Irish Tax Institute

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Pre-Finance Bill 2024 Submission

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About the Irish Tax Institute

The Irish Tax Institute is the leading representative and educational body for Ireland's Chartered Tax Advisers (CTA) and is the country's only professional body exclusively dedicated to tax.

The Chartered Tax Adviser (CTA) qualification is the gold standard in tax and the international mark of excellence in tax advice. We benchmark our education programme against the very best in the world. The continued development of our syllabus, delivery model and assessment methods ensure that our CTAs have the skills and knowledge they need to meet the ever-changing needs of their workplaces.

Our membership of over 6,000 is part of the international CTA network which has more than 32,000 members. It includes the Chartered Institute of Taxation UK, the Tax Institute of Australia, the Taxation Institute of Hong Kong, and the South African Institute of Taxation. The Institute is also a member of the CFE Tax Advisers Europe (CFE), the European umbrella body for tax professionals.

Our members provide tax services and business expertise to thousands of Irish owned and multinational businesses as well as to individuals in Ireland and internationally. Many also hold senior roles in professional service firms, global companies, Government, Revenue, state bodies and in the European Commission.

The Institute is, first and foremost, an educational body but since its foundation in 1967, it has played an active role in the development of tax administration and tax policy in Ireland. We are deeply committed to playing our part in building an efficient and innovative tax system that serves a successful economy and a fair society. We are also committed to the future of the tax profession, our members and our role in serving the best interests of Ireland's taxpayers in a new international world order.

Irish Tax Institute - Leading through tax education

Executive Summary

The Irish Tax Institute has set out in this submission a number of legislative amendments for consideration in the drafting of Finance Bill 2024 in the following four key areas:

1. Support the growth of the indigenous sector
2. Enhance Ireland's competitiveness
3. Tax technical issues arising from the implementation of Pillar Two
4. Tax technical measures required to mitigate certain unintended consequences

Support the growth of the indigenous sector

Ensure existing tax reliefs for SMEs meet their policy objective

Effective tax measures for SMEs have a significant role to play in building an innovative and productive indigenous sector which can in turn mitigate the risk of over-reliance on the multinational sector.

We welcome the establishment of the new Sub-committee of the Tax Administration Liaison Committee (TALC) on the Simplification and Modernisation of Business Reliefs for SMEs following the announcement by the Minister for Finance in last year's Budget. The Institute has been an active participant throughout the group's deliberations and looks forward to the delivery of the sub-committee's report to Main TALC in the coming weeks.

Furthermore, we welcome the commitment given by Minister McGrath at the Institute's Annual Dinner last February that any proposals from the sub-committee which would require legislative change will be considered as part of the normal Finance Bill process.

We have outlined in the body of this submission, the legislative and administrative reforms which we believe are necessary to maximise existing tax reliefs to encourage investment in SMEs, make them more accessible to smaller businesses and ensure the measures achieve their policy objective.

Impose proportionate sanctions for administrative errors

While the Institute recognises the role of penalties in encouraging compliant behaviour by taxpayers, it is essential that the penalties which apply for a failure to comply with a tax rule are appropriate. There are instances in our tax code where the penalties that apply for non-compliance have a disproportionate impact on certain cohorts of taxpayers which can undermine the objective of the underlying tax measure.

In our view, the penalties which apply for errors by taxpayers in complying with the requirements of the new Enhanced Reporting Requirements (ERR), the Employment Investment Incentive (EII), the Key Employee Engagement Programme (KEEP) and the Special Assignee Relief Programme (SARP) are disproportionate and should be reconsidered.

Reduce the CGT rate

The tax that matters most to investors is capital gains tax (CGT) and the Irish CGT headline rate, at 33%, is one of the highest in Europe. This rate has remained unchanged since it was increased during the financial crisis. In our view, a reduction in the rate to 25% for active business assets would encourage investment which in turn would lead to innovation and productivity in the indigenous sector as well as increasing the yield.

Enhance Ireland's competitiveness

Simplify the corporation tax code

The Institute welcomed the publication of the Feedback Statement on a Participation Exemption for Foreign Dividends which set out a Strawman Proposal for the key structural elements of the participation exemption for foreign dividends. In our response[1] to the Feedback Statement, we highlighted a number of aspects of the proposal which we believe should be reconsidered such as the limited geographic scope and the effective date for the participation exemption.

As work on drafting the legislation for the participation exemption progresses, an iterative process of consulting with stakeholders will help ensure the exemption can achieve its objective of providing much-needed administrative simplification and greater certainty for businesses. In this regard, we welcome the establishment by the Department of Finance of a dedicated subgroup to facilitate technical discussions with the Institute and other stakeholders. We note the intention to publish a second Feedback Statement in mid-2024 and we urge that this timeframe is adhered to so that stakeholders have sufficient time to fully consider the impact of the proposed legislative provisions.

The Feedback Statement notes that the policy consideration of the merits of a foreign branch exemption are not yet as fully developed and further engagement with stakeholders on this matter is expected in 2024. As Ireland does not have a branch exemption at present, there can be significant differences in the timing and measure of taxable income for Irish companies between the head office and branches resulting in tax uncertainty and complexity. If Ireland is to remain an attractive location for foreign direct investment (FDI), a foreign branch exemption should be introduced in Finance Bill 2024 in tandem with the participation exemption for foreign dividends.

We welcome the ongoing review by the Department of Finance of the interest deductibility rules. We note that the review is likely to be a multi-year project and we urge that a clear timeline is provided for the completion of the project including the implementation of reforms of the interest deductibility rules on foot of that review. The ATAD Interest Limitation Rule (i.e. 30% of EBITDA ratio rule), introduced in Finance Act 2021, was simply layered on top

[1] Irish Tax Institute Response to the Feedback Statement on a Participation Exemption for Foreign Dividends, May 2024

of existing comprehensive interest deductibility provisions. As a consequence, Ireland now has one of the most complicated and onerous interest deductibility regimes within the EU.

It is critical that a clear policy decision is taken at the outset of the review to overhaul the interest deductibility provisions to ensure Ireland permits a broad base for a deduction of interest against both trading and non-trading income, using the protection of the ATAD Interest Limitation Rule against base erosion risks. This would ensure that Ireland's interest deductibility rules are easier to administer and more in line with the measures contained in the corporate tax systems of our European counterparts.

Consideration should also be given to removing Ireland's schedular tax system and different corporation tax rates. The trading and non-trading distinction between the 12.5% trading rate and passive 25% rate creates unnecessary complexity within the Irish corporation tax code, which businesses do not have to contend with in other tax systems.

Reduce the marginal cost of employment for businesses and individuals

The Irish personal tax system is strongly progressive, and the tax and social welfare systems combined contribute substantially to the redistribution of income and to the reduction of income inequality. However, Ireland's high marginal tax rates apply at relatively low-income levels by international standards and the country's personal tax base is narrow. In our view, an objective of any long-term strategy aimed at attracting and retaining FDI should include reducing the marginal cost of employment in Ireland for both businesses and individuals.

Share-based remuneration can play an important role in rewarding key employees at all stages of development of a business. It can significantly reduce fixed labour costs and free up business cashflow. Further legislative amendments to the KEEP are needed to improve the feasibility of the scheme. However, there are limitations inherent in its design which inevitably limit its uptake. Consequently, it is important that the significant obstacles to the use of other types of share-based remuneration by SMEs and start-ups are dealt with such as addressing the upfront tax cost faced by employees on the receipt of a share award or on the exercise of a share option.

For larger companies, given the high cost of employment in Ireland, it is vital that the benefits associated with existing share-based remuneration schemes are retained. Furthermore, it is essential that the complexity and administrative burden associated with operating such schemes in Ireland is minimised.

Introduce targeted tax measures to promote sustainability

Robust climate action policies, including supports for the green agenda and sustainability, have become key considerations for investors. Many jurisdictions are using tax incentives to support businesses in reducing their carbon emissions and to attract investment in green enterprises. In our view, Ireland's offering in this regard does not compare favourably with competitor jurisdictions.

We firmly believe that consideration must be given to tax measures which would support businesses in reducing their carbon emissions. The introduction of tax measures targeting the green agenda would assist the country in achieving its climate change targets.

Tax technical issues arising from the implementation of Pillar Two

Following the transposition of the EU Minimum Tax Directive, to implement the Pillar Two Global Anti-Base Erosion (GloBE) Rules into Irish law in Finance (No.2) Act 2023, a number of issues which require clarification have been identified arising from the application of the GloBE Rules in relation to deferred tax assets on losses. We understand from discussions with Revenue at the TALC BEPS Sub-committee that clarification of these issues would necessitate an amendment to the Irish legislation implementing the GloBE Rules. We have outlined these issues in more detail in the body of this submission.

Tax technical measures required to mitigate certain unintended consequences

Arising from recent legislative changes, we have identified several tax technical measures which, in our view, require a legislative amendment in order to mitigate certain unintended consequences. These have been set out in the body of the submission.

Conclusion

We have outlined the Institute Recommendations in more detail on pages 8 - 17. Further detailed analysis of each technical matter mentioned above has also been included in the body of this submission. Please contact Anne Gunnell at agunnell@taxinstitute.ie or (01) 6631750 if you require any further information regarding the matters raised in this submission.

Institute Recommendations

Our recommendations for Finance Bill 2024 are grouped into four broad areas below. Further detailed analysis on each technical matter has been included in the body of the submission.

Support the growth of the indigenous sector

Ensure existing tax reliefs for SMEs meet their policy objective

EII

1. We believe the following legislative and administrative changes are necessary to ensure the EII scheme can fulfil its policy objective of supporting the growth of indigenous business:

   Legislative Recommendations

   - Remove the exclusion of holding company structures.
   - Amend the employment conditions.
   - Apply more proportionate monetary sanctions for administrative errors or the late filing of a return.
   - Provide a carve-out from the connected party rule linked with a control test.
   - Recognise additional exit strategies for EII investors.
   - Allow the offset of capital losses.

   Administrative Recommendations

   - Commit appropriate and adequate resourcing to the administration of EII.
   - Provide a streamlined EII administrative process for small and micro companies.
   - Reduce duplication of administration under the EII.
   - Provide separate Tax and Duty Manuals (TDM) for each relief in Part 16 of the Taxes Consolidation Act (TCA) 1997.

Start-up Capital Incentive (SCI)

2. We believe the following measures are necessary to ensure the SCI scheme can fulfil its policy objective of supporting the growth of indigenous business:

   Legislative Recommendations

   - Review the narrow criteria of the SCI scheme.
   - Review the penalties imposed under the SCI scheme which are disproportionately high.

Administrative Recommendations

- Raise awareness of the SCI scheme by enhancing the information available on the Revenue website.
- Revenue guidance on the SCI scheme should be contained in a separate TDM for ease of reading rather than as part of a TDM on all reliefs contained in Part 16 of the TCA 1997.

Start-up Relief for Entrepreneurs (SURE)

3. The SURE income tax refund scheme for those who start their own business is restricted to former PAYE workers. In our view, the following measures are necessary to ensure the SURE can fulfil its policy objective of supporting the growth of indigenous business:

   Legislative Recommendation

   - Extend the SURE scheme to include new business founders who were previously self-employed and starting up a new business.

   Administrative Recommendation

   - Revenue guidance on the SURE scheme should be contained in a separate TDM for ease of reading rather than as part of a TDM on all reliefs contained in Part 16 of the TCA 1997.

R&D Tax Credit

4. We believe the following legislative and administrative changes are needed to encourage increased investment in R&D and innovation in Ireland:

   Legislative Recommendations

   - Condense the 3-year R&D Tax Credit payment schedule to one year for SMEs.
   - Align the definition and criteria for R&D grants given by IDA Ireland and Enterprise Ireland which include innovation with the R&D Tax Credit.
   - Increase the limits for outsourcing.
   - Allow rent to qualify as R&D expenditure.
   - Incentivise green or energy related R&D.

   Administrative Recommendations

   - Increase the limit for Revenue's streamlined R&D validation process for small and micro companies.

- Provide a pre-approval process for first-time R&D Tax Credit claims by small and micro companies.
- Simplify the documentation requirements for R&D Tax Credit claims by SMEs.
- Amend Revenue guidance on agency staff.
- Develop SME-friendly Revenue guidance on sector specific R&D issues.
- Ensure Revenue Compliance Interventions are proportionate and conducted in a timely and efficient manner.
- Increase transparency over Revenue's R&D technical experts.
- Ensure stakeholders are consulted in advance of updates to Revenue guidance.

Tax Relief for New Start-up Companies

5. The tax relief for new start-up companies in their first three years of trading in section 486C TCA 1997 is linked to the amount of Employers’ PRSI paid by a company in an accounting period. We recommend the following changes are made to ensure the relief can fulfil the policy objective of supporting the growth of start-ups:

   Legislative Recommendation

   - The link to Employers’ PRSI should be removed as it acts as a significant barrier to start-up companies availing of the relief.

   Administrative Recommendation

   - Awareness of the relief in section 486C TCA 1997 is low and could be increased by enhancing the information available on the Revenue website.

Transfer of a business to a company

6. Relief under section 600 TCA 1997 on the transfer of a business to a company applies by deferring chargeable gains on the transfer of a business as a going concern to a company and all assets of the business must transfer. We believe Revenue guidance on the meaning of ‘bona fide trade creditors’ for the purpose of the relief should be updated as we consider Revenue has adopted a narrow interpretation of the legislation which essentially precludes businesses with any degree of leverage with legitimate business liabilities, from availing of the relief in full.

KEEP

7. Several amendments were made to the KEEP in Finance Act 2022 which came into operation by Commencement Order on 20 November 2023. We believe more legislative and administrative changes are needed to ensure KEEP can achieve its policy aim of helping SMEs attract and retain key employees. These include:

   Legislative Recommendations

- Impose a proportionate sanction for undervaluing share options.
- Amend the definition of a ‘qualifying holding company’.
- Remove the annual emoluments cap from the qualifying share option limits.
- Allow for the continuation of the relief should the SME undergo a corporate reorganisation during the period in which the KEEP share option rights are outstanding.
- Provide for ‘roll over relief’ of KEEP share options.

Administrative Recommendation

- Provide a Revenue agreed ‘safe harbour’ for share valuations.

