Irish Tax Institute

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Minister Michael Noonan T.D.
Minister for Finance
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Finance (No.2) Bill 2013 and related issues

Dear Minister

We would like to take this opportunity to acknowledge the positive measures introduced in Budget 2014 and the subsequent Finance (No.2) Bill 2013.

We welcome in particular the announcement on 20 November that there will be no change to the income tax Pay & File deadline for 2014. We were grateful for the opportunity to participate in a very constructive consultation process on this issue.

Institute representatives made the case for retention of the current Pay & File system in a well-received appearance before the Oireachtas Committee on Finance, Public Expenditure and Reform on 20 November. That Committee undertook to prepare a report, which will reflect the views of the Institute, and we understand that your Department will receive a copy of the report. We look forward to further consultations and discussions on this matter over the coming months.

Provisions of Finance (No.2) Bill 2013

We would like to acknowledge the very welcome commitment in Budget 2014 to maintain income tax rates, bands and basic credits at their current levels. We also welcome the various initiatives comprised in the "Tax Package Building Business and Creating Jobs".

In this letter, we would like to raise some issues on behalf of our members in relation to certain measures in the Finance Bill. The following is a summary of our specific observations and recommendations, and further details on these issues are set out in the body of this letter:

Summary of Institute observations and recommendations

(a) Some amendments to the new "Entrepreneur relief" could broaden its applicability and would likely enhance its attractiveness to potential entrepreneurs.
(b) A strong commitment would be welcome that there will be no further extensions of the Pension Levy.
(c) We welcome the proposed clarification that the amendments to capital gains tax retirement relief for disposals of leased land will retain the existing relief under section 599 TCA 1997 for disposals within the family.
(d) Some clarification would be welcome on various aspects of the capital gains tax amendment introduced for debt releases.
(e) We welcome the proposed clarification that the relief on loans applied in acquiring an interest in a partnership will continue to apply to replacement loans drawn down after 15 October 2013.
(f) We wish to highlight issues with certain aspects of the requirement introduced in the Bill for businesses that do not pay their suppliers within a certain 6 month period to repay the input VAT previously claimed.

(a) Entrepreneur relief

The Institute has strongly advocated the need for a capital gains tax incentive to encourage entrepreneurs and investors to build and invest in Irish businesses and to consolidate their business activities and employment base in Ireland. We therefore welcome the introduction of the new capital gains tax "Entrepreneur relief" in section 43 of the Bill as a positive first step in this direction.

However, we are concerned that the measure introduced in the Bill does not go far enough in its current form. It is clear that, certainly in the near future, the scope will be limited and the cost will be low – we note that the estimated cost of the measure is €20m in a full year by 2018. This will be the case in practice given that the relief does not arise until ultimate disposal, and also given the large amounts of capital losses currently in the system.

We believe that, if the incentive is to be meaningful, the relief should be given at the point of reinvestment rather than the point of disposal. We appreciate that it is difficult to introduce measures at this time which would have an upfront cost, but, in the longer term, the relief will need to have broader application if it is to be meaningful.

One immediate amendment which may make the incentive more attractive in the short term might be to extend the period in which the initial gain is required to have been made, to include earlier years, in which capital gains are more likely to have arisen.

Other issues which we believe should be reviewed are as follows:

- The definition of "qualifying company" and whether the company is required to meet that definition throughout the period of investment. If that is the case, it could be said to be contrary to the purpose of the relief, which is to invest and reinvest for growth.
- The question of whether a company qualifies if it is in a start-up phase when the investment is made and commences to trade shortly thereafter.
- The issue of the "full-time working director" requirement and the minimum level of time involved to meet this criterion. This is particularly relevant where a business person has investments in more than one businesses or ventures.

- The possibility that the "control" requirement may inadvertently exclude a founding shareholder, who is involved in the business as a full-time working director, but may not hold more than 50% of the shares.

We believe that this relief should be reviewed after 12 months, to measure uptake and revise the underlying premise if necessary. To achieve the policy objective of encouraging entrepreneurship, the relief must be attractive enough to achieve uptake, particularly in light of the highly competitive offerings of our close competitor, the UK.

(b) Pension Levy

Our members have expressed some concern with the provisions included in the Finance Bill to increase the Pension Levy to 0.75% for 2014 and to extend it beyond 2014 (when it had been scheduled to end) and into 2015 at a rate of 0.15%.

The concern arises from the following commitment given in the Budget 2013 speech:

"I want to clarify this Government's policy on a number of important issues…The Pension Levy announced as part of the Jobs Initiative will not be renewed after 2014".

In responses to parliamentary questions, the Pension Levy has been repeatedly referred to as "temporary", and the response to a question on 7 May 2013 stated that *"[t]he levy will operate for a period of 4 years only (2011 to 2014) and the legislative provisions giving effect to the levy (section 4 of Finance (No 2) Act 2011) were specifically drafted to reflect this".*

The feedback from our members is that the change in Budget 2014 to extend the levy into 2015 has resulted in uncertainty among those currently making prudent pension contributions. The increase in, and extension of, the Pension Levy will further reduce the value of the funds to which workers have contributed throughout their working lives and will further decrease the pension income of retirees.

Therefore, we would welcome a strong commitment that no further extensions in this levy will be implemented.

(c) Retirement relief – leased land

Section 41 of the Bill introduces amendments to retirement relief in relation to disposals of leased land. We have highlighted the concerns of some of our members that the section in the Bill as initiated brought a disposal of leased land to a child into the lower "disposal outside the family" caps set out in section 598 TCA 1997 instead of the current section 599 caps for disposals to children.

