Irish Tax Institute – Fantasy Budget 2019

DCU – JK4RL

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Introduction

The following is our analysis of some of the impacts that Budget 2019 will have on: the individual and family, indigenous Irish business and foreign direct investment. We finish with a proposal outlining why we feel a revision of the Entrepreneur Relief is necessary.

Individual/Family

One key measure was the increase in income thresholds for the Affordable Childcare Scheme. This measure sees an increase in the base income and maximum income thresholds that qualify for childcare subsidies.

Over the past number of years childcare costs have become increasingly burdensome to families. Larkin (2018) highlights how the average cost of childcare breaks down to €177.92 a week for full-time and €101.82 a week for part-time care. From these figures it is clear that the €20 default universal childcare payment received by families isn't sufficient.

Murphy (2018) notes that "as a percentage of wages, net childcare costs in Ireland are the highest in the European Union" - this stands at almost "23% of the full-time earnings of a couple". Furthermore, dual-income households may decide that it would be cheaper to have one spouse stay at home with their children. They could incur fewer childcare costs and could avail of the Home Carer's tax credit which has been increased to €1500 a year in Budget 2019 (Reddan, 2018).

Childcare costs have become a real obstacle especially for women, who after childbirth, have to consider the financial viability of returning to work because of childcare costs. Lone parents and low-income families are exposed most to this situation and Murphy (2018) describes how two-thirds of lone parents and 70% of couples, with pre-school aged children, who work full-time rely on non-parental childcare.

It's crucial that this new measure allows 7,500 children to qualify for the scheme for the first time and another 40,000 to receive improved subsidies (Reddan, 2018).

The key changes to the Affordable Childcare Scheme in Budget 2019:		
	2019	**2018**
Base Income Threshold	€26,000	€22,700
Maximum Income Threshold	€60,000	€47,000
Multiple Child Deduction	€4,300	€3,800

As a result of these changes more couples will receive greater subsidies including those qualifying for the full subsidy of €220 a week per child. Reddan (2018) gives several examples:

Example 1: A lone parent with net income of €26,000 with one child aged two years that needs 40 hours of childcare per week, will see their subsidy rise from €148 a week to €175 a week, or €700 a month.

Example 2: A family of four with net income of €47,500 who were previously only entitled to €52 per week will receive €128 under the new proposals, saving them €304 a month.

The National Council for Women in Ireland declared that the lack of affordable and accessible childcare is "one of the biggest barriers to women's employment and participation in public life" (RTE, 2018), and the new measures should assist in providing accessible childcare to a greater number of families and encouraging more women to return to work. This shows that the Government recognises a real need to support people in looking after their children.

Indigenous Irish Business

With Brexit looming, indigenous Irish businesses, both in the SME and agri-business sectors, are some of the most likely stakeholders to be impacted. According to the CSO (2018), Irish businesses exported approximately €16.4 billion worth of goods last year to the UK, making it the country's largest EU trading partner. However, Brexit could potentially severely disrupt these trading relationships, with the introduction of tariffs and non-tariff barriers such as border checks along the Irish border (Burke-Kennedy & Hilliard, 2018).

In his speech, the Minister acknowledged that "SMEs provide most of our employment and additional Government support for this sector is crucial in light of Brexit" (Fine Gael, 2019). As a result, the Minister announced the launch of a Future Growth Loan Scheme - which will be available to "eligible Irish businesses and the primary agriculture and seafood sectors to support strategic long-term investment in a post Brexit environment" (Moran, 2018).

Expected to be introduced in early 2019 and run for a period of three years following its launch, the initiative will make €300 million worth of loans available to eligible businesses- these include SMEs and businesses operating in the primary agriculture and seafood sectors (DBEI, 2018), with 40% of the €300m fund earmarked specifically for the agri-food sector (Cummins, 2018).