Accelerated Capital Allowances for Energy Efficient Equipment

8. We believe the following changes are needed to the existing accelerated capital allowances regime for Energy Efficient Equipment (EEE) as it is administratively difficult to operate and limited in scope:

    - Widen the scope of the relief beyond EEE to whole buildings that receive a recognised accreditation for overall energy performance.
    - Remove the condition that the equipment must not be leased, let, or hired, as this precludes landlords and lessors from availing of the relief.
    - Introduce a tax credit for companies which can be monetised where the company is loss-making for the element of the loss generated by the accelerated capital allowances claim.
    - Introduce an enhanced rate of relief above the current 100% first-year allowance.
    - Simplify the process required to add new products to the approved list.

Revised Entrepreneur Relief

9. We believe the following legislative and administrative changes are needed to Revised Entrepreneur Relief to ensure it can meet its policy objective of supporting entrepreneurship:

    Legislative Recommendations

    - Broaden the definition of a holding company.
    - Remove the restriction on relief where a group holds a dormant company.
    - Remove the restriction on relief where a group has a shareholding in a joint venture company of less than 51%.
    - Allow claims for relief where EII funds have been raised by a company.

Administrative Recommendations

- Allow the relief to apply on the liquidation of a holding company following sale of the trading subsidiary.
- Amend the working time requirement in particular for non-group companies.
- Allow apportioning of the relief where a company/ group holds investments or leases trading premises.

Relief for Investment in Innovative Enterprises

10. It is critical that the certification process for the new Relief for Investment in Innovative Enterprises (Angel Investor Relief) is made as simple as possible for SMEs. Given this scheme operates under the General Block Exemption Regulation (GBER), we urge that lessons are learned from the complexities encountered in the administration of the EII and are avoided where possible in the roll-out of this new scheme.

CGT Share Buyback Relief

11. The CGT Share Buyback Relief would be enhanced if a *bona fide* test is inserted in section 135(3A) TCA 1997 to provide certainty for taxpayers when selling shares in closely held companies. In our view, inserting an exclusion for *bona fide* commercial transactions into section 135 TCA 1997 would provide much needed certainty to taxpayers and their advisers, when implementing transactions involving the disposal of shares in a company with cash on its balance sheet. In addition, Revenue guidance on situations where a vendor who is retaining a connection with the company can meet the "trade benefit test", in our view goes beyond the legislative requirements in section 178 TCA 1997 and should be updated.

Small Benefit Exemption

12. We believe increasing the number of permissible benefits under the Small Benefit Exemption in section 112B TCA 1997, so that the €1,000 limit applies to the cumulative value of the incentives received by an employee in the year of assessment (rather than the first two received), would ensure the exemption operates as intended. The amendments made in Finance Act 2022 to the section were intended to provide employers with greater flexibility to grant tax-free non-cash rewards to their employees up to a maximum of €1,000. Where the €1,000 limit is exceeded, the portion of any benefit received in excess of the limit should be subject to benefit-in-kind (BIK).

Proportionate sanctions for administrative errors

ERR

13. A fixed penalty of €4,000 applies where an employer inadvertently omits to report, in real time, a non-taxable benefit or expense reimbursed to their employee under the ERR regime. In our view, this penal sanction for failing to comply with a reporting requirement in real time is wholly disproportionate and places an inordinate burden on

smaller businesses that have limited resources. We urge that the level of penalty be reviewed and replaced with a more appropriate sanction.

EII

14. Administrative errors or delays in the certification and reporting process for EII can result in a full clawback of the relief on the fundraising company. This is disproportionate to the error and can act as a disincentive for companies to avail of EII. We believe it would be more proportionate for a monetary penalty to be imposed as the sanction for an administrative error or the late filing of a return, rather than a clawback of the entire EII relief.

KEEP

15. If share options are not granted for market value, the options do not qualify as KEEP options under section 128F TCA 1997, resulting in no exemption from income tax, USC and PRSI on exercise. Where options are granted at an undervalue within say a certain percentage of the Revenue determined value (for example, 75%), we believe that a more proportionate sanction would be for a charge to income tax to arise on the exercise of the options on the difference between the market value at the date of grant and the option price.

SARP

16. We believe the 90-day timeframe for the employer to certify and submit the Form SARP 1A to Revenue should be removed from the legislation or, at a minimum, it should be removed from the part of the legislation that defines a 'relevant employee'. This would ensure that the automatic 'penalty' in the refusal of the SARP relief to an employee arising from an employer failing to lodge the notice within 90 days of arrival, would not arise.

Reduce the CGT rate

17. Ireland's headline rate of CGT, at 33%, is high by international standards. In our view, a reduction in the rate to 25% for active business assets would encourage innovation and productivity in the indigenous sector as well as increasing the yield.

Enhancing Ireland's competitiveness

Simplify the Irish corporation tax code

18. In conjunction with the introduction of a participation exemption for foreign dividends, Ireland should adopt a foreign branch exemption which applies automatically, with taxpayers given the option to elect out of the exemption on a branch-by-branch basis. Where an election is made to opt out of the exemption, the branch should remain taxable under the current system.

19. It is critical that a clear policy decision is taken at the outset of the current review of Ireland's interest deductibility rules to overhaul the legislative provisions, to ensure a broad base for deduction of interest against both trading and non-trading income is permitted, using the protection of the ATAD Interest Limitation Rule against base erosion risks. This would ensure that Ireland's interest deductibility rules are easier to administer and more in line with the measures contained in the corporate tax systems of our European counterparts.

20. Consideration should be given to removing Ireland's schedular tax system and different corporation tax rates. The trading and non-trading distinction between the 12.5% trading rate and passive 25% rate creates unnecessary complexity within the Irish corporation tax code, which businesses do not have to contend with in other tax systems.

Reduce the marginal cost of employment for both businesses and individuals

21. An objective of any long-term strategy aimed at attracting and retaining FDI should include reducing the marginal cost of employment in Ireland for both businesses and individuals. We believe reducing the marginal rate of income tax (including social insurance contributions) would help to attract highly skilled and mobile labour to Ireland.

22. In addition to our recommendations on the KEEP (outlined above), we believe the following reforms[2] should be implemented in respect of the taxation of share-based remuneration in Ireland:

    Legislative Recommendations

    - Introduce measures to address the difficulties faced by employees in funding the upfront tax cost arising on the exercise of a share option or receipt of a share award. Deferring the tax arising until such time as the employee is permitted to dispose of the shares would mean that the employee is able to fund the tax arising. Alternatively, the removal of the BIK charge on employer loans, or at a minimum reducing the 13.5% interest rate on such loans to a more commercial rate of interest would make share-based remuneration a more viable option for many companies.

    - Consider the disapplication of the share buyback provisions in section 176 TCA 1997 in the context of share-based remuneration as the broad application of these provisions can act as an impediment to companies that wish to incentivise employees using share-based remuneration.

    - Address the limitations inherent in section 128D TCA 1997 by removing the anomaly where restricted shares are exchanged for shares with equivalent

[2] Recommendations made by the Irish Tax Institute in response to the public consultation on Ireland's taxation of share-based remuneration, January 2024.

restrictions and expanding the scope of the section to include instruments other than shares.

- Extend the existing 'sell to cover' provisions in section 985A(4B) TCA 1997 to situations where an employee exercises a right to acquire shares and a taxable gain arises under section 128 which is now subject to PAYE.

- Align the tax treatment of Restricted Stock Units (RSUs) with the rules followed in other OECD countries and the existing Irish tax treatment for share options exercised by non-residents.

- Extend the current filing deadline for employer returns of share awards, which is three months after the year end, by a least a further month, to allow sufficient time for the collation and aggregation of data.

Administrative Recommendations

- Provide clear principle-based guidance on share valuations, including acceptable methodologies and safe harbours, to support companies that offer share-based remuneration to their employees.

- Allow employers to report information on share awards to Revenue via a single annual online return. This would facilitate ease of completion by employers and avoid duplication of reporting.

Targeted tax measures to promote the green agenda and sustainability

23. We believe the following enhancements to existing tax measures and incentives are necessary to improve Ireland's offering to businesses seeking to reduce their carbon emissions and to enhance Ireland's position as a location for sustainable investment:

- Enhance the existing Accelerated Capital Allowances regime for EEE (as outlined above).
- Extend the CGT participation exemption to early-stage renewable energy projects.
- Re-introduce section 486B TCA 1997 and refine the provisions to encourage investment in sustainable projects and build on Ireland's reputation as a hub for sustainable innovation.
- Extend section 81C TCA 1997 (emissions allowances) to cover carbon offsets in the voluntary sector.
- Enhance the EII scheme to encourage investment in high-risk ventures which support green or energy efficient projects.
- Introduce targeted measures for green or energy related R&D activities.
- Extend the scope of the relief available in section 664 TCA 1997 to include solar panel activity to incentivise the leasing of farmland for solar panels which would

expand the generation of renewable energy and assist Ireland in achieving its climate change targets.

Tax technical issues arising from the implementation of Pillar Two

24. In respect of deferred tax assets (DTAs) on losses brought into a Transition Year under section 111AW(2)(c) TCA 1997, a legislative amendment is necessary to allow taxpayers to apply a First In First Out (FIFO) approach when seeking to analyse whether the losses are attributable to a qualifying loss.

25. A legislative amendment is necessary to allow taxpayers the flexibility to elect which loss is used for GloBE purposes where a DTA is recognised on transition in respect of amounts attributable to a qualifying loss (i.e., brought into GloBE at 15%), as well as other tax losses forward (e.g., brought into GloBE at 12.5% with respect to Irish trading losses), in future years when the losses forward are utilised.

26. Pillar Two Rules state that historical Loss DTAs can be uplifted from 12.5% to the 15% rate where the loss is equivalent to a GloBE loss. Where companies determine that a portion of the loss brought forward equates to a GloBE loss and is subsequently recast and there is a portion which does not equate and as such, is not recast, it is not possible to determine which should be used against future taxable income from an Irish tax perspective. We believe clarification should be provided in legislation to allow the DTA that has been recast (i.e. which equates to a GloBE Loss) in such scenarios to be unwound in the first instance.

Tax technical measures required to mitigate certain unintended consequences

27. The clawback provisions in the new section 480C TCA 1997 residential premises rental income relief do not work properly as the clawback is assessable at marginal rates whereas the relief will have been granted at a rate of 20%. It is important that this position is rectified as otherwise it could disincentivise landlords from availing of the relief.

28. The definition of ‘specified amount’ in section 473B TCA 1997 should be amended to ensure that the increase in the amount of the Rent Tax Credit from €500 to €750, and in the case of jointly assessed taxpayer units, from €1,000 to €1,500, for the years of assessment 2024 and 2025, applies as intended.

29. Section 89 Capital Acquisitions Tax Consolidation Act (CATCA) 2003 should be amended so that CAT agricultural relief can apply in circumstances where a beneficiary part farms and part leases the land.

30. Section 623(3) TCA 1997 should be extended to ensure that no clawback applies where there is a merger by absorption followed by a disposal of the Irish subgroup containing the transferee. Where a domestic merger by absorption occurs between two Irish companies in a group, there will generally be a transfer of assets that meets the

requirements of section 617 TCA 1997. Currently, a charge to CGT would arise if there is a subsequent disposal of the Irish subgroup containing the transferee within 10 years of the merger by absorption as the exception to the clawback provision in section 623(3 does not currently apply in those circumstances.

31. The exemption from withholding tax in section 410 TCA 1997 should be extended to address instances where an Irish company is required to apply withholding tax on patent royalty payments to another Irish group company where there is an intermediate holding company located in a double tax treaty country such as the USA or Switzerland.

1. Support the growth of the indigenous sector

1.1. Ensure existing tax reliefs for SMEs achieve their policy objective

Ireland's overdependence on corporation tax receipts from the multinational sector is widely recognised as a significant risk to the economy. The proportion of income tax receipts from these companies also represents a significant risk for the Exchequer. Effective tax measures to support SMEs have a significant role to play in building an innovative and productive indigenous sector which can in turn mitigate the risk of over-reliance on the multinational sector.

During his Budget 2024 speech last October, the Minister for Finance announced that Revenue would establish a dedicated sub-committee of the Tax Administration Liaison Committee (TALC) to identify any opportunities to simplify and modernise the administration of business supports.

The Institute has been an active participant on the new sub-committee which has been examining the tax reliefs available for SMEs at each stage of the business life cycle, i.e., start-up, growth and expansion and possible divestiture or succession. The administrative recommendations of this TALC Sub-committee on the Simplification and Modernisation of Business Reliefs will be delivered to Main TALC in the coming weeks.

We welcome the Minister's commitment at the Institute's Annual Dinner last February, that any proposals from the TALC sub-committee which require legislative change will be considered as part of the normal Finance Bill process.[3]

In April, the Institute made a written submission to the TALC sub-committee outlining the legislative and administrative reforms we believe are necessary to existing tax reliefs to encourage investment in SMEs, make them more accessible to start-ups and ensure they achieve their policy objective. We detail these recommendations in paragraphs 1.1.1 to 1.1.11 below.

We have also included our recommendation for an amendment to the Small Benefit Exemption at paragraph 1.1.12 as it is apparent from discussions between practitioners and Revenue at TALC on the practical application of the new ERR rules, that the current drafting of section 112B TCA 1997 creates an administrative burden which gives rise to unintended consequences.

1.1.1 EII

For early stage and small businesses that have limited financing options, the EII should be an essential source of funding to help them grow and develop. However, contrary to the objective of the scheme, the feedback we continue to receive is that the scheme can

[3] Speech by the Minister for Finance, Michael McGrath TD to the Irish Tax Institute Annual Dinner, February 2024

hamper a company's ability to grow and expand because the rules of the EII do not reflect commercial investment norms.

Whilst the changes introduced in recent Finance Acts have, for the most part, enhanced the scheme, the EII continues to be very complex and burdensome to administer. Finance (No.2) Act 2023 introduced amendments to Part 16 TCA 1997 to reflect amendments to the GBER[4] which has added to the complexity of the scheme.

Further amendments are necessary to ensure the EII can fulfil the policy objective of supporting the growth of indigenous business. We have set out our legislative and administrative recommendations below.

EII Legislative Recommendations

i. Permit holding company structures

The exclusion of holding company structures is causing genuine businesses to be precluded from EII finance. Typically, founder holding companies are established before raising EII finance is even a consideration. These structures are inadvertently borne out of genuine commercial arrangements, sometimes as a result of partnerships or Joint Ventures (JVs) arising from incubator programmes or due to the understanding of founders as to market norms and investor expectations on certain structures. In some cases, the structure can be a legacy from a previous failed venture.

