



**Irish Taxation
Institute**

Educating, Developing & Representing

Pre-Budget 2010 Submission

Fostering Economic Activity and Innovation

October 2009



Irish Taxation Institute

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Budget 2010

The Irish Taxation Institute (ITI) is the leading representative body for taxation affairs in Ireland. ITI is a centre for thought leadership and is a balanced and authoritative voice on tax policy matters.

The Irish economy faces very significant challenges in the coming years. To meet these challenges we need to carefully plan a route towards economic recovery that includes a strategic use of tax policy. Our taxation policy should enhance the competitive strength of our economy and bring some stability to revenue yield. This will not be achieved easily.

We support recent comments by the Minister for Finance that there is no scope for further tax increases in Budget 2010. The ITI believes that any further tax burden on the business or personal taxpayer would be counterproductive – it would discourage enterprise and innovation at a time when they are critically needed. Budget 2010 provides an opportunity to bring certainty to key elements of our tax policy and to make some innovative changes to our tax code at little or no Exchequer cost. This Budget Statement should be used to send out a clear message that Ireland remains open for business and that we will maintain a tax environment where enterprise is fostered, innovation is encouraged and high-value jobs can be created.

In this context we are proposing that:

- There should be no increases to personal taxation introduced in Budget 2010
- We should set a target in this Budget to reduce the aggregate marginal rate of tax, PRSI and levies from its current level of 55% to below 50% by 2012.
- There should be a restatement of our absolute commitment to our 12.5% corporate tax rate.¹

¹ We welcome the guarantee in the Renewed Programme for Government that the 12.5% rate will remain.

- The Budget Statement should set out clearly the tax treatment of residential property over the coming three years²
- There should be no reduction in the tax incentive for pension provision included in Budget 2010.
- To stimulate job creation, new businesses should be exempt from Employer PRSI for the first three years in respect of the first ten jobs created.
- The rate of interest charged on business and self-assessed individual taxpayers needs to be reduced from the current penal levels of 8 to 10% and aligned with commercial rates – hard pressed taxpayers who are struggling to make their payments on time should not be severely penalised by the State for their current cash-flow difficulties

Our detailed recommendations are set out below under four main themes:

- **Certainty in the tax system**
- **Fostering economic activity and innovation**
- **Retaining and attracting human capital**
- **Tax Administration**

1. **Certainty in the tax system**

The recently published Commission on Taxation Report provided a welcome overview of the tax system.³ However the Report together with subsequent media and international speculation has resulted in uncertainty regarding certain aspects of our tax policy. This has extended to areas where the Commission Report was unambiguous. Budget 2010 provides an ideal opportunity to Government to restore certainty on these issues to taxpayers and to key international audiences. All taxpayers deserve certainty regarding their tax affairs – business, in particular the international business sector, requires certainty in tax policy if they are to make investment decisions that benefit Ireland.

We propose that:

- The commitment to our 12.5% corporation tax rate should be reaffirmed in Budget 2010. We welcome the guarantee included in the Renewed Programme for Government that the 12.5% rate will remain.
- Levies should be phased out and integrated with income taxes. The emergency income levy, which was intended as a temporary measure, should be removed prior to 2012
- Personal taxes should not be increased in Budget 2010 and the combined marginal rate of income tax and PRSI should be reduced below 50% by 2012.

² The Renewed Programme for Government includes a proposal to introduce a Site Valuation Tax (SVT). This will be a major administrative project. Budget 2010 should provide as much detail as possible regarding the timetable for the introduction of the SVT.

³ A number of the recommendations in our submission are also made in the Commission on Taxation Report.

- Family businesses (including farms) play a key role in the Irish economy and provide a very stable and valuable source of employment. To encourage enterprise and job creation and to avoid stagnation of businesses it is important that retirement relief from capital gains tax is retained and is not restricted. Furthermore, business relief and agricultural relief from capital acquisitions tax should not be restricted.

