VAT 'cash receipts' threshold from €1m to €1.25m, to ease cash flow.
- Revising the 'carried interest' provisions in the tax code to help small and medium businesses access venture capital funding.
- Allowing any existing 'start up' company relief (which reduces corporation tax in the first three years for a new company) to be carried forward into future years if it cannot be used because of insufficient profits.
- Increasing the level of estate and investment income that can be retained in a company before close company surcharges apply from €635 to €2,000.
- Increasing the amount of initial expenditure that can be claimed for R&D tax credit purposes on a value basis (without looking at the increase in R&D spending over the 2003 basis period) from €100,000 to €200,000.
- Reducing the R&D 'time allocation' required before a company can transfer R&D tax credits to a key employee from 75 per cent to 50 per cent.
- Extending a new tax relief which gives a foreign earnings deduction to encourage businesses to opening up trading opportunities with the 'BRICS' countries, (identified as key markets for Irish business) to cover Algeria, Democratic Republic of Congo, Egypt, Ghana, Kenya, Nigeria, Senegal & Tanzania.

Extending the term of certain existing tax reliefs (subject to EU approval). The EIIS and BES schemes for seven years to 31 December 2020, and the stock relief provisions for all farmers (including young trained farmers) have been extended to 31 December 2015.

The farming sector has benefited from the focus on SMEs and in addition a stock relief deduction of 50 per cent now applies to qualifying farming partnerships, and a new CGT relief has been provided for farm restructuring, which involves the sale, purchase or exchange of agricultural land.

Conclusion

Ireland continues to have a significant Budget deficit (8.2 per cent in 2012) and further taxation measures, together with spending cuts will have to be introduced in order to reduce the deficit. The recent deal that the Government agreed with the European Central Bank in relation to the promissory notes for IBRC (formerly Anglo Irish Bank) will go some way to reducing the cashflow impact of this deficit (according to the Government the deal will result in a reduction of 0.6 per cent in the deficit).

Ireland's tax base has changed significantly as the tax system has moved away from a dependency on tax receipts from property transactions, to a wider tax base, focused on collecting small levels of revenue from new taxes such as water rates, and local property tax, increasing the level of taxes on income and preserving the corporation tax position.

In order to maintain a stable economic future and ensure a somewhat reliable tax base there is a need for real economic growth. Such growth is necessary to both reduce the level of unemployment, and increase the tax take through production of goods and the provision of services rather than simply increasing the tax burden of existing tax payers. Whether the measures provided for in Budget 2013 and in the Finance Bill will help achieve this goal remains to be seen. ■

Ireland - Fact File

GENERAL OVERVIEW	
Location	Western Europe.
Time zone	Greenwich Mean Time +/– 0.
Population	4,588,000.
Capital	Dublin.
Airport(s)	Dublin, Cork and Shannon Airports.
Language	English.
Currency	Euro.
Political system	Democratic Republic.
International dialling code	+353.
Legal system	Statute and common law.
Centre's expertise	Finance, banking, international trusts.
TAX	
Personal Income tax	Standard rate of income tax at 20% and higher rate at 41%.
Corporate income tax	12.5%.
Exchange restrictions	None.
Tax information exchange agreements	For full details, please go to www.ifcreview.com/TIEA
SHARE CAPITAL	
Permitted Currencies	All major currencies.
Minimum authorised capital	No minimum requirement.
Minimum share issue	€1.
TYPE OF ENTITY	
Shelf companies	Not available.
Timescale for new entities	5 – 10 working days.
Incorporation fees	€100.
Annual fees	Annual return €40.
DIRECTORS	
Minimum number	Two.
Residency requirements	Every company must have one EEA resident director or failing that, provide a fund to value of €25,394.76 as a surety.
Corporate directors	Not permitted.
Meetings/frequency	At the discretion and convenience of the directors.
SHAREHOLDERS	
Disclosure	Yes.
Bearer shares	Permitted but restricted.
Minimum number	One.
Public share registry	None.
Meetings/frequency	Must hold an annual general meeting.
ACCOUNTS	
Annual return	Yes.
Audit requirements	Yes.
OTHER	
Registered office	Yes.
Domicile issues	
Company naming restrictions	Yes.