The exclusion of structures which include founder holding companies from the EII is in stark contrast to other funding sources (including Enterprise Ireland and other Government funding) where founder holding company structures are permitted and in fact, are encouraged in certain sectors.

It is our understanding that the GBER, which sets out the conditions which the EII as a State aid must satisfy, does not prohibit holding companies. The restriction appears to stem from rules that pertained to the former Business Expansion Scheme (BES).

ii. Amend the employment conditions

Section 26(b) Finance Act 2021 reintroduced a condition in section 502(5) TCA 1997 regarding increases in employment or expenditure on R&D. The condition must be satisfied three years after the year in which the eligible shares are issued. Failure to satisfy the condition will result in a partial withdrawal of the tax under the scheme.

This condition was removed in 2019 following the removal of second stage relief for shares issued after 8 October 2019. The removal of the condition was in line with the

[4] On 23 June 2023, the European Commission adopted Commission Regulation (EU) 2023/1315 which provided for a targeted amendment to the GBER to help facilitate, simplify and speed up support for the EU's green and digital transitions. Member States had a 6-month transition period to implement the necessary changes to ensure their applicable schemes are compatible with the revised GBER.

stated objective at that time, to increase the efficiency and effectiveness of the scheme. The reintroduction of the condition further adds to the administrative burden and does not take account of the fact that businesses may pivot and change their business models during the interim period.

Section 502(5) TCA 1997 requires an increase in (a) both the number of employees and the total remuneration of employees, or (b) the expenditure on R&D. The requirement to increase both the number of employees and the total remuneration of employees can be problematic and would appear to be contrary to section 496(2)(a) TCA 1997, which states that EII is for the creation or maintenance of employment.

In our view, it would be more appropriate for a company to be deemed to have fulfilled the employment condition if they satisfy either of the tests i.e., an increase in the number of employees under section 502(5)(a) or an increase in total remuneration under section 502(5)(b) TCA 1997.

iii. Impact of non-compliance

Under the existing rules, administrative errors or delays in the certification and reporting process can result in a full clawback of the relief on the fundraising company which is disproportionate to the error in our view. This sanction can act as a disincentive for companies considering using the EII. We believe it would be more proportionate for a monetary fixed penalty to be imposed as a sanction for an administrative error or the late filing of a return, rather than a clawback of the entire EII relief.

iv. Amend the connected party rules

We welcomed the Finance Act 2022 amendment to the connected party rules where the EII investment in a company is made via an investment fund. However, we believe a further amendment to the connected party rules is necessary where the EII investment is made directly in the qualifying company.

The connected party rule limits the ability of early-stage companies to attract strong board membership because shares and share options granted to non-executive directors or other key employees to incentivise them to join the board, are curtailed. Investment by such individuals can be key to developing a business as it means they are committed to its future.

In our view, there should be a carve-out from the connected party rule linked with a control test, so that shares and share options granted to non-executive directors or other key employees will not automatically result in ineligibility as a qualifying investor.

v. Recognise additional exit strategies for EII investors

Normal commercial investment decisions are always made with exit strategies being provided to investors. Investors will always ask about what the company will do with their money and how and when they will receive a return on their investment.

The EII only allows investors to exit by way of share redemption or a trade sale. The former attracts income tax treatment and requires the company to have accumulated distributable reserves, and the latter only materialises for a small number of companies. Investee companies also need to be able to tidy up their share capital tables in advance of a potential exit or for other commercial reasons without the fear of contravening the EII rules.

The EII imposes a clawback of relief for investors still within their relevant period if other EII investors are taken out. In the event a company raises several rounds of EII funds, it is not reasonable to expect the investors in Round 1, who took on the highest levels of risk, to have to wait until the 4-year period of the final round has expired to receive a return on their investment. The redemption windows set out in section 508R(9) TCA 1997 are not sufficient.

We believe the EII should recognise exit strategies for investors beyond what is provided by way of a share redemption under section 508R(9) TCA 1997 or trade sale, given the high commercial risks investors assume.

vi. Allow the offset of capital losses

Capital losses, net of the tax relief already received, incurred on EII investments should be allowable, in line with the recommendation made by Indecon in their 2018 evaluation of the scheme, provided the loss relief does not impact the income tax relief available under the revised GBER. We believe limiting the loss to the actual cash loss to the investor is fair and reasonable and there is a precedent for such under section 552(1A) TCA 1997.

EII Administrative Recommendations

i. Commit appropriate and adequate resourcing to the administration of EII applications

To ensure consistency in dealing with applications in a timely manner, it is important that there are dedicated full-time Revenue staff who understand the complicated rules of the scheme, together with Revenue officials who have commercial knowledge and experience in dealing with such businesses.

Under section 508H TCA 1997, taxpayers can request confirmation from Revenue through the Revenue Technical Service (RTS) on the interpretation of certain eligibility criteria for EII. However, we have received feedback that delays up to six months can be experienced by taxpayers in obtaining such confirmations. Such delays mean that often taxpayers decide not to proceed with EII.

Publishing a summary of Revenue confirmations given on EII to date, akin to what has been published in the past in relation to trading opinions, would help taxpayers to understand Revenue's interpretation of the relevant criteria, which could remove the need to obtain clarification from Revenue in their individual case.

ii. Provide enhanced support for small and micro companies

A streamlined administrative process needs to be introduced for small and micro companies to help them avail of EII finance. This could be achieved by adopting non-mandatory template forms (i.e. for business plans, cash flows etc.) and or Revenue accepting already completed Enterprise Ireland or Local Enterprise Office forms, where relevant, as supporting documentation for EII claims.

As an initial step, collating the relevant information included in various sections of the Revenue TDM on Part 16 TCA 1997 on the information required to be included in a business plan, cashflow etc. into an appendix could assist small and micro companies in understanding the requirements. Such steps would ease the extensive administrative burden for small and micro companies.

iii. Reduce duplication of administration

Companies claiming EII are required to file Form RICT, Form 21R and to tick a box on the Form CT1. The Form RICT is macro enabled and can be prone to technological errors. Feedback from members has highlighted that information that has already been submitted on the aforementioned forms to Revenue, is often requested subsequently by Revenue when conducting a Level 1 Compliance Intervention.

Revenue officials dealing with a particular taxpayer should have access to the relevant information contained on their submitted EII forms when undertaking a compliance intervention without having to request the taxpayer to submit the information again.

Furthermore, Revenue officials should be able to download the relevant share information that has been submitted by a company on its Form B5 to the CRO, instead of requesting it again from the taxpayer when conducting an EII compliance intervention.

iv. Separate TDM for each relief in Part 16 TCA 1997

The TDM on Part 16 TCA 1997 currently runs to 108 pages and covers the three schemes contained in Part 16 (i.e. EII, SCI and SURE). We understand that Revenue is considering separating the Manual into three separate TDMs to cover each relief which we consider essential.

Furthermore, the TDM on EII should be streamlined to contain guidance on the current rules that apply, with historical material archived into separate Manuals for reference, so that the Manual is easier to navigate.

1.1.2 SCI

Although the SCI scheme was introduced to alleviate the connected party restrictions for early-stage micro companies embarking on a brand-new venture in recognition of their reliance on friends and family for initial small-scale capital, claimants are still subject to the same level of administrative requirements as a company seeking to raise EII finance. This means start-ups raising funds under the SCI scheme must do so through a similar shareholder structure that satisfies the complex GBER rules and detailed business plan requirements, as companies availing of EII.

Typically, small/micro businesses or their accountants do not have the in-house expertise (or the time to upskill) to raise EII finance, which means they must engage further outside experts to prepare and implement the scheme at additional cost. The penalties are disproportionately high for any missteps under the scheme, which means the same process must be followed for raising €5 million as it is for €50,000. Further amendments are necessary to ensure the SCI can fulfil the policy objective of supporting the growth of small indigenous businesses.

SCI Legislative Recommendations

i. <u>Review the criteria of the scheme</u>

Feedback from our members suggests the narrow criteria set out in the SCI scheme has impacted its take up. The limit of €500,000, which is considered quite low, and the fact the company must not have any linked enterprises are barriers to claiming the relief.

Furthermore, as follow on investment under Part 16 TCA 1997 only qualifies for 20% tax relief in line with the revised GBER, we understand that members advise their clients to undertake a larger round of investment first, which can qualify for 40% or 50% under the EII provisions before obtaining finance from family/friends which qualify for relief under the SCI scheme.

SCI Administrative Recommendations

i. <u>Raise awareness of the scheme</u>

Feedback from our members indicates that awareness of the SCI scheme is low. Therefore, we would recommend that Revenue enhance the information on their website to ensure the SCI scheme is easily accessible to small and micro companies and start-ups.

ii. <u>Separate TDM on SCI</u>

As outlined above, we recommend that Revenue guidance on the SCI is contained in a separate TDM for ease of reading rather than as part of a TDM on all reliefs contained in Part 16 of the TCA 1997. We understand that Revenue is actively considering this matter.

1.1.3 SURE

SURE was introduced to provide tax relief to PAYE taxpayers who leave employment and start a new company. In our view, the following amendments are necessary to ensure the SURE can fulfil the policy objective of supporting the growth of indigenous business.

SURE Legislative Recommendations

Extend SURE to the self-employed

Under the SURE scheme, an individual needs to have paid sufficient income tax through the PAYE system in the previous four years. This means that a previously self-employed person, who has paid equivalent levels of income tax through the self-assessment system, does not qualify for relief.

Apart from discriminating against self-employed workers, this restriction acts as a significant barrier to the effectiveness and applicability of SURE. In our view, the SURE scheme should be extended to self-employed workers who set up a new business.

SURE Administrative Recommendations

i. Raise awareness of the scheme

Feedback from our members indicates that awareness of the SURE scheme is low, particularly among people who have recently left employment and are looking to quickly start up a new business. Therefore, we recommend that Revenue enhance the information on their website to promote this incentive to increase uptake and in turn encourage entrepreneurship and job creation.

ii. Separate TDM on SURE

As outlined above, we recommend that Revenue guidance on the SURE is contained in a separate TDM for ease of reading rather than as part of a TDM on all reliefs contained in Part 16 of the TCA 1997. We understand that Revenue is actively considering this matter.

1.1.4 R&D Tax Credit

With the implementation of Pillar Two, many countries are currently improving or introducing new incentives for R&D to attract investment. Given the mobility of R&D investment, it is critical that Ireland's R&D Tax Credit is continually benchmarked against key competitor jurisdictions to ensure that the country can continue to attract additional R&D investment. Further legislative and administrative changes to the R&D Tax Credit are also needed to encourage more SMEs to be innovative and undertake R&D.

R&D Tax Credit Legislative Recommendations

i. Condense the 3-year R&D Tax Credit payment schedule to one year for SMEs

The changes introduced in Finance Act 2022 to align the R&D Tax Credit with new international definitions of refundable tax credits provide for a three-year fixed payment schedule. While the Finance (No.2) Act 2023 amendment to double the first-year payment threshold to allow the first €50,000 of a R&D Tax Credit claim to be paid in full in the first year of the claim rather than having to be spread over the normal three-year period is welcome, we believe condensing the 3-year R&D Tax Credit payment schedule to one year for SMEs would provide valuable assistance to smaller companies. After all such companies tend to be cash constrained and therefore, accelerating the refund for them would be very beneficial, with only a timing cost for the Exchequer.

ii. Align the definition and criteria for R&D

We believe consideration should be given to aligning the definition for R&D grants given by IDA Ireland and Enterprise Ireland which include innovation with the R&D Tax Credit.

Section 2.7.1. of Revenue's Guidelines[5] on the R&D Tax Credit refers to a concession for small or micro enterprises whereby Revenue would not, as a rule, seek to challenge the science test in relation to a project where an Enterprise Ireland, Horizon 2020, Horizon Europe or IDA R&D grant has been approved in respect of the R&D project (where the total credit is €50,000 or less). However, Revenue's Guidelines draw a distinction whereby projects may be "innovative" rather than qualifying R&D, while national grants often include reference to innovation (e.g., the Enterprise Ireland "RD&I Fund" or the IDA "RD&I Grant").

Enterprise Ireland's, Horizon Europe and IDA's R&D grants in respect of research and experimental development projects come within the meaning of the OECD's Frascati Manual 2015, which states: *"Research and experimental development comprise creative and systematic work undertaken in order to increase the stock of knowledge….and to devise new applications of available knowledge. [Innovation] has to do with putting new or significantly improved products on the market or finding better ways (through new or significantly improved processes and methods) of getting products to the market. R&D may or may not be part of the activity of innovation, but it is one among a number of innovation activities. These innovation activities may be carried out in-house or procured from third parties."*

Ideally, the criteria for the R&D Tax Credit administered by Revenue should be aligned with other State agencies, the EU, and the OECD Frascati Manual for simplicity. However, at a minimum, it should be aligned with the criteria adopted by other State agencies. Given all R&D grants from IDA and Enterprise Ireland are subject to

[5] Tax and Duty Manual Part 29-02-03 Research and Development (R&D) Corporation Tax Credit

assessments on the science element by Technical Assessors, this should be relied upon by Revenue for the purposes of meeting the science test for R&D Tax Credit claims.

iii. <u>Increase the limits for outsourcing</u>

We believe the level of qualifying expenditure incurred by a company when R&D is sub-contracted or outsourced to a third-party or university or Institute of Higher Education should be increased, above the current limits of 15% of in-house R&D expenditure or €100,000 (whichever is greater). This would be in keeping with Government policy to foster collaboration between academia and private business. The current limits on outsourcing can severely hamper the ability to outsource activities such as clinical trials or AI development.

Where clinical trials are outsourced, the outsourcing is usually managed by a senior scientist/ engineer employed by the company who is responsible for co-ordinating and driving the outsourced clinical trial. It can be unclear whether such management activities are considered qualifying R&D activities. In our view, these activities are a critical part of the R&D and it is important that clarity is provided that such management type activities are considered as qualifying R&D activities.

iv. <u>Allow rent to qualify as R&D expenditure</u>

The disallowance of rent as qualifying expenditure on R&D substantially reduces the attractiveness of the R&D Tax Credit for SMEs. In July 2020, Revenue updated their guidance on section 766(1) TCA 1997 on the circumstances in which rental costs can be considered qualifying expenditure for the purpose of the R&D Tax Credit.