These reliefs are vital to encourage the passing on of the family business and farm to the next generation in a manner that preserves the business, protects existing jobs but allows fresh thinking and energy to drive and develop the business.

Individuals and businesses are incurring great difficulties in sourcing financing. If additional tax becomes payable on such transfers of businesses, it is likely to result in the break up or sale of businesses with consequent job losses. While a restriction of these reliefs might result in some additional tax yield in the short term we believe that it would be highly counterproductive in the long term, it would cost us jobs and sustained future tax yield.

- The PRSI system should be subject to an overall review to ensure it is fit for purpose. We note the proposal in the Renewed Programme for Government to remove the cap on employee PRSI contributions. We recommend that this cap should not be removed until this review has been completed.
- There is a need for certainty in respect of the Government's intentions on the taxation of property. The Renewed Programme for Government proposes the introduction of a Site Valuation Tax (SVT). We believe that the administration of such a tax requires a very significant degree of advance preparation including a single, national property registration system. Budget 2010 should include a timetable for the introduction of an SVT and the preparatory work required by the State, Revenue and local authorities and the taxpayer base. A move to an SVT should be matched by a removal of the stamp duty charge and provision should be made for credit against the SVT for stamp duty already paid on the property.
- Given the fluctuations in tax receipts from transactional taxes, to stabilise the Irish tax system there is a necessity to broaden the tax base. While tax reliefs and exemptions may reduce the tax base, many serve a valid and desirable purpose and should be retained. We have previously recommended a structure to certify and assess tax incentives to ensure they deliver on their objectives.⁴ Those expenditures which no longer serve a valid economic or social purpose should be removed. However incentives that have the potential to create jobs and assist in our ambitions to build a world class, innovation-centred economy, such as the patent exemption, should be retained. Government should clarify its intentions in this regard.
- The tax exemption for patent royalties encourages innovation and invention and should form an important part of our Smart Economy. The patent exemption should be retained and modified to ensure it promotes our Smart Economy ambitions.

⁴ "Proposals for a certification process for tax incentives and exemptions" – Report to Oireachtas Committee on Finance and the Public Service – November 2005

- No changes should be made to the current tax measures to encourage taxpayers to provide for their pensions. Now is not the time to remove assistance to taxpayers to fund their own pensions, thereby reducing the future burden on the State. We note that the Renewed Programme for Government proposes moving to a single 30% rate of tax relief for pension contributions. We strongly recommend that this proposal is not acted upon before stability is restored to our public finances and analysis is undertaken of the negative impact such a move would have on pension provision by taxpayers paying tax at the marginal rate.

The current system of allowing relief for pension contributions at the individual's marginal rate reflects the fact that the relief is in fact a deferral of taxation and not tax permanently foregone to the Exchequer. A reduction in the rate of marginal pension relief undermines this deferral position and could discourage many middle income earners from making adequate pension provision.

2. Fostering economic activity and innovation

Ireland is currently experiencing a significant economic downturn which has resulted in a sharp rise in unemployment and deterioration of public finances. To create additional employment we must encourage business enterprise and innovation. In addition, to continue to attract foreign investment to Ireland we must retain our competitiveness and consider introducing new, innovative tax measures. To emerge from the economic downturn we must incentivise and reward business activity and job creation. In this regard, ITI makes the following proposals:

- The relief from corporation tax for start up companies should be extended to companies commencing business beyond 2009 and the duration of the exemption should be maintained at three years. The relief for start up companies should also be extended to unincorporated businesses.
- Some companies have significant cash reserves which, due to high rates of personal taxes, have not been distributed to shareholders. To encourage the distribution of these reserves a reduced income tax rate (25%) could be introduced to apply to distributions. This also is in line with the Commission on Taxation's recommendation to equate the rate of tax on dividends to the rate applying to deposit interest. This should encourage the distribution of cash currently locked in companies and should further encourage investment in businesses.
- To incentivise productivity and to ensure employees participate in business growth, the current exemptions from income tax, levies and PRSI should be retained for share based remuneration schemes and the SAYE share option scheme should be extended to permit a broader range of employee purchase plans be eligible for the relief.
- To stimulate job creation, new businesses should be exempt from Employer PRSI for the first three years in respect of the first ten jobs created.

