Review of the Corporation Tax code

A submission to the Department of Finance
4 April 2017

Review of the corporation tax code
Tax Policy Division
Department of Finance
Government Buildings
Upper Merrion Street
Dublin 2.

VIA EMAIL: cctcodereview@finance.gov.ie

Dear Sirs/Mesdames:

We are pleased to submit comments on behalf of Deloitte in response to your call for public consultation on the review of the corporation tax code. We appreciate this opportunity to share our views and trust that you will find our comments valuable to the discussion.

We look forward to continued collaboration with the Department of Finance on this and other tax initiatives and are available to discuss anything in this document, as needed. In the meantime, if you have any queries please do not hesitate to contact either Tom Maguire, Tax partner, or myself on 01-417-2200.

Yours sincerely,

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Lorraine Griffin
Partner
Head of Tax and Legal
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Key Recommendations and Messages

For the past number of years international tax debate has intensified in several areas as a result of countries desires to protect and enhance their own tax base. The OECD Base Erosion and Profit Shifting (BEPS) consultative period has come to a conclusion and the implementation phase has now commenced. The EU has accelerated this phase through agreement on the Anti-Tax Avoidance Directives (ATADs 1 and 2) and has gone further than BEPS in several respects. These substantial changes run parallel with international political and economic disruption brought about by Brexit, the impact of US corporate tax reform, the EU's proposed Consolidated Corporate Tax Base (CCTB) and State Aid challenges from the European Commission. In that context, we welcome the fact that the Minister for Finance is seeking feedback from interested parties on a review of Ireland’s Corporation Tax Code.

There is now strong competition among countries in the European and Asia Pacific regions for foreign direct investment (FDI). Various countries offer different structures and incentives to attract such investment. With the globalisation of trade, the increasing value of intangible property (IP) to business and the dominance of technology in global industry, we acknowledge the context and impetus for the OECD BEPS project and the EU ATAD in seeking to align profit allocation with all facets of global business operations. Ireland should take every step to continue its strong track record in attracting foreign direct investment, and particularly MNCs who perform high value activities in their Irish operations.

In particular, given the abovementioned international developments, it is necessary to develop, encourage and incentivise the domestic corporate and entrepreneurial sector. We have commented on the specific questions raised in the public consultation document. Within Questions 3 and 4 we have broadly structured our response into two areas, FDI and the domestic corporate sector but it is important to note that the issues are not mutually exclusive while recognising the overlap between the sectors.

In our view that the following priority measures should be addressed in any proposed reform of the corporation tax code:

- On implementation of the BEPS and ATAD measures, we note Ireland’s desire to engage in best practice globally. Consideration should be given to the significant downsides to adhering to non-mandatory BEPS provisions as part of the ongoing Multilateral Instrument (MLI) negotiations. Further, in the case of mandatory BEPS and ATAD measures, consideration should be given to adopting the least onerous implementation options (and by definition the most attractive choices for investors) within those provisions e.g. the selection of the genuine arrangements exclusion within the proposed Controlled Foreign Company (CFC) rules.

- We recommend a reform of a number of areas of the corporation tax code which are of particular relevance to companies looking to base holding, treasury or equivalent operations in Ireland including
  i. Provisions regarding the tax deductibility of interest on borrowings used to acquire companies or assets,
  ii. Provisions applying relief from double taxation,
  iii. Tax efficient repatriation of income and the taxation of gains through participation exemption, including following recent proposed UK changes
which seek to remove the ‘trading’ requirement for the participation exemption to apply on share disposals in certain instances,

iv. The introduction of a notional equity deduction as suggested as part of the EU’s CCCTB proposal which would allow businesses to deduct a notional yield on equity increases.

By international standards the Irish provisions in these areas are overly complex and make Ireland a less attractive jurisdiction for those financing such investments. At a time when Ireland is faced with competition from Paris, Frankfurt and Luxembourg in its efforts to ‘win’ high-value financial services business post-Brexit, it is critical that the above measures be addressed to ensure Ireland is a highly attractive location for companies in such industries who are seeking to rebase their EMEA or global operations.