Notwithstanding representations from tax advisers through TALC, Revenue confirmed their view that in most cases rent does not qualify as R&D expenditure but there may be scenarios where rent can qualify where the expenditure is incurred wholly and exclusively in the carrying on of the R&D activities.

The guidance provides examples of rent incurred on a specialised laboratory or a clean room in order to advance R&D activities which it states may be qualifying expenditure but the rent of an office space in which R&D activities are carried on is not qualifying expenditure as the office is *"the setting in which R&D happens and does not itself perform a key function in relation to the R&D process"*. We believe that Revenue's guidance significantly narrows the circumstances where rent may be included as qualifying expenditure on R&D and in our view, is contrary to the policy intention of the R&D Tax Credit.

We consider that Revenue's interpretation also creates a clear inequity in favour of companies that have the available resources to incur expenditure on the construction or refurbishment of a building or structure for R&D purposes rather than incur a rental cost. It must be the purpose to which the building is used that is relevant as opposed to the occupancy type i.e. owned versus rented.

Section 766A TCA 1997 provides that where a company acquires a building and incurs expenditure on the refurbishment of the building for R&D purposes, these costs, subject to meeting specific conditions, qualify for the R&D Tax Credit. However, based on Revenue's most recent guidance, renting the same refurbished R&D building may not qualify for the R&D Tax Credit even if the same R&D activity is being undertaken in the building. This measure clearly discriminates against SMEs who are, in many instances, unlikely to have the financial resources to purchase a building, but very often are the start-ups carrying out significant and innovative R&D.

Equally, as rental costs are a substantial cost for most small and micro sized companies, the disallowance of rent as qualifying expenditure on R&D significantly diminishes the attractiveness of the R&D Tax Credit for such companies. Feedback the Institute has received directly from SMEs confirms that legislative clarification is necessary to ensure rent is a qualifying cost for the purpose of the R&D Tax Credit so that the tax incentive can continue to encourage investment in R&D and innovation by Irish business.

v. Incentivise green or energy related R&D

In our view, consideration should be given to new targeted measures for R&D in specific priority areas, such as green or energy related R&D and AI/innovation in general. The introduction of such targeted measures could help the Government to deliver its ambitious carbon emission targets.

R&D Tax Credit Administrative Recommendations

i. Increase the limit for Revenue's streamlined R&D validation process for small/ micro companies

In an effort to reduce the administrative burden, Revenue does not seek to challenge the 'science test' as part of any validation checks on a R&D Tax Credit claim made by a small or micro company that has already been approved for an Enterprise Ireland, IDA or EU grant for the R&D project, provided the credit claim is no more than €50,000 for any accounting year and the R&D project is undertaken in a qualifying field of science or technology.

While this is a welcome simplification measure for small/ micro companies, consideration should be given to increasing the amount that can be claimed from €50,000 to make the credit more accessible for small/ micro companies and start-ups. For example, the €50,000 limit could apply per project rather than per claim or it could be increased by a multiple of what it is now, say to €100,000.

We understand from discussions at the TALC Sub-committee on Simplification and Modernisation of Business Reliefs that Revenue may not in a position to increase the limit on an administrative basis. In that case, it would be important that a legislative amendment is introduced to put the simplification measure on a statutory footing to ensure that the limit is increased appropriately.

ii. <u>A Revenue pre-approval process for first-time R&D Tax Credit claims by small/ micro companies</u>

We believe a pre-approval process for first time R&D Tax Credit claims by small/ micro companies would help to alleviate the uncertainty over Revenue subsequently challenging the claim on the 'accounting test' (i.e., the record-keeping requirements). Notably, the OECD has recommended the introduction of such a pre-approval process to help reduce uncertainty for SMEs.[6]

In the UK, SMEs making their first R&D claim can qualify for 'Advance Assurance.' If 'Advance Assurance' is granted, HMRC will accept any R&D claims in the first three accounting periods without the need for HMRC to carry out further checks on the claim.

iii. <u>Simplified documentation requirements for R&D Tax Credit claims by SMEs</u>

The 'accounting test' must be passed by small and micro companies. Only those revenue expenses that are incurred by the business wholly and exclusively in the carrying on of R&D activities can qualify for the R&D Tax Credit. This includes salaries and wages of staff directly involved in the R&D activity, cost of raw materials used in the R&D activity and fuel, power, water, etc. used in the R&D process.

The time and resources required to prepare this documentation can deter some taxpayers, and particularly SMEs, from claiming the credit. For them, the compliance cost for the business is greater than the potential benefit of the tax credit.

Having a 'one size fits all' approach, regardless of the size of the company is not fit for purpose and does not encourage engagement from the SME sector. Simplified documentation requirements for claims by SMEs would help improve the uptake of the R&D Tax Credit among start-up and SMEs.

Revenue should consider leveraging financial documentation prepared by SMEs for other Government agencies, such as for Enterprise Ireland grants, to support R&D Tax Credit claims. While Revenue do not specify the documentation which is required, Revenue provide a "Suggested File Layout" which is based on 24 questions, in addition to sub-questions, as a basic guide to the contemporaneous documentation that it expects a company to maintain. This includes a caveat that *"further supplementary/ clarifying information may be requested."*

Typically, grant agencies require supporting information in a different format to support a grant funding drawdown, including a "Claims Checklist" and associated documentation (e.g. Independent Accountant's Report, Directors' Statement, Revenue Grant Claim Form, Progress Report) and further documentation to be available upon inspection (e.g. payslips, timesheets, and invoices).

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[6] OECD (2019), SME and Entrepreneurship Policy in Ireland, OECD Studies on SMEs and Entrepreneurship, OECD Publishing, Paris

Furthermore, we recommend that Revenue guidance relating to overhead costs should be simplified as it has become increasingly complex to navigate, particularly for SMEs. This could be achieved, for example, by providing for a set percentage of labour overheads in guidance to simplify R&D expense claims and provide more certainty to taxpayers.

iv. Amend Revenue guidance on agency staff

The use of agency staff is considered to be outsourcing for the purpose of computing the amount of qualifying R&D activity and related expenditure and is subject to the limitations on outsourcing. This rule relates to any individual not remunerated directly by the company for their services.

Revenue allows costs incurred which relate to individual consultants who are hired on a part-time or short-term basis to undertake sub-contracted activity to be treated as part of the direct employee costs of the company and not as agency staff, provided that the following conditions are met:

- The individual works under the company's control and direction.
- The individual works on the company's premises.
- The individual must be able to contribute specialist knowledge, which cannot be supplied by the in-house research team, to a specific R&D project being undertaken by this in-house team.
- The engagement period does not exceed 6 months.

This is a welcome concession in Revenue's guidance but feedback from our members suggests that the conditions to satisfy the concession for agency staff often do not reflect the commercial reality of such projects, in particular the requirement for the individual to work on the company's premises and for the engagement period not to exceed 6 months.

We understand from discussions as the TALC Subcommittee on Simplification and Modernisation of Business Reliefs that the requirement for an individual to work on the company's premises does not preclude normal hybrid working arrangements. It would be helpful for this clarification to be provided in published guidance.

We would contend that there should not be any restriction imposed on SMEs using agency staff or individual consultants, where those agency staff/ individual consultants cannot make a R&D Tax Credit claim as there is no risk of double-dipping of the credit. Feedback from our members indicates that the removal of this restriction for agency staff/ individual consultants would greatly benefit SMEs.

v. Develop SME-friendly Revenue guidance on sector specific R&D issues

The processes and documentation needed to support a R&D Tax Credit claim can be daunting. This is a particular challenge for business sectors such as food, software, and

IT, which traditionally do not document their processes and costs to the extent done in highly regulated sectors, such as pharma and financial services. Providing SME-friendly guidance, with step-by-step instructions on the claims process and practical studies, together with tips on how to avoid common errors in claims is essential, similar to the approach adopted by HMRC in the UK.

Industry specific guidance, with detailed practical instances of what qualifies and what does not qualify would be welcome. For example, starting with sector-specific guidance for food production, software, and med-tech industries, all of which engage in very different R&D processes. Uncertainty surrounding what can qualify and how to document such processes, continues to persist in these sectors. If it is not possible for Revenue to provide separate guidance for specific sectors, then at a minimum, the current guidance should be updated to include additional sector specific examples.

vi. <u>Ensure Revenue Compliance Interventions are proportionate and conducted in a timely and efficient manner</u>

There is a certain level of anxiety amongst companies over the potential for Revenue to subsequently challenge R&D Tax Credit claims. While verification of claims by taxpayers is an intrinsic part of a self-assessment system, it is important that Revenue Compliance Interventions are proportionate and conducted in a timely and efficient manner, in the interest of all parties.

In addition, given the nature of R&D, it is important that there is recognition of the appropriateness of “technical adjustment” treatment for R&D Tax Credit claims, where due care has been taken by the taxpayer and they have applied the legislation in good faith.

vii. <u>Access to Revenue's R&D technical experts</u>

Providing access to Revenue’s R&D technical experts is a way in which R&D Tax Credit claims could be dealt with more smoothly. Taxpayers and their advisers should be given the opportunity to participate in briefings with R&D technical experts during the review process, which would reinforce the independence of the expert and increase the overall transparency of the review process.

It is also vital that the R&D technical experts tasked with opining on the science element of R&D Tax Credit claims have the experience of the application of science in a business environment. Feedback the Institute has received indicates that the technical experts used by Revenue to opine on the ‘science test’ tend to be from academic backgrounds, which can often result in knowledge gaps, as the technical expert is applying science theory to commercial practices. Revenue should explore ways to expand the pool of experts undertaking this work to ensure it adequately reflects the necessary expertise.

Furthermore, Revenue needs to consider ways to address the serious concerns among taxpayers and their advisers in relation to the perceived lack of independence of the R&D technical experts including:

- The level of consistency among the R&D technical experts which can vary widely on the science test.
- Delayed response times from the R&D technical experts, with some responses delayed up to six months.
- Some R&D technical experts do not appear to fully understand that they are independent given they are engaged by Revenue; provided with Revenue guidance at the start of the engagement; issue the draft report to Revenue (to ensure it meets certain technical standards per the legislation) and appear as a Revenue witness in appeal cases.
- Experts sharing draft reports on R&D Tax Credit claims with Revenue and not with the relevant taxpayer.
- Experts having pre-meetings with Revenue to discuss R&D Tax Credit claims and not with the relevant taxpayer.

Stakeholder consultation in advance of updates to Revenue guidance

Revenue guidance on the R&D Tax Credit has changed 18 times since the introduction of the credit. While many of the updates have provided more clarity on various aspects of the credit, the combination of the volume of iterations and the change in emphasis to the extent to which a company may rely on the guidance, has added to the uncertainty in particular where the legislation underpinning the guidance has not been amended but Revenue's interpretation of it has altered.

Consultation with stakeholders in advance of updates to Revenue's guidance would help to provide more tax certainty for claimants. This should also include consultation with corporation tax software providers to ensure R&D Tax Credit claims can be submitted to Revenue without processing difficulties.

1.1.5 Tax relief for new start-up companies

Section 486C TCA 1997 provides relief from corporation tax for start-up companies in their first three years of trading. The relief was introduced to provide support to new business ventures in their critical early years of trading, thereby supporting the creation of additional employment and economic activity in the State.

Remove the link to Employers' PRSI

Finance Act 2011 modified the relief to link the quantum of corporation tax relief to the amount of Employers' PRSI paid by a company in an accounting period, subject to a maximum of €5,000 per employee and an overall limit of €40,000. Finance Act 2013 enhanced the relief to allow a carry-forward of any unused relief arising in the first three years of trading, due to losses or insufficient profits, for use in subsequent years.

Feedback from our members indicates that linking the quantum of relief to Employers' PRSI has acted as a significant barrier to availing of the relief under section 486C. This is because often in start-ups companies, salaries are frequently paid at reduced levels due to salary caps imposed by funders until certain milestones are reached by the business.

Furthermore, employees in start-ups are often given a mix of a lower salary and share-based remuneration. All of this results in lower levels of Employers' PRSI being paid by start-ups to support claims for relief under section 486C.

Raise awareness of the scheme

Feedback from our members indicates that awareness of the relief available under section 486C TCA 1997 up to now has been low and has therefore been rarely claimed by companies.

It was highlighted during discussions of the TALC Sub-committee on the Simplification and Modernisation of Business Reliefs that it is difficult to locate content on the tax relief for new start-up companies on the Revenue website. We welcome the ongoing work by Revenue to improve the accessibility of this content on the Revenue website to ensure the relief can be more easily accessed by small and micro companies and start-ups.

1.1.6 Transfer of a business to a company

Relief under section 600 TCA 1997 applies by deferring chargeable gains on the transfer of a business as a going concern to a company (by someone who is not a company). All assets of the business must transfer. The relief applies to the extent that the consideration for the business as a going concern is in the form of shares. According to Revenue's interpretation of the relief, any liabilities of the business included in the transfer ranks as consideration for the transfer and therefore, that proportion of any gain on transferring chargeable assets is chargeable to CGT.

However, Revenue guidance provides that "bona fide trade creditors" do not form part of consideration for the purposes of the calculation. Revenue's Tax & Duty Manual Part 19-06-04, states *"the term 'bona fide trade creditors' means genuine creditors who supply goods or services to a business. An example of a trade creditor is a supplier of food to a restaurant. Liabilities of a business such as bank loans or tax liabilities taken over by the company are not trade creditors and, if taken over, are to be included as consideration for the transfer of a business."*

It is important to note that section 600 does not contain any such definition of the meaning of "consideration paid". In practice, the value of a business as a going concern is calculated taking into consideration all assets and liabilities of the business including bank loans, finance lease, invoice discounting/factoring, tax liabilities etc. These factors must be taken into account to establish the market value of a business. In our view, it is counter intuitive to exclude these items when transferring the business.

Revenue's interpretation seems to apply the relief on an asset-by-asset basis whereas the relief is targeting the transfer of a business as a whole with a deferral of CGT. Revenue has adopted a narrow interpretation of the legislation which essentially precludes businesses with any degree of leverage with legitimate business liabilities, from availing of the relief in full. Of course, it is accepted that liabilities should reduce the base cost for any future disposal of the share but having to pay CGT upfront makes this relief unworkable in practice for many taxpayers.