- To alleviate the current levels of unemployment and to encourage people to upskill, unemployed individuals should be entitled to off-set any costs incurred on retraining against income tax over the previous three years.
- The Business Expansion Scheme (BES) and Seed Capital Scheme (SCS) have played a key role in supporting enterprise and employment in Ireland. These reliefs should be simplified and broadened in scope and should be extended to fully support the green economy.
- Unilateral credit relief for foreign withholding tax on royalty payments should be extended to all trading companies and a foreign pooling system should be introduced for foreign withholding tax credits.
- Companies should be given the flexibility to offset the Research & Development tax credit either against its corporation tax liability or against certain payroll costs. This can be done at no cost to the Exchequer.

3. Retaining and attracting human capital

Much of Ireland's recent success in attracting foreign direct investment has resulted from our commitment to a low corporate tax rate and attractive tax credit regimes. To remain competitive and to continue attracting foreign investment we also need to concentrate on attracting human capital. While equity must remain a core principle of the Irish tax system, there are circumstances which warrant deviation from this principle. We should offer incentives to foreign executives to locate in Ireland. Such an approach would strengthen our ability to attract and retain significant foreign direct investment projects with the knock-on benefits of increased employment and increased tax revenue.

The current remittance basis of taxation has been of particular assistance in attracting executives and specialists with key skills to Ireland. It bolsters Ireland's reputation as an open and progressive economy and should be retained or enhanced.

A new regime was introduced in Finance (No.2) Act 2008 for skilled foreign employees assigned to work in Ireland. It is unclear as yet what the impact of this rather limited regime will be though ITI believes that it should be retained and its scope extended to cover all jurisdictions, including the EU.

To compete with other jurisdictions in attracting foreign investment, the Government should consider further innovative measures to attract human capital. The Netherlands, for example, grant a special tax free allowance of 30% of salary to certain skilled foreign employees who are assigned to a post with a domestic employer. This is paid in addition to employees' pay and is seen as reimbursement of the extra costs of living outside the homeland.

The Renewed Programme for Government proposes reform to Ireland's tax residency rules. Our current residency rules are based on days spent in the country and provide a stable and certain basis of assessing residency. If any changes are made to the residence rules for individuals they should avoid uncertainty and should be in accordance with the rules that apply in comparable jurisdictions.

4. Tax Administration

While Ireland is a competitive and efficient place to do business, it continuously faces enhanced international competition and therefore must continue to focus on reducing administrative burdens on business. In this context we propose:

- The Appeals process for all taxpayers should be fair and cost efficient.
- The decisions of the Appeal Commissioners should be equally available to taxpayers and Revenue.
- Interest rates on overdue tax should reflect commercial market rates and international standards. The reduction in the rate charged earlier this year was very welcome. However there is still a very large gap between the rate charged and commercial rates. We are also charging significantly more interest on tax underpaid compared to the UK. A great many viable businesses are now struggling to pay their full tax liability on time. All businesses are facing very significant cash-flow difficulties. The Exchequer should not severely penalise taxpayers at such a perilous time- rather our framework should support them in their efforts to keep their business going and protect jobs.
- The general anti-avoidance rules should be reviewed and the four year time limit for Revenue to form an opinion should be reinstated
- Self assessment rules should be extended to other areas including CG50 clearance certificates, dividend withholding tax, and withholding tax on interest and royalty payments.
- The close company surcharge for service companies should be abolished
- The relevant “small company” threshold should be raised over successive Budgets so that all companies should eventually be entitled to compute preliminary corporation tax based on their prior year’s tax liability.
- The rate of Relevant Contracts Tax (RCT) should be reduced in line with the standard rate of income tax.
- In bona fide situations interest and penalties for RCT and VAT should be waived where there has been a technical default but no loss to the Exchequer.