- Certainty is a key component of tax competitiveness, and the ability of Ireland to deliver tax certainty to investors make it a significantly more attractive jurisdiction for inward investment. As such we have recommended various measures be taken to provide taxpayers with greater certainty. These include the publication of redacted Revenue opinions, the introduction of consultation periods for key pieces of proposed tax legislation and increased Dáil debate on tax law.

- To ensure a comprehensive tax approach to the management and use of IP, which remains central to global and country specific economic development, we recommend that issues relating to supporting innovation through the R&D tax credit are addressed and to ensure that section 291A TCA 1997 can be made as attractive as possible by allowing its current amortisation continue notwithstanding financial reporting standards may not allow for amortisation into the future. Further, additional enhancements would include the ability to transfer such IP intragroup while maintaining capital allowances thereon. Consideration should also be given to allowing certain amendments which would alleviate the financial accounting requirement to recognise deferred tax assets on such IP.

- We have recommended a number of measures to grow the domestic corporate sector, such as
  i. The introduction of a notional equity deduction as suggested as part of the EU’s CCCTB proposal. Given 37% of Irish domestic small and medium enterprises have no debt it is appropriate that companies who are predominately equity financed are provided with similar reliefs afforded to those who are more heavily geared,
  ii. With a tax policy objective in mind of maximising the funds available for re-investment in the company, start-up companies could, by election, be treated as transparent for tax purposes for the first three years. This would provide for more efficient use of start-up losses at a critical time in the life cycle of a business by allowing entrepreneurs to offset certain business losses against their own taxable income,
  iii. The introduction of a refundable start-up company credit, which would be a more relevant relief for start-ups dealing with the commercial difficulties (which to a large extent revolve around cash flow) they typically face.
  iv. Review of the close company surcharge. The majority of Irish domestic enterprises are closely held, and the surcharge acts to actively discourage the reinvestment of funds to grow such businesses,
  v. Consider following the UK in its recent reforms regarding the treatment of corporation tax loss utilisation. Among the new UK reliefs British companies will have total flexibility on how current year reliefs are set against trading and non-trading profits.
We have also outlined a number of corporation tax incentives currently in operation across the EU which should be considered from an Irish perspective.

- Of course, Brexit is a key concern. There are many provisions within Irish law which look to countries being a member of the EU or at least the EEA. An example is the legislation dealing with capital gains tax groups whereby all companies within that group must be resident in the EU or an EEA state with which Ireland has a tax treaty. Where an asset is transferred within a group and a company leaves the group with that asset within 10 years then the deferred capital gain may crystallise for capital gains tax purposes. Post Brexit it is conceivable that such groups may suffer such a charge in the absence of relieving legislation where a group is no longer in point at that time. Given our key economic ties with the UK then relieving legislation would be necessary for this and other domestic provisions which require EU/EEA membership before benefits can apply.

- In light of the abovementioned competitive pressures we therefore recommend that Ireland considers all necessary steps to remain a highly attractive jurisdiction from an FDI perspective, up to and including a potential reduction in the headline 12.5% corporation tax rate.

- Given corporation tax policy cannot be successful in isolation, we have also noted several areas below which we feel should be addressed in tandem with corporation tax reform. Such areas include the improvement of share option schemes to encourage company ownership, addressing the current housing crises, measures to make lending to the domestic sector more attractive and income tax reform. The domestic sector is a key engine of the economy employing over 900,000 individuals in Ireland. Our view is that this sector is key to the next phase of Irish economic growth. It is time that significantly more focus is placed on this sector to make starting and scaling a business both more attractive and crucially more viable. Measures that encourage rather than penalise investment and reinvestment in closely held businesses would be welcome as would measures to provide for increased cash flow at the critical early stage of a business.