For example, common occurrences such as businesses owning a premises with bank debt; businesses with assets on finance lease or hire purchase; businesses with invoice discounting and businesses with overdrafts, are essentially prohibited from availing of full relief under section 600. The main reason for this, is the upfront CGT liability which creates a real cash cost without any corresponding cash income for the business owner.

If Revenue consider the liabilities of the business should remain as consideration/ deemed consideration, then the taxpayer should be entitled to choose how to allocate the liabilities to asset line items (i.e. allocate bank loan against non-chargeable assets first to maximise the amount which can qualify for relief under section 600).

1.1.7 KEEP

The KEEP was introduced by Finance Act 2017 to assist SMEs[7] to attract and retain skilled workers through the provision of share-based awards. It provides for an exemption from income tax, USC and PRSI for any gain arising on the exercise of a share option by a qualifying individual in a qualifying company. Irish SMEs continue to experience difficulties recruiting and retaining skilled workers. Attracting the best talent is central to building a successful company and is crucial to the future growth and export potential of the business.

Over the last few years, the publicity surrounding the KEEP has raised awareness of the benefits of share-based remuneration among start-ups and SMEs. Feedback from our members highlights that while many of their clients may have sought professional advice, regarding the potential use of the KEEP in their business to help recruit and retain skilled workers, its inherent limitations meant they could not implement the scheme and instead, they explored other options for share-based remuneration.

Several amendments were made to the KEEP in Finance Act 2019 which related to companies operating through a group structure qualifying for the scheme; extending the definition of a 'qualifying individual' to include certain part-time employees and permitting the grant of KEEP options over existing shares, as opposed to newly issued shares. The Finance Act 2019 provisions were brought into effect in Finance Act 2022.

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[7] A company will be considered a micro, small or medium sized enterprise (SME) where the company employs fewer than 250 employees and its annual turnover/annual balance sheet does not exceed €50 million and €43 million respectively.

In addition, further amendments were made to the KEEP in Finance Act 2022, including extending the scheme to 1 January 2026, doubling the lifetime company limit for the KEEP shares from €3 million to €6 million, and enabling CGT treatment to apply to the buyback of KEEP shares by a company from a relevant employee. These changes were subject to a commencement order which the Minster for Finance signed in November 2023. Therefore, the impact of the Finance Act 2022 amendments on the uptake of the KEEP remains to be seen.

Since its introduction, the Institute has continued to highlight limitations with the operation of the KEEP which significantly impact the feasibility of the scheme and ultimately, its success in achieving the policy aim of helping SMEs to attract and retain talent. Although the KEEP was designed to incentivise talent to take up employment in such companies and allow them to compete with listed companies, there has been a very low uptake of the scheme, with just 31 employers filing KEEP returns with Revenue for 2022.[8]

Notwithstanding the recent Finance Act amendments, we believe further legislative reforms are needed to improve the feasibility of the KEEP. In our view, the policy intention of the KEEP, to help SMEs attract and retain key employees, can only be achieved if these limitations are addressed.

In our response to the Department of Finance consultation on the KEEP in June 2022,[9] our response to the Department of Finance consultation on Ireland's Taxation of Share-based Remuneration[10] and list of recommendations to the TALC Sub-committee on Simplification and Modernisation of Business Reliefs, we outlined the limitations of the scheme in detail together with our recommendations for reforms to the existing legislation. In summary, we recommended the following legislative and administrative changes.

KEEP Legislative Recommendations

i. Impose a proportionate sanction for undervaluing share options

As outlined above, obtaining certainty over the valuation of KEEP shares is a key concern for companies considering availing of the scheme. Where options are granted at an undervalue within say a certain percentage of the Revenue determined value (for example, 75%), we believe a more proportionate sanction would be for a charge to income tax to arise on the exercise of the options on the difference between the market value at the date of grant and the option price. This would allow the options to remain qualifying share options, but it would also enable Revenue to collect income tax on the portion of the gain attributable to the undervalue.

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[8] Department of Finance, Consultation on Ireland's Taxation of Share-based Remuneration, December 2023
[9] Irish Tax Institute Response to the Consultation on KEEP, 17 June 2022
[10] Irish Tax Institute Response to the Consultation on Ireland's Taxation of Share-based Remuneration, January 2024

The income tax arising on exercise could be collected under the same mechanism as section 128 TCA 1997 (i.e., a charge to income tax under Schedule E is imposed on any gain realised by a director or employee from a right granted to him/her, by reason of his/ her office or employment, to acquire shares or other assets in a company).

ii. Amend the definition of a 'qualifying holding company'

A 'qualifying holding company' for KEEP purposes cannot be a trading company. If it is trading, it is not a 'qualifying holding company,' even if it is wholly or mainly holding shares in trading subsidiaries.

Company structures with an intermediate holding company will not be regarded as a qualifying company if there is no qualifying subsidiary held directly by the ultimate holding company. In contrast, Revenue guidance for Revised Entrepreneur Relief (Section 597AA TCA 1997) acknowledges that structures with a double holding company are not precluded from that relief.

A holding company can only hold shares in a qualifying subsidiary and a 'relevant subsidiary' and no other companies. A 'relevant subsidiary' is one in which the 'qualifying holding company' holds more than a 50% interest in the ordinary share capital. Therefore, if the holding company had a 50% joint venture interest in another company it cannot be a 'qualifying holding company', even if it had a qualifying subsidiary that was a qualifying company.

The definition of 'qualifying holding company' in section 128F(1) TCA 1997 should be amended to permit the group as a whole to be considered, rather than simply considering the holding company in isolation. This could be achieved by amending the wording of the definition of 'qualifying holding company' at subsection (c) to state that it means a company where *"the business of the company, its qualifying subsidiary or subsidiaries, and as the case may be, its relevant subsidiary or subsidiaries, taken together consists wholly or mainly of the carrying on of a trade or trades."* This approach would be similar to the approach taken for the CGT holding company exemption in section 626B TCA 1997.

iii. Remove the annual emoluments cap from the qualifying share option limit

Currently, the total market value of all shares, in respect of which qualifying share options have been granted by the qualifying company to an employee or director, must not exceed €100,000 in any year of assessment; €300,000 in all years of assessment or 100% of the annual emoluments of the qualifying individual in the year of assessment in which the qualifying share option is granted.

Linking the amount of share options that can be awarded under the KEEP to the employee's annual emoluments restricts high growth companies in start-up mode availing of the scheme. Often in start-up businesses, employees and directors have lower salaries, compared with larger multinationals, which can prohibit such companies under the KEEP offering equity as an incentive for these individuals to stay in the business.

Rather than discriminating in practice against the remuneration strategies of these companies and the mix of cash-based and equity-based remuneration that they offer employees, the KEEP measures should simply set absolute values, such as those included in subparagraph (i) and (ii) of part (d) of the definition of a qualifying share option in section 128F(1) TCA 1997. It should be left to a company to determine the proportionate mix of cash and share-based remuneration as a commercial matter and to follow market driven pay awards.

An amendment to the qualifying limit of 100% of the annual emoluments of the qualifying individual would take account of situations where an employee's salary has reduced because of reduced working hours or a temporary layoff. It would also address situations where employees, who are temporarily absent from work due to maternity or paternity leave, are limited in terms of the relief which may apply, as often their salary levels would be reduced during this time.

The lifetime limit of €300,000 can act also as a barrier to claiming relief under the scheme where shares have increased in value. Consideration should be given to applying the limit on a rolling basis. In the UK scheme, the cap is on the value of the share options as opposed to the value of the shares, which can be rolled over every three years.

iv. <u>Allow for the continuation of the relief where a SME undergoes a reorganisation</u>

The current KEEP legislation does not provide for the continuing availability of the relief in the event of the SME (e.g., holding company and its subsidiaries) undergoing a corporate reorganisation during the period in which the KEEP share option rights are outstanding.

The KEEP legislation should be amended to include similar provisions to those contained within the Revised Entrepreneur Relief legislation, which seeks to address reorganisations that might affect the entitlement of a qualifying individual and a qualifying company to meet the scheme requirements.

v. <u>Provide for ‘roll over relief’ of the KEEP share options</u>

Section 128F TCA 1997 should be amended to provide ‘roll over relief’ of KEEP share options, similar to that provided in section 128(8)(a) TCA 1997. Where share rights are exchanged between directors and employees or a company grants a new right in exchange for the surrender of an original right, the new right and the original right are looked at as one for the purpose of the charge to tax under section 128.

This ‘roll over relief’ effectively means that the tax charge arises at the point of exercise of the new right, with the history of the original share right taken over in respect of a future exercise of the new right. A similar relief is not included in the KEEP legislation.

For example, Company A grants share options that meet the conditions of the KEEP under section 128F TCA 1997 and would qualify for an exemption from income tax on exercise. During the exercise period, a transaction is entered into which results in the share capital of Company A being acquired, and unexercised share options are exchanged or assigned for new options in the acquiring company.

Section 128F should be amended to provide 'roll over relief' in respect of KEEP share options. This would apply where during the exercise period, a transaction is entered into which results in the share capital of a company being acquired, and unexercised KEEP share options are exchanged or assigned for new options in the acquiring company.

In such circumstances, if the acquiring company meets the qualifying company/ group criteria set out in the legislation, the future exercise of the new replacement options should qualify for relief, with the history of the original share option being taken over for the purposes of determining the charge to tax.

KEEP Administrative Recommendations

<u>Provide a Revenue agreed 'safe harbour' for share valuations</u>

Share valuations in relation to KEEP are costly and difficult in practice because a company may be required to undertake multiple valuations within a 12-month period depending on when employees are recruited.

Currently, there is no clear guidance on how to determine what market value is for the purposes of the KEEP. If qualifying options are not granted for market value or the market value is subsequently determined by Revenue to be higher than originally projected, the options will not qualify as KEEP options under section 128F TCA 1997, resulting in no exemption from income tax, USC and PRSI on exercise.

Revenue's guidance on KEEP states that Revenue expects that in valuing the shares the company should use a valuation method which complies with relevant accounting standard and that Revenue will not provide an opinion regarding company specific share valuations. No guidance is provided by Revenue on what may be appropriate regarding acceptable discounting of shares in a private company.

Furthermore, it is unclear if Revenue's CAT Manual on the valuation of unquoted shares can be relied upon by taxpayers when valuing KEEP shares given the CAT guidance is directly linked to section 27 CATCA 2023 inheritance cases. It can often be difficult to apply general accounting principles, depending on the stage in the lifecycle of a business, especially if the company is not yet generating revenues.

Comprehensive Revenue guidance on share valuations is urgently required to support companies adopting the KEEP. This could be achieved by Revenue developing templates or safe harbour approaches for valuing shares in a SME. For example, if the taxpayer has undertaken 'best endeavours' to make a reasonable attempt to value 'potential' at a point in time and that valuation is accepted by Revenue to last for 12 months, provided no significant events are likely to take place which could impact the valuation.

This would mean that a taxpayer would have assurance from Revenue that the share valuation is not less than market value for tax purposes, where the taxpayer has adopted the safe harbour approach to valuing the KEEP shares.

It is noteworthy that it is possible to agree a valuation of a company with HMRC for the purposes of the Enterprise Management Incentive (EMI) which is a share scheme in the UK that is similar to the KEEP. An application request for a share valuation in connection with the EMI can be made online by the SME and is given priority by HMRC.

1.1.8 Revised Entrepreneur Relief

Ireland's high rate of CGT makes reliefs such as Revised Entrepreneur Relief[11] even more important as the relief can reduce the high CGT burden on the sale of a business albeit to a limited extent. The relief allows for a lower 10% CGT rate on business gains which is subject to a lifetime limit of €1 million.

Feedback we have received from members and directly from entrepreneurs is that the current design of the relief is one of the key contributing factors to holding back the indigenous entrepreneurial ecosystem.

Revised Entrepreneur Relief Legislative Recommendations

i. <u>Broaden the definition of a holding company</u>

Following enactment of Finance (No.2) Act 2023, a holding company for Entrepreneur Relief purposes means a company that holds shares in other companies, all of which are its 51% subsidiaries, and whose business consists wholly or mainly of the holding of shares in those subsidiaries.

Whilst this is a legislative definition, there is one main issue which commonly occurs in practice, which can be illustrated by the following example: HoldCo has two subsidiaries, Sub1 which is trading and Sub2 which owns the property which is used wholly for the purposes of the trade of Sub1. Entrepreneur Relief is denied in such circumstances.

There is a myriad of scenarios where these types of structures are implemented for commercial reasons such as for banking requirements; insurance requirements where there is a high-risk asset within the business like a quarry or to de-risk the trade/business interests from property. This is particularly prevalent in the context of emergency accommodation provision at present. Business owners who manage their risk regarding

[11] Section 597AA TCA 1997

their business assets in a prudent manner are disadvantaged against business owners who do not.

This could be addressed by amending the definition of a "qualifying group" in section 597AA TCA 1997 to include a company (which would include a holding company or another subsidiary company) that owns an asset that is used wholly or mainly for the purposes of a qualifying business carried on by another company within the qualifying group.

ii. <u>Remove the restriction on relief where a group holds a dormant company</u>

According to Revenue's guidance, Entrepreneur Relief is not available in situations where a dormant company is present in the group. This is a very significant limitation to the relief because a subsidiary company can commonly become dormant over time. For example, this might happen where the company has ceased to trade or where the trade has been transferred to another group company and the company cannot be wound up or liquidated due to company law legislation for the protection of creditors.

A group company could have dozens of trading subsidiaries, out of which only one is dormant, yet the relief is completely denied to the entrepreneur in this situation. We recommend that the legislation should be amended to remove the restriction from Entrepreneur Relief in situations where a group holds a dormant company for *bona fide* commercial reasons.

iii. <u>Remove the restriction on relief where a group has a shareholding in a joint venture company of less than 51%</u>

One of the conditions of Entrepreneur Relief is that all subsidiaries must be minimum 51% subsidiaries for the relief to apply. If a group is party to a joint venture and holds less than 51% of the joint venture company, this again can result in full denial of the relief. We recommend that the legislation should be amended to remove restrictions to the relief in situations where a group has a shareholding in a joint venture company of less than 51%.

iv. <u>Allow claim for relief where EII funds are raised by a company</u>

A founder of a company which was financed using shares issued under the EII scheme may be denied Entrepreneur Relief on disposal of their shares in certain circumstances. This issue arises because Entrepreneur Relief requires the vendor to own 5% of the ordinary share capital of a company.