According to the DBEI (2018), any loans taken out by eligible businesses under the scheme must be used for capital expenditure purposes such as:

- Investment in tangible/intangible assets
    - related to process and organisational innovation or;
    - on agricultural holdings linked to primary agricultural production.

Furthermore, while the approval of any loans will be dependent on the credit policies and procedures of participating finance providers, some of the expected loan terms include:

- "Minimum borrowing of €100,000 for SMEs or €50,000 for businesses in primary agriculture.
- Maximum loan amount of €3,000,000.
- Loans available for periods of 8-10 years.
- Loans of under €500,000 to be made on an unsecured basis" (DBEI, 2018).

The Minister for Business, Enterprise and Innovation, Heather Humphreys, noted that the scheme will provide many businesses with an opportunity to avail of loans for longer terms than the seven years which financial institutions usually lend up to. She also noted that the interest rates on the loans will be "very competitive" and "well below 5%" (Cummins, 2018). Meanwhile, Michael Creed, the Minister for Agriculture, Food and the Marine aired his belief that the initiative will fill "a gap in the market" (O'Sullivan, 2018) and will be particularly beneficial for "young farmers who may not have a long-established banking record" (Cummins, 2018). Additionally, Lorraine Griffin (2018), Head of Tax at Deloitte, further

pointed out the new scheme should provide Irish exporters with "greater supports to develop new markets" and assist in dealing with any "future Brexit shocks".

Overall, we believe the scheme is evidence of the Government's determination and commitment to ensure that Irish businesses are protected from the potential adverse effects that Brexit may offer, particularly to those heavily reliant on the UK as an export market.

Foreign Direct Investment

Foreign Direct investment (FDI) is imperative to the Irish economy. Many see FDI as one of the main factors which has contributed to helping Ireland's economic recovery in recent years and to be fuelling Ireland's current economic growth (Chartered Accountants Ireland, 2017). Therefore, it is in the government's best interest to keep a steady stream of FDI coming into Ireland.

Ireland's low corporation tax rate of 12.5% has been recognised by many as one of the key factors which has led to such high levels of FDI in the country. AIB listed corporation tax as one of the 4 main reasons that companies choose to locate in Ireland (AIB, 2014). The government evidently recognises the importance of the low rate in maintaining high levels of FDI in the country by leaving it unchanged in Budget 2019. This will be reassuring to foreign investors in Ireland and may also attract further investment.

The government did however introduce an exit tax, which became effective on the 10th of October, well before the ATAD (Anti-Tax Avoidance Derivative) deadline of January 1st, 2020 (under article 5) (Duffy and Bailey, 2018). This 12.5% rate applies to any unrealised gains arising from transferring assets abroad "such that they leave the scope of Irish tax" and applies to all companies without exception (Quinn et al, 2018). It also represents a reduction from the 33% exit tax rate that only applied to companies with an Irish tax residency who wished to change residency.

It will come as welcome news that the announced rate is the same as our low corporation tax and not the 33% originally feared (McDonald, 2018). The overnight introduction will also

provide Irish-based businesses and potential foreign investors with certainty as to "the rate of tax on exit" (Reilly, 2018).

In other respects, the new regime may dissuade MNCs from restructuring and moving assets, like Intellectual Property, to benefit from the new 13.125% tax on foreign derived intangible income introduced in the US (Gulliver, 2018). Furthermore, the EU and ATAD had been applying pressure on Ireland to close certain tax loopholes and having the government implement it now may stabilise Ireland's relationship with the EU with regard to tax (Crowe, 2018).

There are also potential negative impacts associated with the introduction of the exit tax. The Minister's quick introduction and implementation of the tax may be viewed unfavourably by foreign investors as it shows a degree of unpredictability from the Government and creates uncertainty around future tax policy changes which may deter future FDI. It also comes at a time when competitors for FDI, such as Malta and Luxembourg, are aggressively defending their tax policies and should they succeed, this could see a significant drop in foreign investment into Ireland (Crowe, 2018).