If one could summarise the approach taken in this document it would be to acknowledge that over recent years Ireland has constructively engaged with OECD and EU international tax discussions. Further the measures suggested argue that Ireland should not seek to implement what may be perceived as a best in class regime if it puts us as at the back of the class in terms of attractiveness; it is our “force of attraction” which should be our primary focus from now on. It is certain that Ireland has and will implement what is required of it but the focus now needs to be on enhancing our attractiveness to investment, foreign and domestic. Others are doing the same and this is not the time to be left behind.
Responses to Consultation Questions

1.0 Question 1

*What additional legislative measures, if any, should Ireland take to achieve the highest international standards in tax transparency, having regard to the benefits which may accrue to developing countries from enhancing global tax transparency?*

1.1 Continue to engage with global reform

It is important to acknowledge that Ireland has been an active and engaged participant in the global drive for tax transparency. Ireland has been constructive in signing up to new standards on the exchange of tax information between countries and has continued to implement global best practice in this regard. Ireland has been an engaged member in the BEPS project and has consistently attained the highest international standards on transparency.

In addition to the above global policy measures Ireland is an engaged member in the EU’s Code of Conduct Group and the OECD’s Forum on Harmful Tax Practices. As a member of the G20, Ireland has long been a constructive participant in the global debate regarding tax fairness. Ireland signed up to the BEPS recommendations in October 2015 and has been an early mover in implementing its recommendations. We understand the Irish government will also sign up to the OECD Multilateral Instrument (MLI) later this year.

To continue to achieve the highest international standards in tax transparency Ireland should therefore continue to constructively engage, as it has always done, in determining the requirements to be imposed by the various global tax policy bodies to which it is a party. That said, Ireland’s commitment in this regard is clear given the level of engagement and acceptance that has been undertaken over the past number of years and we outline a number of examples below.

*Country by Country Reporting*

An example of Ireland’s active participation in the global drive for tax transparency has been the early adoption of BEPS Action 13, Country by Country (CbC) Reporting, which was introduced in Finance Act 2015. The adoption of this legislative measure will require taxpayers to articulate consistent transfer pricing positions, and will provide tax administrations with useful information to assess transfer pricing risks. Developing countries which fulfil the conditions of confidentiality, consistency, and appropriate use, may obtain the data provided by MNCs in their country-by-country reports under exchange agreements, or in certain circumstances through local filing.

Ireland as an early adopter of CbC is an engaged participant in the drive towards tax transparency as it pertains to developing countries.

*Automatic Exchange of Information*

Ireland has also signed up to the Convention on Mutual Administrative Assistance in Tax Matters, which provides for the exchange of information, including simultaneous tax examinations and participation in tax examinations abroad. Over 100 jurisdictions have

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1 http://www.oecd.org/tax/transparency/exchange-of-information-on-request/ratings/#d.en.342263
2 http://www.oecd.org/ctp/beps-frequentlyaskedquestions.htm Q83
signed up to this convention, including an increasing number of developing countries⁴.
The Convention is the most comprehensive multilateral instrument available for all forms
of tax co-operation to tackle tax evasion and avoidance, a top priority for all countries⁵.
Ireland’s participation in the Convention is a demonstration of its active commitment to
the highest international standards in tax transparency, particularly with regard to the
benefits which may accrue to developing countries.

Within the EU Ireland also implemented updates in respect of the EU Directive on
Administrative Cooperation. This will enable the exchange of tax rulings and Advance
Pricing Agreements (APAs) between Member States.

Common Reporting Standard

The Common Reporting Standard (CRS) is a new, single global standard on Automatic
Exchange of Information. Irish financial institutions will be required to submit CRS
information to Revenue by 30 June each year with the first returns due by 30 June 2017.
Legislation to implement the CRS in Ireland was introduced in Finance Act 2014 by
inserting Section 891F of the Taxes Consolidation Act 1997, and Regulations (Statutory
Instrument 583 of 2015) came into effect on 31 December 2015. Ireland was an early
adopter of CRS⁶. Automatic Exchange of Information is broadly recognised to be a
positive step for global transparency, and developing countries are encouraged to
participate in the new global standard⁷.