We therefore welcome the proposed Committee Stage amendment which ensures that the existing relief, i.e. relief under section 599, for disposal of leased land to a child is retained.

(d) Capital gains tax – amendment to section 552 TCA 1997

Section 40 of the Bill provides for amendments to the allowable acquisition or enhancement cost for capital gains tax purposes where borrowed money is used to acquire or enhance the asset and the debt is subsequently released.

We believe it would be worth reviewing the following aspects of this measure:

(a) The provision applies to a debt release where the asset has already been disposed of in 2013 or earlier. We believe it would be more equitable to make the provision effective only where the asset funded by the debt is disposed of from 1 January 2014 onwards.

(b) It appears that the provision would apply in a situation where a portion of a debt, which had been parked for an extended period of time (say, 15 to 20 years) under a debt resolution agreement, is eventually released if the borrower is still unable to pay. We believe it would be worth considering a cut-off period, after which time the release of the debt would no longer be taxable.

(c) It would appear difficult to apply the provision in the context of a debt buy-back at a discount. In many cases it can be difficult to determine what, if any, part of the funds raised were applied towards base cost of a chargeable asset. Perhaps this issue could be clarified by way of Revenue e-Brief.

(d) The wording of the section is unclear in relation to a debt release arising in the year following the date of disposal but before the filing of the tax return containing the computation of the gain. We believe that the taxpayer should have the option to treat the amount of the release in this situation as either a reduction in the base cost of the asset disposed of, or as a chargeable gain for the year of the release.

We welcome the proposed Committee Stage amendments to address issues which we raised on behalf of our members in relation to the section's application in the following scenarios:

- Where a write-off of intercompany debt could have given rise to a capital gains tax liability even though there had been no benefit to the group as a whole, and
- Where a release of a debt in a year later than an exempt disposal to which it related may not have taken on the exempt status of the disposal.

(e) Relief on loans applied in acquiring interest in partnerships

Section 3 of the Bill abolishes the interest relief in section 253 TCA 1997 for loans applied in acquiring interest in partnerships, with effect for loans made after 15 October 2013. Our members raised some practical issues in relation to application of these provisions to replacement loans. We therefore welcome the proposed clarification at Committee Stage of the Bill that the relief will continue to be available in respect of replacement loans drawn down after 15 October 2013.

(f) VAT

Section 58 of the Bill introduces a measure which requires businesses that do not pay their suppliers within a certain 6 month period to repay the input VAT previously claimed.

When the Minister announced the measure in Budget 2014, it was proposed as one of a number of VAT "anti-fraud measures". In the Second Stage speech for the Bill the Minister described the measure as an "anti-avoidance measure". However, as drafted, section 58 has a much broader application, requiring all taxpayers who meet the conditions of the section to adjust their input VAT or individually satisfy Revenue that there are "reasonable grounds" for not having paid.

While section 59 of the Bill entitles Revenue to make Regulations as to the circumstances in which an adjustment is not required, nothing in section 58 makes the obligations of that section subject to these regulations. As such it is not clear how Revenue will deem a taxpayer not to fall within the scope of the section.

We are liaising with Revenue directly for clarification on the application of Section 58 vis-à-vis intra-community acquisitions of goods and "reverse charge" services.

We are also engaging with Revenue on section 57 of the Bill to seek clarification on the scope and application of the provision whereby input VAT would be denied in a "transfer of business" scenario.

Issue previously raised – interaction of USC surcharge on property reliefs and High Earners' Restriction

Finally, we wish to reiterate an issue which we raised with your officials prior to the publication of the Finance Bill, which relates to the interaction of the property reliefs Universal Social Charge (USC) surcharge and the High Earners' Restriction.

Finance Act 2012 introduced Section 531AAE TCA 1997 which imposes an additional 5% USC liability on an individual with aggregate income of €100,000 or more where the individual uses certain property or area-based incentive reliefs.

The legislation provides that this 5% "property reliefs surcharge" applies to the amount of reliefs used in respect of a tax year. Section 531AAE(2) notes that the reference to relief being used in respect of a tax year *"shall be a reference to that part of that specified property relief to which full effect has been given for that tax year"*.

It came to the Institute's attention that there are differing interpretations as to how the surcharge should be applied in cases where the High Earners' Restriction (HER) applies.

We raised this matter with Revenue at TALC to obtain their view. Revenue's view is that the "property reliefs' surcharge" does not take account of any restriction imposed by the HER. Revenue stated that the restriction under Chapter 2A of Part 15 TCA 1997 (the HER) does not reduce the amount of any of the specified reliefs claimed by a taxpayer but rather restricts the taxpayer's ability to reduce their taxable income below a certain amount. This is done by increasing the taxable income rather than by adjusting the amount of reliefs claimed. Therefore, in Revenue's view the application of the HER does not affect the amount of reliefs to which 'full effect' has been given – "full effect" has been given to a property relief if there is sufficient income to absorb the claim.

In practice, this interpretation gives rise to situations in which the USC surcharge is applied to income which, due to the application of the HER, has not in fact been sheltered through the use of property reliefs.

We would welcome a clarification in Finance (No.2) Bill 2013 that the surcharge will only apply to income sheltered after taking account of the restrictions imposed under the HER.

We are available to you and your officials for any further information and consultations which you may require in relation to the issues raised above.

Yours truly

Helen O'Sullivan

President

Irish Tax Institute