Often, EII shares do not have voting rights and have limited dividend and winding up entitlements. However, such EII shares may be considered to be ordinary share capital for tax purposes, as section 2 TCA 1997 defines ordinary share capital as *"all the issued share capital (by whatever named called) of a company, other than capital the holders of which have a right to a dividend at a fixed rate, but have no other right to share in the profits of the company".*

This means, for example, if a founder shareholder owned 100 €1 ordinary shares but the company also had 500,000 €1A ordinary shares in issue from a previous EII round, a disposal of the founder's shares may not qualify for Entrepreneur Relief, as the legislation is silent on whether to consider the number of shares in issue or the nominal value of the shares in issue, when applying the 5% shareholding test.

We recommend that the legislation be amended to confirm that shares which qualified for relief under Part 16 TCA 1997, with the exception of shares qualifying for SURE, should be ignored for the purposes of meeting the 5% shareholding test for Entrepreneur Relief. Clarification would also be welcome on whether it is the number of shares or the nominal value of shares that is relevant when determining the 5% test.

Revised Entrepreneur Relief Administrative Recommendations

i. Liquidation of a holding company following sale of the trading subsidiary

Section 597A TCA 1997 does not specify whether Entrepreneur Relief is available on a liquidation of a holding company following the sale of its trading subsidiary. Revenue's guidance on Entrepreneur Relief only refers to situations where the liquidated company is carrying on a qualifying business at the date the liquidator is appointed.

However, it is unclear whether Entrepreneur Relief can apply on the liquidation of a qualifying holding company. For example, where the trading company is sold because the purchaser did not want to acquire the entire group and the holding company is immediately liquidated following the sale. It would be helpful if Revenue guidance could clarify whether relief is available in such circumstances.

ii. Working time requirement – non-group companies

It is not uncommon for a business owner to own two individual companies, which are not in a group and wants to sell one of those companies. Consider the example of Taxpayer A who owns two Centra shops each in a separate company. This structure was not created by design but occurred commercially, as Taxpayer A inherited one shop and acquired the second. Taxpayer A wants to sell one of the companies to reduce his hours and scale back. The question then must be considered regarding whether Taxpayer A has met the full-time working requirement for Entrepreneur Relief particularly if the payroll is processed through the company which is not being sold.

The abovementioned example arises frequently in practice across a number of sectors including, fast-moving consumer goods (FMCG (e.g., Centra etc.)), pharmacies and hospitality. We understand from discussions at the TALC Subcommittee on Simplification and Modernisation of Business Reliefs that where the payroll is processed may not be determinative, however, it would be helpful if such clarification could be provided by Revenue in guidance to give certainty to such taxpayers.

iii. Apportioning relief where a company/group holds investments or leases trading premises

When either the holding of investments or the leasing of trading premises takes place within a group company, this can exclude an entrepreneur from claiming Entrepreneur Relief. We believe consideration should be given to either apportioning the relief in circumstances where there is a mix of investments and qualifying activities (similar to the Retirement Relief provisions) or to allow the relief in full where non-trading activities are below a certain *de minims* level.

This is the approach adopted in the UK, where Business Asset Disposal Relief (formerly known as Entrepreneurs' Relief) is available on the sale of shares in a holding company, provided non-trading activities in the group do not comprise of more than 20% of the group's overall activities.

A *de minims* level could also be determined on a valuation basis, for example, less than 20% of the value of the company, where the valuation basis is defined.

1.1.9 Relief for Investment in Innovative Enterprises

We recommend that the certification process for the new relief for investment in innovative enterprises, also known as, Angel Investor Relief, is made as simple as possible for SMEs. Given this scheme operates under GBER, we urge that lessons are learned from the complexities encountered in the administration of the EII and are avoided where possible in the roll-out of this new scheme.

Furthermore, the investment made must be for a minimum amount of €20,000, or €10,000 where at least a 5% shareholding is acquired. We understand that there is concern that some investors may not be able to obtain the minimum 5% ordinary issued share capital of a company to qualify for the relief and that the overall limit of €20,000 is too low to encourage claimants.

1.1.10 CGT Share Buyback Relief

At the TALC Sub-committee on the Simplification and Modernisation of Business Reliefs, we recommended the following legislative and administrative changes to share buyback relief for CGT purposes.

CGT Share Buyback Relief Legislative Recommendations

i. Insert a bona fide test in section 135(3A) TCA 1997 to provide certainty for taxpayers when selling shares in closely held companies

Finance Act 2017 inserted a new subsection 3A into section 135 TCA 1997. The policy intent at the time of its introduction was "*to deal with a number of specific tax avoidance schemes which have been uncovered by the Revenue Commissioners.*" However, unlike other targeted anti-avoidance measures in Irish tax legislation, section 135 TCA 1997 does not include a *bona fide* test, which is normally used to prevent unintended consequences from arising.

The passing on of family businesses and management buy-outs (MBOs) involving close companies continue to be hindered by the anti-avoidance provision contained in section 135(3A). If Revenue take the view that a company has retained profits in excess of the company's commercial needs, subsection 3A imposes income tax treatment rather than CGT treatment on the selling shareholders. This prevents selling shareholders from claiming CGT treatment and retirement relief on an exit from the business.

In the absence of a statutory *bona fide* test, considerable concern continues to exist regarding the potential effect of section 135 on scaling up and passing on of businesses in the SME sector. Although, Revenue guidance may assert that *bona fide* financing arrangements entered into by a purchaser relating to the acquisition of shares are outside the scope of the provision, this is not expressed in legislation. Therefore, it cannot be relied upon by taxpayers in the event of the matter being disputed and subject to an appeal.

Indeed, the Appeal Commissioners have expressly stated that their jurisdiction does not extend to supervising the administrative actions or any purported inequity in the application of the tax code by Revenue.

A number of examples are provided by Revenue in its guidance to demonstrate the application of the section. However, given the broad scope of the measure, the examples do not address the wide range of circumstances in which the provision can potentially apply. Furthermore, as it is an anti-avoidance section, Revenue do not provide an advance opinion as to the application or otherwise of section 135(3A) to any given transaction.

Take the following scenario which often arises in practice. There is a straight-forward sale of shares in a trading company. Increasingly, our members report that purchasers require vendors to leave certain levels of cash in the business to fund post-acquisition working capital for a period of time (usually 2 to 3 months). Cash levels can vary depending on the nature of the business. Ultimately that cash is repatriated back to the selling entity over time. Clearly, both parties are part of the agreement, as these terms are generally specified in the legal documents. Section 135(3A) catches such situations and they are not specifically excluded in Revenue guidance.

Inserting an exclusion for *bona fide* commercial transactions into section 135(3A) TCA 1997 is critical, to provide the necessary level of certainty to taxpayers and their advisers, when implementing transactions involving the disposal of shares in a company with cash on its balance sheet. This matter has been continually highlighted by advisers since the introduction of this legislative provision and it frequently prevents the sale or transfer of family businesses.

It is worth noting that Revenue has other substantial anti-avoidance legislation to rely on, such as sections 817 and 811C TCA 1997 to address any concerns.

CGT Share Buyback Relief Administrative Recommendations

i. Update Revenue guidance on the Trade Benefit Test

Where a company buys back its shares for a price above the subscription price for the share, any amount in excess of the subscription price, is treated as a distribution by the company subject to income tax at marginal rates in the hands of the shareholder, unless the shareholder meets the conditions of share buyback relief to avail of CGT treatment.

Appendix II of Revenue's Manual on the acquisition by a company of its own shares (TDM Part 06-09-01) provides guidance on the application of the Trade Benefit Test. It outlines situations where a vendor who is selling all the shares but retaining a connection with the company can meet the test.

The guidance states: *"However, there may be situations where:*

- *For sentimental reasons, a retiring director of a company wishes to retain a small shareholding in the company. In this context,* ***Revenue would consider that a small shareholding would not exceed 5% of the share capital of the company****.*

- *A controlling shareholder in a family company is selling his/her shares to allow control to pass to his/her children but remains on as a director for a specified period purely because his/her immediate departure from the company at that time would otherwise have a negative impact on the company's business.* ***Revenue would consider that the specified period that the director remains with the company should not exceed 6 months****.*

  In such circumstances it may still be possible for the company to show that the main purpose is to benefit its trade."

There is nothing in legislation which requires a disponer to dispose of all (or practically all) of his shares and retire from the business. The only requirement under section 178 TCA 1997 is that the vendor's shareholding is substantially reduced and that they are not otherwise connected with the company post buy-back. We believe Revenue's guidance goes beyond the legislative requirements on the basis of an interpretation of what generally benefits a trade.

In most cases the purpose of a buy-back is to allow control and decision-making to pass on to someone else (usually the next generation) allowing them to progress the business trade further. Usually, this would entail embracing new technology and introducing new practices and procedures to improve productivity within the business. Furthermore, in family business situations, the preference of parents in many instances is to pass the business on a gradual basis to children.

Remaining on as a director of the company post buy-back is generally a legitimate benefit to the trade of the company, retaining experience, networks, customer, supplier, staff relationships etc and successfully managing the transition. This can last for much longer than a six-month period. While exiting as a shareholder and ceding control is one aspect, being available as a resource and support for the new owners can be invaluable and a necessary requirement with key customers.

Of course, every case turns on its own facts, but the guidance should be clearer that it is only Revenue's interpretation and it is not legislation, or at the very minimum, it should state that longer periods can be referred to Revenue Technical Service (RTS) to be considered on a case by case basis.

1.1.11 Accelerated Capital Allowances – Energy Efficient Equipment

The cost incurred by a business in investing in energy efficient equipment (EEE) can be relieved for tax purposes through accelerated capital allowances under section 285A TCA 1997. Accelerated capital allowances provide a tax deduction equal to 100% of the costs incurred on qualifying EEE in the year the expenditure was incurred. In our view, the accelerated capital allowances scheme is administratively difficult and is limited in scope. We would recommend the following enhancements to the accelerated capital allowances scheme.

Accelerated Capital Allowances for EEE Legislative Recommendations

i. Widen the scope of the relief beyond EEE to whole buildings that receive a recognised accreditation for overall energy performance.

ii. Remove the condition that the equipment must not be leased, let, or hired, as this precludes landlords and lessors from availing of the relief.

iii. Introduce a tax credit for companies which can be monetised where the company is loss-making for the element of the loss generated by the ACA claim.

iv. Introduce an enhanced rate of relief above the current 100% first-year allowance.

Accelerated Capital Allowances for EEE Administrative Recommendations

<u>Simplify the process to add new products to the approved list</u>

The Accelerated Capital Allowances scheme is administratively difficult and is limited in scope. We would ask that the process for adding new products to the list of eligible EEE, which is maintained by the Sustainable Energy Authority of Ireland (SEAI), is simplified to reduce the delay experienced when new products are added to the list.

This could be achieved by determining the eligibility of a product based on it meeting certain specified performance criteria for its particular product category. For example, the SEAI criteria could be used to determine qualification rather than being based on different individual product codes and registered with the SEAI.

1.1.12 Small Benefit Exemption

Under the Small Benefit Exemption (SBE), an employer may provide up to two small benefits to an employee in a year which are exempt from income tax, PRSI and USC, provided all of the conditions contained within section 112B of the TCA 1997 are satisfied.

Amendments were made to the SBE in Finance Act 2022 to increase the number of permissible benefits from one to two and to increase the maximum amount of the benefits from €500 to €1,000. The objective of the Finance Act 2022 changes was to allow employers greater scope and flexibility to grant tax-free non-cash rewards to their employees, for example in respect of exceptional performance, meeting targets, or increased profits.[12]

Under the new ERR rules for employers, from 1 January 2024, where the SBE applies, an employer is required to return details of the benefit provided to their employees/ directors on or before the benefit is provided to an employee. During the course of discussions between practitioners and Revenue at TALC regarding the application of the new ERR in practice, it has become clear that the current drafting of section 112B gives rise to unintended consequences.

This is because where a benefit provided to an employee satisfies the conditions set out in section 112B, the benefit will automatically qualify for the SBE. An employer cannot opt to tax the first and/ or second benefit received by an employee in a year to allow an employee to avail of the exemption later in the year when further benefits are granted. This can give rise to unexpected outcomes as demonstrated in the following example.

Example
In January, an employer gives their employee, Louise, who is getting married, a bunch of flowers which cost €50. In April, with a view to encouraging staff to increase awareness of the employer's business on LinkedIn, the employer has a competition amongst its staff for the best LinkedIn post. The prize for winning the competition is a €25 voucher. Louise wins the competition. In December, all employees of the firm receive a voucher for €500 to reward them for their hard work during the year.
As the flowers and €25 voucher which Louise received from her employer in January and April are considered benefits which qualify for the SBE under section 112B, the €500 voucher she receives from her employer in December will not qualify for the SBE and will be subject to income tax, USC and PRSI. It is not possible for her

[12] Parliamentary Questions 116 and 126, 1 February 2024

employer to opt to tax either of the benefits received in January or April so that the €500 voucher received in December qualifies for the SBE.

In our view, section 112B should be amended so that the €1,000 limit applies to the cumulative value of the incentives received by an employee in the year of assessment. Retaining the monetary limit of €1,000 but removing the limit on the number of incentives that an employee can receive in a year would mean that employers would have the flexibility to reward and incentivise staff as they see fit.

We consider such an amendment to be in line with the policy intention of the Finance Act 2022 changes to section 112B which were intended to provide employers with greater flexibility to grant tax-free non-cash rewards to their employees up to a maximum of €1,000. Where the €1,000 limit is exceeded, the portion of any benefit received in excess of the limit should be subject to BIK.

1.2. Proportionate sanctions for administrative errors

The Institute recognises the role of penalties in encouraging compliant behaviour by taxpayers. However, it is essential that the penalties which apply for a failure to comply with a tax rule are appropriate.

There are instances in our tax code where the penalties which apply for non-compliance have a disproportionate impact on certain cohorts of taxpayers. There are also cases where the penalties which apply for administrative errors are entirely disproportionate and consequently, undermine the objective of the underlying tax measure.

We have outlined below four areas where we believe that the penalties which apply for errors by taxpayers are disproportionate and should be reviewed.