Foreign Account Tax Compliance Act

The Foreign Account Tax Compliance Act (FATCA) is aimed at combating tax evasion by
improving exchange of information between tax authorities in relation to U.S. citizens
and residents who hold assets off-shore. In December 2012, the Minister for Finance, on
behalf of the Government, signed an agreement with the U.S. in relation to the
implementation of FATCA in Ireland.

The Agreement provides for the automatic reporting and exchange of information on an
annual basis in relation to accounts held in Irish Financial Institutions by U.S. persons,
and the reciprocal exchange of information regarding U.S. Financial Accounts held by
Irish residents. Ireland was the fourth country in globally to sign up to this agreement,
and it is another example of Ireland’s commitment to international tax transparency.

Multilateral Instrument

The Irish government has indicated that it will sign up to the OECD MLI later this year⁸.
The MLI, through its provisions on Mutual Arbitration Procedure (MAP) will require
countries to exchange information in solving any tax disputes. The availability of such
information to developing countries would form part of Ireland’s commitment to
enhancing tax transparency. It is not been officially indicated which provisions of the MLI
Ireland will sign up to, but the signing up to provisions such as the MAP would
demonstrate Ireland’s continued commitment to tax transparency.

Public Country by Country Reporting

The European Commission proposed a directive which would require Public CbC
Reporting of tax and other financial data by large companies with operations in the EU.
While Ireland engaged constructively in discussions regarding Public CbC Reporting, it

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ultimately sent a reasoned opinion to the European Commission objecting on grounds of subsidiarity.

1.2 Expansion of Tax Treaty Network

Treaty Network

All of Ireland’s Double Tax Agreements (DTAs), which are given the force of law under Section 826(1) TCA 1997, contain exchange of information provisions\(^9\). Ireland currently has 72 DTAs in effect. However only a small number of these are with developing countries\(^10\). Ireland also has Tax Information Exchange Agreements (TIEAs) in effect with 23 jurisdictions, which are given force of law under Section 826 (1B) TCA 1997\(^11\).

Ireland should to continue to expand the DTA or TIEA network to include more developing countries. This would provide an additional channel for information exchange with developing countries, in addition to those already outlined above. Further the reader is directed to our previously submitted response to the public consultation on the proposed US tax treaty and our recommendations for same.

\(^9\) Exchange of Information
2.0 Question 2

**What additional legislative measures should Ireland take to further implement the actions of the OECD initiative to combat BEPS?**

Ireland, along with more than 100 jurisdictions, participated in negotiations on the MLI which has as its aim the swift implementation of a series of tax treaty measures to allow for adherence to international tax rules. The new instrument will transpose certain aspects from the BEPS Project into more than 2,000 tax treaties worldwide. A signing ceremony will be held in June 2017 in Paris. This will be a key step for Ireland in introducing a number of BEPS Actions.

Ireland will also be required to introduce certain other BEPS equivalent measures which are contained as part of the EU ATAD.

We have set out below those measures which will be implemented through the EU ATAD or the MLI, and those for which Ireland must act unilaterally to implement.

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**Action 7 – Permanent Establishment Status**

Article 7 is not a BEPS minimum standard which requires implementation. Ireland’s DTA network currently extends to 72 countries. We also note that the new Action 7 principles may lead to numerous ‘technical’ PEs. Such technical PEs may have very low levels of profit attributable to them, and the administrative burden may be challenging for Revenue to manage as each PE would be subject to the many registration and filing requirements which apply to Irish tax resident companies. Therefore purely from a cost/benefit perspective the adoption of certain Article 7 provisions would not be in
Ireland’s interest. Therefore in our view there is no need to modify the existing PE definition and in any case some of the exceptions included within in the new PE definition should not be subject to the condition that the activities referred to be of a preparatory or auxiliary character.

Further and as highlighted below, we understand that the UK will not adopt elements of a definition of a permanent establishment that greatly expands its application but will aim to adopt the OECD’s proposed anti-fragmentation rules. By adopting more onerous rules than those of other nations Ireland will be unnecessarily be put at a competitive disadvantage. Therefore, it is essential that Ireland remain competitive in this regard.