Proposal

While Budget 2019 announced the launch of the Future Loan Growth scheme and changes to the Key Employee Engagement Programme, we believe that more could be done to encourage entrepreneurship within the Irish economy.

Ireland's current capital gains tax (CGT) rate of 33% is the third highest in the OECD and 13% higher than the median (Gunnell, 2018). The Tax Strategy Group (TSG) (2018) note that due to globalisation, capital has become "highly mobile" meaning high capital taxes can reduce the international competitiveness of a particular tax system and reduce the number of "job creating investments". Furthermore, high CGT rates can encourage asset holders to hold them longer than required rather than sell them and use the proceeds to fund further entrepreneurial opportunities.

Therefore, we feel that Minister Donohue should consider a further revision of the Entrepreneur Relief currently in place. Following revisions of the scheme by Finance Acts 2015 and 2016, it provides for the application of a reduced 10% rate of CGT on chargeable

gains made by qualifying individuals on the disposal/part-disposal of qualifying business assets up to a lifetime limit of €1 million (Revenue, 2018).

However, the Irish relief is uncompetitive by international standards. While the British Entrepreneurs' Relief also stands at 10%, the lifetime threshold is instead cut-off at £10 million (Byrne, 2018). For example, where a 10% rate applies to a gain of £7.5m in the UK, the effective rate in Ireland on a similar gain of €7.5m would be 29.93%.

Entrepreneurs' Relief - Ireland vs UK

	Ireland	UK
Gain on disposal of qualifying business assets	€7.5m	£7.5m
£7.5m @ 10% (UK)		£0.75m
€1m @ 10% (Ireland)	€0.1m	
€6.5m @ 33% (Ireland)	€2.145m	
Total CGT payable on disposal gains	**€2.245m**	**£0.75m**

As Lynch and Newman (2018) note, this means that once the limit has been reached, "the entrepreneur takes the risk and creates employment, but the state takes 33% of the upside" on the remaining balance.

A key consideration is whether Irish entrepreneurs see the current limit as equitable in relative terms compared to the UK scheme. A survey by Deloitte (2017) shows that 90% of Irish entrepreneurs "stated that the relative attractiveness of the UK entrepreneur relief would make Irish entrepreneurs more likely to set up and base their operations in the UK". This could see entrepreneurs selling their Irish businesses and relocating to the UK where they could have 90% of future disposal gains - subject to the £10m limit - available to fund any future ventures.

As a result, we believe that raising the lifetime limit to around the €10m-€15m mark, like the UK, would significantly improve the likelihood that entrepreneurs, who establish successful businesses within Ireland, are incentivised to remain here as they could retain and reinvest a higher proportion of disposal proceeds as capital in setting up additional businesses. Equally, this would improve the international competitiveness of our current Entrepreneur Relief which could attract further investment and business from foreign entrepreneurs, particularly

those from the UK, as Ireland would be offering a similar scheme, with an additional potential post-Brexit benefit of access to the European Single Market.

According to the TSG (2018), an increase in the limit to €10m or €15m would cost the Exchequer €54m or €56m per annum respectively, however we believe that the long-term benefit of the scheme to the overall economy would outweigh the cost as the business/economic activity and employment opportunities created by new entrepreneurial ventures would in turn generate greater tax revenues (e.g. VAT and income tax) for the Government.

Conclusion

In conclusion, we believe the main points of Budget 2019 are:

- Welcome changes to the Affordable Childcare Scheme should assist families that are struggling with childcare costs.
- The launch of a €300 million Future Growth Loan scheme should improve the ability of indigenous firms in the SME and agri-business sectors to deal with the potential impact of Brexit.
- The unexpected overnight introduction of the 12.5% exit tax may bring potential benefits and drawbacks to attracting and retaining FDI.

Lastly, we believe that increasing the Entrepreneur Relief lifetime limit to €10m or €15m would improve its international competitiveness, incentivise serial entrepreneurship and generate future Government revenues.

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