1.2.1. ERR

Section 897C TCA 1997 which introduced ERR for employers, came into operation with effect from 1 January 2024. The section requires employers to report details of certain expenses and benefits made without the deduction of tax to employees and directors. The items that come within the scope of the ERR are the Small Benefit Exemption (SBE), the remote daily working allowance and travel and subsistence payments.

The Institute fully acknowledges the value of collecting data that will enable the Department of Finance to ascertain the cost to the Exchequer of non-taxable payments/benefits to better inform tax policy. We also recognise the importance of ensuring compliance with the tax rules for such payments, even if they are already subject to robust scrutiny in Revenue’s compliance interventions.

However, it should be recognised that the real time nature of ERR places a very significant administrative burden on employers, in particular smaller businesses who may not have the resources available to larger companies to automate the processes required to ensure compliance with ERR. This burden is further compounded by the fixed penalty of €4,000 which applies where an employer inadvertently omits to report, in real time, a benefit or expense reimbursed to their employee.

Notably, the €4,000 penalty applies notwithstanding there may be no risk of an underpayment of tax. Furthermore, given the real time nature of ERR, the penalty will apply even where an omission is discovered by an employer and is subsequently reported to Revenue at the earliest opportunity.

While Revenue confirmed that it would not seek to apply any penalties for non-compliance for the first six months of 2024, employers face the prospect of a potential fixed penalty of €4,000 for each failure to comply with the ERR from 1 July 2024. In our view, such a penal sanction for failing to comply with a reporting requirement in real time is wholly disproportionate and places an inordinate burden on smaller businesses that have limited resources. We urge that the level of this penalty be reviewed and replaced with a more appropriate sanction.

1.2.2. EII

As outlined in section 1.1.1 of this submission, under existing rules for the EII, administrative errors or delays in the certification and reporting process for EII can result in a full clawback of the relief on the fundraising company which is disproportionate to the error in our view.

For example, where eligible shares are held by a nominee, a failure to file a nominee return (Form 21R) may result in such shares ceasing to be eligible shares and as a consequence, there is no longer a qualifying investment for the purposes of the relief (see sections 494(2) and 496 TCA 1997). This means that there is a clawback of the relief on the company under section 508U TCA 1997. Equally, the filing of a Form RICT without an Eircode number could trigger a full clawback of the relief.

These penal sanctions act as a disincentive for companies to avail of EII. We believe it would be more proportionate for a monetary penalty to be imposed, rather than a clawback of the entire EII relief, as a sanction for an administrative error or the late filing of a return.

1.2.3. KEEP

As detailed in section 1.1.7 of this submission, one of the most significant practical issues that SMEs face when implementing KEEP is the ability to achieve as much certainty as possible that the valuation conditions have been met. For example, that the share option price is not less than the market value of the shares at the date of grant.

Currently, there is no clear guidance on how to determine what market value is for the purposes of the KEEP. If qualifying options are not granted for market value or the market value is subsequently determined by Revenue to be higher than originally projected, the options do not qualify as KEEP options under section 128F TCA 1997, resulting in no exemption from income tax, USC and PRSI on exercise.

Where options are granted at an undervalue within say a certain percentage of the Revenue determined value (for example, 75%), we believe that a more proportionate sanction would be for a charge to income tax to arise on the exercise of the options on the difference between the market value at the date of grant and the option price. This would allow the options to remain qualifying share options, but it would also enable Revenue to collect income tax on the portion of the gain attributable to the undervalue.

1.2.4. SARP

The SARP is an incentive designed to help reduce the cost to employers of assigning skilled individuals in their companies from abroad, to take up positions in the Irish-based operations, thereby facilitating skills transfer and the creation of jobs and the development and expansion of businesses in Ireland.

Where conditions for the SARP are satisfied, an employer must submit and certify a Form SARP 1A within 90 days of the employee's arrival in the State to perform the duties of his or her employment in the State. The 90-day timeframe can be difficult to meet given the multiple practical issues that a new assignee must address upon his/her arrival in Ireland. Often, the new assignee is taking over a senior role in the company, organising housing and schools for their children and in addition, they must obtain a Personal Public Service Number (PPSN). All of this takes time, and in such circumstances, the SARP notification (Form SARP 1A) can be inadvertently overlooked or delayed.

Frequently, the notification may be incomplete because of a delay in obtaining a PPSN. It is possible to submit the Form SARP 1A without the PPSN, however, it will not be considered certified in accordance with section 825C(2AA)(f) TCA 1997 until the PPSN has been added to the Form SARP 1A and the form is successfully 'Certified and Submitted' to Revenue through their online portal.

If the employer fails to certify and submit the Form SARP 1A to Revenue within the requisite timeframe, this can result in the refusal of the SARP relief to an employee, who would otherwise meet the qualifying conditions. We believe that the application of a rule, which makes a relief dependent on the actions of a third party (the employer), is at odds with the basic principle that a relief is personal to the individual and ultimately, must be claimed on the individual's statutory income tax return. There is no obligation on the individual to claim SARP relief during the year, via payroll. Like any other relief, SARP can be (and in many cases, is) claimed by way of a refund at the end of the tax year.

We understand from Revenue that the purpose of the early notification is to gather information for statistical purposes. However, there is a separate statutory requirement obliging employers to provide detailed information on SARP employees and relief claims, on a SARP Employer Return, which is submitted on or before 23 February after the end of each tax year. In addition, it may not be apparent within 90 days that the employee will in fact qualify for or claim SARP. For example, the employee may not meet the tax residency requirement, or their circumstances may change. As such, the value of the information provided at this point is limited.

Refusing the relief on the basis that the employer has not certified and submitted the notice within 90 days can result in what is, in effect, a financial 'penalty' that is entirely disproportionate. For example, where an individual is earning €500,000 per annum, the effective penalty would be as much as €240,000 in total over 5 years, for something that may effectively be outside of their control.

The 90-day timeframe for submitting the Form SARP 1A does not enhance the operation of the relief and it can in fact operate to deny relief in circumstances, which would not be consistent with the underlying policy objective. We recommend removing the 90-day timeframe from the legislation or, at a minimum, removing it from the part of the legislation that defines a 'relevant employee'. This would ensure that the automatic 'penalty' for the employee referred to above, arising from an employer failing to lodge the notice within 90 days of arrival, would not arise.

1.3. Reduce the CGT rate

Ireland's headline rate of CGT, at 33%, is one of the highest in Europe. The rate has remained unchanged since it was increased during the financial crisis. A high CGT rate can result in delays in selling investments that have large unrealised gains. In contrast, reduced capital gains taxes can encourage entrepreneurship because the capital gain payoff from a successful start-up is improved.

In our view, Ireland's high CGT rate is restricting external investment in Irish business. It is also creating reluctant business owners who may hold onto businesses beyond the point where they have capacity to grow them to the scale required to expand into export markets. This dampening effect on productivity and growth in the SME sector is, in our view, evidenced by the low level of CGT receipts in recent years, which fell further in 2023 compared with the previous two years. We know from previous experience that reducing the CGT rate can stimulate activity and increase the yield to the Exchequer.

It is our firm view that applying a reduced CGT rate of 25% applying to active business assets would encourage innovation and productivity and attract more investment in indigenous business.

2. Enhancing Ireland's competitiveness

2.1. Simplify the Irish corporation tax code

Pillar Two reduces Ireland's scope to compete for FDI based on its corporation tax rate. As a result, it is now imperative for policymakers to consider other ways to improve the Irish tax system in order to safeguard Ireland's future competitiveness.

2.1.1. Adopt a branch exemption in tandem with the participation exemption for foreign dividends

As Ireland does not have a branch exemption at present, there can be significant differences in the timing and measure of taxable income for Irish companies between the head office and branches resulting in tax uncertainty and complexity. The Feedback Statement on a Participation Exemption for Foreign Dividends notes that the policy consideration of the merits of a foreign branch exemption are not yet as fully developed and further engagement with stakeholders on this matter is expected in 2024.

In our view, if Ireland is to remain an attractive location for FDI, it is imperative that a foreign branch exemption is introduced in Finance Bill 2024 in tandem with the participation exemption for foreign dividends. Adopting a foreign branch exemption would significantly reduce the administrative burden for Irish companies with foreign branches. It would also copper fasten Ireland's position as a competitive and attractive location for business investment.

The Institute's responses to the Department of Finance's 2022 public consultation on a Territorial System of Taxation,[13] the 2023 technical consultation on the Introduction of a Participation Exemption to Irish Corporation Tax[14] and our Pre-Finance Bill Submission[15] last year, outlined in detail our views on how a foreign branch exemption could be structured together with consequential amendments that policymakers may need to consider on adopting a branch exemption.

2.1.2. Reform Ireland's interest deductibility provisions

The ATAD Interest Limitation Rule (i.e. 30% of EBITDA ratio rule), introduced in Finance Act 2021, was simply layered on top of existing, already comprehensive interest deductibility provisions. This makes it difficult and costly for businesses to operate in Ireland and comply with their tax obligations and has resulted in Ireland having one of the most complicated interest deductibility regimes within the EU. Accordingly, we welcome the confirmation that the Department of Finance is undertaking a review of

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[13] Irish Tax Institute Response to the Consultation on a Territorial System of Taxation, March 2022
[14] Irish Tax Institute Response to the Technical Consultation on the Introduction of a Participation Exemption to Irish Corporation Tax, December 2023
[15] Irish Tax Institute Pre-Finance Bill Submission 2023

Ireland's interest deductibility rules and note that this review is likely to be a multi-year project.

Retaining two separate interest limitation regimes on a permanent basis will increase the cost of borrowing for Irish businesses. Consequently, it is our firm view that tweaking the interest deductibility rules will not be sufficient. We strongly urge that a clear policy decision is taken at the outset of the review to overhaul the interest deductibility provisions to ensure Ireland's reformed regime reflects a broad base for interest deduction against both trading and non-trading income, using the protection of the ATAD Interest Limitation Rule against base erosion risks.

As Ireland has differing rules for trading and non-trading activities, a legislative basis for claiming a tax deduction for interest arising in a non-trading context would need to be established within the Irish corporation tax code, in conjunction with a full removal of section 247 TCA 1997, by incorporating a general test for permitting a deduction for interest expense that is incurred for a business or commercial purpose, similar to the German tax system. Such an approach would ensure that Ireland's interest deductibility rules are easier to administer and more in line with the measures contained in the corporate tax systems of our European counterparts.

In the Institute's response to the Department of Finance's Feedback Statement on the implementation of the ATAD ILR in 2021[16] and in our Pre-Finance Bill Submissions in 2022[17] and 2023[18], we identified the interest deductibility provisions which we believe, following the enactment of the ATAD ILR into domestic legislation, are either no longer required or should be amended.

2.1.3. Eliminate the distinction between trading and non-trading activities

We believe consideration should be given to removing Ireland's schedular tax system and different corporation tax rates. The trading and non-trading distinction between the 12.5% trading rate and passive 25% rate creates unnecessary complexity within the Irish corporation tax code, which businesses do not have to contend with in other tax systems.

Ireland should have only one rate applying to corporates, particularly as the Pillar Two global minimum effective tax rate of 15% has now been implemented. This would help Ireland maintain a clear, competitive, sustainable, and stable taxation policy with regard to its attractiveness to FDI in a rapidly changing global environment.

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[16] Irish Tax Institute Response to the Feedback Statement on ATAD Implementation Article 4 Interest Limitation, March 2021
[17] Irish Tax Institute Pre-Finance Bill Submission, June 2022
[18] Irish Tax Institute Pre-Finance Bill Submission, May 2023

2.2. Reduce the marginal cost of employment for both businesses and individuals

The Irish tax system is strongly progressive, and the tax and social welfare systems combined contribute substantially to the redistribution of income and to the reduction of income inequality. However, Ireland's high marginal tax rates apply at relatively low-income levels by international standards and the country's personal tax base is narrow.

The Institute believes that all income earners should contribute to the Exchequer according to their means and that those who earn most, must contribute most. Spreading the burden according to means would lighten the load on middle income earners. It would also make the Irish personal tax system internationally competitive and incentivise work. We have outlined below recommendations to reduce the marginal cost of employment for both businesses and individuals.

2.2.1. Reduce the marginal income tax rate

The recent and ongoing changes to the international corporation tax system mean that the attractiveness of a country's personal tax system and the cost of employers employing workers in a country will become an increasingly important factor in determining where businesses will locate.

In our view, an objective of any long-term strategy aimed at attracting and retaining FDI should include reducing the marginal cost of employment in Ireland for both businesses and individuals. Feedback from our members would suggest that a marginal rate of tax (including social insurance contributions) set at 50% would help to attract highly skilled and mobile labour to Ireland.

We endorse the view of the Commission on Taxation and Welfare that the tax treatment for all income earners should be aligned and therefore, the additional 3% USC surcharge which applies to self-employed income over €100,000 should be removed, as it does not comply with the principle of horizontal equity.

2.2.2. Taxation of share-based remuneration

Share-based remuneration can play an important role in rewarding key employees at all stages of development of a business. It can also significantly reduce fixed labour costs and free up business cash-flow.

In response[19] to the Department of Finance's public consultation on Ireland's Taxation of Share-based Remuneration, in addition to our proposals regarding the KEEP outlined above, we set out detailed recommendations for amendments to the legislation

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[19] Irish Tax Institute Response to the Consultation on Ireland's Taxation of Share-based Remuneration, January 2024

governing both approved and unapproved share schemes in Ireland and enhancements to the administration of such share schemes. These include:

Legislative Recommendations

- Measures to address the difficulties faced by employees in funding the upfront tax cost arising on the exercise of a share option or receipt of a share award should be introduced. Deferring the tax arising until such time as the employee is permitted to dispose of the shares would mean that the employee is able to fund the tax arising. Alternatively, the removal of the BIK charge on employer loans, or at a minimum, reducing the 13.5% interest rate on such loans to a more commercial rate of interest would make share-based remuneration a more viable option for many companies.

- The broad application of the share buyback provisions in section 176 TCA 1997 can act as an impediment to companies that wish to incentivise employees using share-based remuneration. The disapplication of these provisions in the context of share-based remuneration should be considered.

- Section 128D TCA 1997 can be a useful relief for companies that reward key personnel with shares as it provides a reduction in the taxable value of shares that employees receive, where there is a restriction on selling those shares for a certain period. However, there are several limitations of the relief which need to be addressed such as removing the anomaly where restricted shares are exchanged for shares with equivalent restrictions and expanding the scope of section 128D to include instruments other than shares.