**Action 13 – Transfer Pricing Documentation and Country by Country notifications**

Ireland introduced Country by County (CbC) reporting requirements as part of Finance Act 2015, and relevant companies are required to file an annual notification with Revenue. The annual notification requirement represents an additional administrative burden for Irish subsidiaries of multinational operations. The imposition of unnecessary notification requirements is not helpful in attracting FDI at a time when Ireland needs to be particularly mindful of its tax competitiveness internationally.

In addition companies required to file CbC notifications with Revenue have also expressed concerns regarding the confidentiality of their data once submitted and there are also concerns that the information shared through CbC reports may make companies the target of audits, which was not the intention of the OECD. As such countries with less onerous CbC reporting requirements may become more attractive jurisdictions than Ireland for future investment.

Ireland has also not introduced a requirement for an Action 13 Master File and a Local File to be prepared. We would welcome clarity as to whether this will be required.

To summarise, significant consideration should be given to imposing rules which are not required vis-à-vis our competitors. In our view Ireland should not seek to implement what may be perceived as a best in class regime if it puts us as at the back of the class in terms of attractiveness. In our view it is our “force of attraction” which should be our primary focus from now on.
3.0 Question 3

What legislative measures, if any, should Ireland take to maintain the competitiveness of the corporation tax code and deliver tax certainty for business in the context of the ongoing implementation of internationally agreed measures to combat BEPS?

3.1 Certainty

Certainty in the tax code has long been established as one of the pre-requisites of a working tax code. Adam Smith in what has been described as his landmark treatise of The Wealth of Nations, dealt with the issue of certainty in taxation matters back in 1776 as part of his four canons of taxation. He noted

"The tax which each individual is bound to pay ought to be certain and not arbitrary. ...The certainty of what each individual ought to pay is, in taxation, a matter of so great importance that a very considerable degree of inequality, it appears, I believe, from the experience of all nations, is not so great an evil as a very small degree of uncertainty."

It’s as true today as it was then. Indeed, a joint report recently published by the OECD / IMF addressed the issue of tax certainty wherein they noted that globally there are many reasons for heightened concerns about tax uncertainty, affecting both taxpayers and tax administrations. These include: the spread and emergence of new business models and increased internationalisation of business activities; heightened concern with aggressive tax planning; some fragmented and unilateral policy decisions; certain court decisions; and updates to the international tax rules, such as through the BEPS Project, which are necessary to ensure that the international tax rules remain up to date with the changing environment. Certainty is a key component of tax competitiveness, and the ability of Ireland to deliver tax certainty to investors make it a significantly more attractive jurisdiction for inward investment.

Ireland exists within a world which is growing increasingly uncertain from a political, social, economic and indeed taxation perspective. Uncertainty may mean scheduled investments are cancelled, put on hold or diverted to other jurisdictions. However, there are policy measures which remain within Ireland’s control and which can help promote certainty and stability and tax is one of them. Ireland’s ability to offer tax certainty represents a distinct competitive advantage which is valued by international investors, and feeds directly into the ‘Rate, Regime and Reputation’ doctrine which forms the three key components of Ireland’s Corporation Tax Strategy12. Certainty is therefore a key component of tax competitiveness. We have set out below a number of areas which could increase this certainty of application.

3.1.2 Legislative Certainty and Consultation

Recent changes to the Irish Real Estate Funds (IREF) and Securitisation (section 110 Taxes Consolidation Act 1997) regimes are examples of unwelcome volatility in an Irish investment context, particularly in areas where the regime may have been one of the factors driving the relevant investment decision in the first instance.

Investors make investments which may be short or long term in nature and they base such investments on various factors and one of those factors can include the tax treatment. However where investors cannot be reasonably assured that the tax

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treatment of that investment will endure throughout the duration of the investment then that brings about increased uncertainty which can negatively impact investment in Ireland. We recommend therefore that when introducing future tax legislation the opportunity be taken to clarify the expected timeframe for which the specific measure is expected to stand.