- The current filing deadline for employer returns, which is three months after the year end, should be extended by a least a further month to allow enough time for collation and aggregation of data.

- The tax treatment of Restricted Stock Units (RSUs) should be aligned with the rules followed in other OECD countries and the existing Irish tax treatment for share options exercised by non-residents. This would mean that the amount of the benefit taxable in Ireland would be apportioned by reference to any part of the vesting period during which the individual is present in Ireland, rather than the full amount of the reward where the individual is resident on the date of vesting.

- Section 12 of Finance (No.2) Act 2023 amended the collection mechanism for tax on gains arising on the exercise, assignment or release of a right to acquire shares or other assets under section 128 TCA 1997 so that the gains will no longer be subject to self-assessment but taxed under the PAYE system. The Institute raised concerns with Revenue via TALC following the publication of the Finance Bill, as to how employers would implement this change in practice as the employees would need to be able to fund the tax liability collected through the PAYE system. The 'sell to cover' provision in section 985A(4B) is limited to instances where the *"employer pays emoluments....in the form of shares..."*.

Consequently, in our view, section 985A(4B) is not sufficiently broad to capture liabilities arising under section 128 as these are triggered by the employee exercising a right to acquire shares. We believe that section 985A(4B) should be amended, to put beyond doubt that there is a statutory entitlement on employers to 'sell to cover' where a section 128 gain arises and is required to be subject to PAYE.

Administrative Recommendations

- Clear principle-based guidance on share valuations, including acceptable methodologies and safe harbours, should be provided to support companies that offer share-based remuneration to their employees.

- A key priority for multinational organisations is to minimise the complexity involved in managing their global share-based remuneration plans across multiple jurisdictions with different tax and reporting rules. In our view, it should be possible for an employer to report information on share awards to Revenue via a single annual online return. This would facilitate ease of completion by employers and avoid duplication of reporting.

2.3. Tax measures to promote the green agenda and sustainability

Many jurisdictions are using tax incentives to support businesses in reducing their carbon emissions and to encourage investment in green/energy efficient projects. Indeed, the environmental, social and governance (ESG) frameworks of many multinational groups mean robust climate action policies, including supports for green initiatives, have become key considerations for investors when considering whether to invest in a particular jurisdiction.

In our view, Ireland's current offering in this regard does not compare favourably with competitor jurisdictions. We firmly believe that consideration must be given to tax measures which would support businesses in reducing their carbon emissions. The introduction of tax measures targeting the green agenda would also aid Ireland in achieving its climate change targets. For example, Ireland's location and geographic landscape provide enormous potential for renewable energy. Tax measures could incentivise business to build green energy infrastructure to exploit these renewable energy sources which in turn would assist Ireland in becoming energy self-sufficient and potentially an exporter of green energy.

In our Pre-Finance Bill Submission last year[20] we outlined in detail a number of enhancements to existing tax measures and new tax measures which remain valid and which we consider would improve Ireland's offering to businesses on their journey to decarbonisation and enhance the country's position as a location for sustainable investment. These include:

- Enhancing the existing Accelerated Capital Allowances regime for EEE (as outlined above).
- Extending the CGT participation exemption to early-stage renewable energy projects.
- Re-introducing section 486B TCA 1997 and refine the provisions to encourage investment in sustainable projects and build on Ireland's reputation as a hub for sustainable innovation.
- Extending section 81C TCA 1997 (emissions allowances) to cover carbon offsets in the voluntary sector.
- Enhancing the EII scheme to encourage investment in high-risk ventures which support green or energy efficient projects.
- Introduce targeted measures for green or energy related R&D activities.
- Extending the scope of the relief available in section 664 TCA 1997 to include solar panel activity to incentivise the leasing of farmland for solar panels which would expand the generation of renewable energy and assist Ireland in achieving its climate change targets.

[20] ITI Pre-Finance Bill Submission 2023

3. Tax technical issues arising from the implementation of Pillar Two

Following the transposition of the EU Minimum Tax Directive, to implement the Pillar Two Global Anti-Base Erosion (GloBE) Rules into Irish law in Finance (No.2) Act 2023, a number of issues which require clarification have been identified arising from the GloBE Rules in relation to deferred tax assets on losses. We understand from discussions with Revenue at the TALC BEPS Sub-committee that clarification of these issues would necessitate an amendment to the Irish legislation implementing the GloBE Rules.

3.1 Using FIFO to identify the portion of Irish tax losses attributable to a qualifying loss

With respect to deferred tax assets (DTAs) on losses brought into a Transition Year under section 111AW(2)(c) TCA 1997, the Institute sought Revenue guidance on how taxpayers should identify what portion of the Irish tax losses are attributable to a qualifying loss. We recommended that taxpayers would be permitted to apply a First In First Out (FIFO) approach in this regard, focusing their analysis on the most recent losses first when seeking to analyse whether the losses are attributable to a qualifying loss.

Revenue has confirmed at TALC BEPS that they cannot provide such guidance because the timing of such loss relief claims could have an Exchequer impact and therefore, a legislative amendment would be required to determine how existing Irish tax losses are attributable to a qualifying loss for Pillar Two purposes. Accordingly, we request a legislative amendment to be included in Finance Bill 2024 to allow taxpayers to apply a FIFO approach in this regard.

3.2 Order of use of tax losses forward for GloBE purposes

We sought confirmation in Revenue guidance, where a deferred tax asset is recognised on transition in respect of amounts attributable to a qualifying loss (i.e., brought into GloBE at 15%), as well as other tax losses forward (e.g., brought into GloBE at 12.5% with respect to Irish trading losses), regarding the order of use in future years when the losses forward are utilised. This will be relevant where the losses attributable to qualifying income and other losses form a single pool for domestic tax purposes and are recognised as a single asset in the taxpayer’s financial accounts.

Revenue confirmed at TALC BEPS that a legislative amendment is required to confirm this. Therefore, we request a legislative amendment to be included in Finance Bill 2024 to allow taxpayers the flexibility to elect which loss is used for GloBE purposes in these circumstances.

3.3 Recast of historical losses for GloBE purposes

Pillar Two Rules state that historical Loss DTAs can be uplifted from 12.5% to the 15% rate where the loss is equivalent to a GloBE loss. In scenarios where companies determine that a portion of the losses brought forward equate to a GloBE loss and are subsequently recast and there is a portion which does not equate and as such, is not recast, it is not possible to determine which are used against future taxable income from an Irish tax perspective.

We sought clarification in Revenue guidance that in such scenarios the DTA that has been recast (i.e. that equates to a GloBE Loss) should be unwound in the first instance. As Revenue confirmed at TALC BEPS that this would require a legislative amendment, we request that such an amendment be included in Finance Bill 2024 to address these circumstances.

4. Tax technical measures required to mitigate certain unintended consequences

We have identified several technical measures which, in our view, require a legislative amendment in order to mitigate certain unintended consequences.

4.1. Residential Premises Rental Income Relief

Residential Premises Rental Income Relief, which was introduced in Finance (No.2) Act 2023 and is contained in the new section 480C TCA 1997, is intended to incentivise residential landlords to remain in the private rental market. The amount of relief allowable for each year is restricted to the lesser of: €600 in 2024; €800 in 2025; €1,000 in 2026 and 2027; or 20% of the landlord’s rental profit from rented residential premises for the year.

It would appear that the clawback provisions in section 480C do not work properly as the clawback is assessable at marginal rates whereas the relief will only have been granted at a rate of 20%. We understand from discussions with Revenue at the TALC Direct/Capital Taxes Sub-committee that this was not the policy intention. In our view, it is important that this technical issue is addressed in Finance Bill 2024 as otherwise it could disincentivise landlords from availing of the relief.

4.2. Rent Tax Credit: Definition of specified amount

Finance (No.2) Act 2023 was intended to increase the amount of the Rent Tax Credit from €500 to €750, and in the case of jointly assessed taxpayer units, from €1,000 to €1,500, for the years of assessment 2024 and 2025.

Section 473B(2) TCA 1997 provides that the Rent Tax Credit is the lower of 20% of the rent paid, 20% of the "specified amount" (i.e. €5,000 for jointly assessed or €2,500 otherwise) or an amount which reduces the income tax to nil.

Section 473B(13) was amended by Finance (No.2) Act 2023 to provide that the aggregate credit shall not exceed €750 or €1,500 if jointly assessed. However, as the definition of specified amount was not also amended, it is unclear that the increased Rent Tax Credit applies as intended.

In our view, the definition of specified amount should be amended to ensure that the increase in the amount of the Rent Tax Credit from €500 to €750 (and in the case of jointly assessed taxpayers from €1,000 to €1,500), for the years of assessment 2024 and 2025, applies as intended.

4.3. Agricultural Relief: Where land is part farmed and part leased

To qualify for Agricultural Relief from CAT, section 89 CATCA 2003 provides that the value of the agricultural property received by the beneficiary must consist of at least 80% of the total property value held by the beneficiary on the valuation date.

For gifts and inheritances taken after 1 January 2015, on the valuation date the beneficiary must:

- farm the agricultural property on a commercial basis for at least six years from that date; or
- lease the property to someone who farms the agricultural property on a commercial basis for at least six years from that date.

If the beneficiary leases the land, they must lease "*substantially the whole*" of the agricultural property. Revenue has confirmed in guidance that they will accept that substantially the whole of the property means "*at least 75% of the property by value".*

However, if a beneficiary wishes to farm 50% of the land and lease 50% of the land, they will not qualify for agricultural relief as section 89 CATCA 2003 does not currently provide for a situation where a beneficiary part farms and part leases the land (subject to a specific exception that applies where land is leased for solar panels). In our view, section 89 CATCA 2003 should be amended so that agricultural relief can apply in circumstances where a beneficiary part farms and part leases the land.

4.4. De-grouping under section 623 and previous mergers

Section 617 TCA 1997 provides that where a member of a group of companies disposes of an asset to another member of that group, the transaction is treated as being for such consideration as would give rise to no gain/ no loss on the disposal. There is a clawback in section 623 TCA 1997, which provides that where a company ceases to be a member of a group, any asset which it acquired from other group members within ten years of the date of leaving the group is deemed to be sold, and immediately re-acquired by the company leaving the group at market value, at the date of acquisition from the other group company. The provision effectively re-instates the charge to CGT deferred under section 617 TCA 1997.

Section 623 is intended to prevent the avoidance of tax on capital gains by a company transferring assets with a built-in gain to a newly formed subsidiary company and then disposing of the shares in that company in circumstances in which no liability, or a reduced liability, to CGT arises. However, an exception to this general provision is provided for in section 623(3) which applies where there is a transfer of assets from one associated company to another associated company and companies leave the group at the same time, while continuing to be in a group relationship with each other.

A merger by absorption is effected where one company, on being dissolved without going into liquidation, transfers all of its assets and liabilities to a company that is the holder of all of the shares representing the capital of the first-mentioned company. Where a domestic merger by absorption occurs between two Irish companies in a group, there will generally be a transfer of assets that meets the requirements of section 617 TCA 1997. Revenue has confirmed at the TALC Direct/Capital Taxes Sub-committee that a charge to CGT would arise if there is a subsequent disposal of the Irish subgroup containing the transferee within 10 years of the merger by absorption, as section 623(3) does not apply in those circumstances.

In our view, section 623(3) TCA 1997 should be extended to ensure that no clawback applies where there is a merger by absorption followed by a disposal of the Irish subgroup containing the transferee.

4.5. Withholding tax on patent royalty payments to another Irish group company

As a general rule section 238(2) TCA 1997 requires that on the making of a royalty payment or other sum paid in respect of the user of a patent, the payer is obliged to deduct out of the payment income tax (WHT) at the standard rate of 20%. Chapter 6 of Part 8 TCA 1997 provides an exemption from WHT for royalty payments made to an associated company resident in another EU Member State, and section 242A TCA 1997 provides that WHT will not apply to royalties paid by a company in the course of a trade or business to a company resident in a treaty country.

However, there are instances where an Irish company is required to apply WHT on patent royalty payments to another Irish group company. This requirement can result in a large preliminary tax obligation for the payer company while the recipient company cannot claim the WHT credit/ refund until its corporation tax return and iXBRL Financial Statements are filed. The timeline between payment of the initial instalment of preliminary tax (PT1) and the refund paid by Revenue is circa 20 months. This creates a significant cashflow disadvantage for such Irish companies even though the Exchequer remains in the same position.

Example
Two Irish companies (IreCo A and IreCo B) are part of the same worldwide group but which are owned by intermediate holding companies in the USA and Switzerland. IreCo A is required to withhold income tax on the basis that it does not meet either of the exemptions from WHT that typically apply on group royalty payments, as follows:
Section 242A TCA 1997 provides that patent royalty payments can be paid without the deduction of WHT where they are paid to companies that are tax resident in relevant territories. For the purpose of section 242A TCA 1997, relevant territory is defined as EU Member States, other than Ireland, or a country with which Ireland has a tax treaty. Irish tax resident companies are not afforded the benefits of section 242A TCA which

are available to companies which are tax resident in EU Member States or tax treaty countries, presumably as it is expected that section 410 TCA 1997 would apply in most cases.

Section 410 TCA 1997 provides an exemption from Irish WHT on payments to companies within the same EU/ EEA group. However, IreCo A and IreCo B do not meet this condition because US and Swiss intermediate holding companies break the EU/ EEA group requirement.

Section 411 TCA 1997 (group losses provision) was amended in Finance Act 2012 to expand the legislative definition of qualifying groups for corporation tax loss relief purposes. The amendment was in response to a European Court of Justice case,[21] in respect of similar tax legislation in the UK, which highlighted the discriminatory nature of the pre-2013 definition of a qualifying group that precluded group formation between certain Irish tax resident companies on the basis that they were subsidiaries of non-EU resident companies.

The amendment extended the group relief rules so that losses can be transferred between two Irish resident companies where both companies are part of a 75% group involving companies who are (a) resident in a jurisdiction with whom Ireland has a treaty, or (b) quoted on a recognised stock exchange.

While section 411 TCA 1997 was amended in 2012, no corresponding amendment of section 410 TCA 1997 (i.e. WHT exemption provision) was made. It is our view, this was an oversight which could, in the event of a legal challenge, be found to be in contravention of the ownership non-discrimination article of Ireland's double tax agreements with the USA and Switzerland.

[21] FCE Bank plc v HMRC