Similar to the system which exists in the UK, we also suggest a period of public consultation for significant pieces of proposed legislation. This would afford all affected stakeholders the opportunity to provide reasoned opinions on the impact of the proposed legislation. The active participation of stakeholders in the legislative process would ensure that relevant or otherwise unforeseen issues should be captured before a tax measure enters into law. This should in turn decrease the likelihood of significant amendments after the enactment of any legislation, which would provide certainty for businesses and Revenue.

If significant, and particularly unforeseen, changes are required to a particular law, greater phase-in times are suggested to allow taxpayers time to manage the period of uncertainty and transition which may result from such changes. This phase in period was notably lacking in the recent IREF and section 110 changes, for example. Another example of legislation which experienced a high volume of amendments is section 766 TCA 1997 (which looks at the R&D credit regime) which was the subject of c50 amendments since its introduction; it must be noted that certain of these amendments were improvements to the law which is to be welcomed, but others were not.

3.1.4 Increased Dáil & Technical Debate

Often highly technical pieces of legislation are introduced to the Dáil but ministers are not afforded sufficient time to consult with their constituents and other stakeholders as to the impact such legislative changes may have. Furthermore insufficient time may be allotted to Dáil debates of such legislation in the first instance. This in turn leads to debates which do not consider sufficiently the scope of the proposed changes. Providing for an increase in the time allotted to review the proposed legislation and also increasing the amount of time allotted to debate proposed tax legislation would ensure the views of constituents and stakeholders concerning the impact of proposed changes are effectively communicated. We anticipate this would lead to less subsequent amendments to legislation, which would provide more certainty and comfort to investors.

3.1.7 State Aid and Revenue Opinions

Ireland and a number of other Member States have recently been the subject of actions taken by the European Commission alleging unacceptable State Aid had been provided by the countries concerned. Among other conditions, it is necessary that the respective measure confers a selective advantage on taxpayers who are in a comparable legal and factual situation in order that it be considered a State Aid.

Ireland should take additional steps to ensure that tax measures, both existing and proposed, are reviewed to provide certainty that they do not breach the broad interpretation of what can constitute State Aid. This is particularly so given the recent caselaw before the European Courts regarding the interpretation of State Aid and its potential broadening of its scope in determining the existence of a selective advantage.

For example the Court of Justice of the European Union (CJEU) in the recent *Santander* decision arguably sought to apply a broader approach in identifying state aid in a case

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13 World Duty Free Group SA, formerly Autogrill España SA, established in Madrid (Spain) (C-20/15 P), Banco Santander SA, established in Santander (Spain) (C-21/15 P), Santusa Holding SL, established in Boadilla del Monte (Spain) (C-21/15 P) [Joined Cases C-20/15 P and C-21/15 P]
dealing with an element of a tax system. There the CJEU noted that “while it is not always necessary that a tax measure, in order for it to be established that it is selective, should derogate from an ordinary tax system, the fact that it can be so characterised is highly relevant in that regard where the effect of that measure is that two categories of operators are distinguished and are subject, a priori, to different treatment, namely those who fall within the scope of the derogating measure and those who continue to fall within the scope of the ordinary tax system, although those two categories are in a comparable situation in the light of the objective pursued by that system”. This is quite a broad approach and the case dealt with a provision which was available to all corporate taxpayers.

The fact that Ireland operates on a legislative based tax system, with Revenue providing clarifications and opinions regarding its interpretation of law, is critical in this instance given that all taxpayers can see the codified reliefs which may be available to them. However there are instances where a case specific opinion or confirmation of a particular tax treatment from Revenue will be necessary for taxpayers. The EU Commission itself recognises the importance of advance ‘rulings’ as a tool to provide legal certainty to taxpayers. Provided they do not grant a selective advantage to specific economic operators, tax ‘rulings’ do not raise issues under EU State aid law. In order to provide an additional channel for tax certainty we urge Revenue to continue to engage with taxpayers in providing fact pattern specific confirmations. We would also recommend measures be introduced to publicise Revenue opinions. This has been done in the past with the rulings given in connection with whether a company as carrying on a trade. This would provide taxpayers with increased certainty that their interpretation of the law is in line with that of Revenue where taxpayers have a similar fact pattern to prior opinions given.

3.2 Global Tax Agenda

Global tax changes mean Ireland is obliged to implement certain provisions of the OECD’s Base Erosion and Profit Shifting (BEPS) initiative, the EU Commission’s Anti-Tax Avoidance Directive (ATAD) and also the upcoming Multilateral Instrument (MLI). However, where these provisions contain optionality then such options should be carefully considered and debated to ensure that Ireland is not put in a competitive disadvantage vis-à-vis other nations.

We note Ireland has made strong advances to been seen globally as engaging in “best practice”. While engaging in “best practice” is essential to maintain our international reputation, Ireland is a small open economy which is heavily reliant on FDI. Ireland does not operate in isolation and must be conscious of the positions being adopted by competitor nations. It is necessary that a desire to engage in “best practice” does not lead to Ireland agreeing to non-mandatory or more onerous provisions which are contrary to its competitive offering and position in this new order. We would therefore encourage the careful consideration of the positions being adopted by other nations when choosing to sign up to non-mandatory provisions which may make Ireland a less favourable location for FDI. Some of these positions are outlined below.

MLI

The changes proposed as part of BEPS Action 7 (permanent establishment) are not regarded as a minimum standard and therefore countries have the choice as to which provisions to adopt as part of the MLI. It has been reported for example that the United

Kingdom will not adopt a definition of a permanent establishment that includes commissionaire agreements, but will aim to adopt the OECD’s proposed anti-fragmentation rules\(^\text{15}\). In our view Ireland should not agree to permanent establishment rules which would generate little tax for Revenue and may make Ireland a less attractive jurisdiction in which to do business.

Article 4 modifies the rules for determining the treaty residency of a person other than an individual that is a resident of more than one Contracting Jurisdiction (dual resident entity). Under this provision, treaty residency of a dual resident entity shall be determined by a Mutual Agreement Procedure (MAP) between Contracting Jurisdictions. Under the MAP in Article 4, Contracting Jurisdictions are not obligated to successfully reach an agreement and in absence of a successful mutual agreement, a dual resident entity is not entitled to any relief or exemption from tax provided by the Covered Tax Agreement except as may be agreed upon by the Contracting Jurisdictions. This could lead to a period of uncertainty for taxpayers due to the lack of phase-in time for the provisions of the Article and may lead to an increase in tax disputes between competent authorities. We therefore reiterate that the significant consideration be given to the impact of adopting non-mandatory provisions which would serve to unnecessarily disadvantage Ireland relative to other jurisdictions.

**ATAD and references in law to EU membership**

Ireland does not currently have Controlled Foreign Company (CFC) rules. These rules now exist within ATAD Article 7 which has to be legislated in Ireland by 2018 and contain various forms of optionality. The provision can attribute to a taxpayer company predefined categories of non-distributed (passive) income (“Option A”), or non-distributed income from non-genuine arrangements (“Option B”), of a greater than 50 per cent controlled, low-taxed, direct or indirect foreign subsidiary of the taxpayer/parent company.

When implementing ATAD Article 7 we would argue that “Option B” presents a more favourable approach to such legislation. The non-genuine arrangements option aligns more closely with the existing “bona fide” tests which is currently used throughout Irish tax law. “Option B” is also more closely aligned with the *Cadbury Schweppes* decision of the European Court of Justice, which dealt with CFC legislation and whether or not CFC anti-avoidance legislation would violate the principle of freedom of establishment where it targeted companies engaged in the “*genuine and actual pursuit of an economic activity in a host Member State*”\(^\text{16}\).

In terms of international competitiveness, a number of international clients will look to base their operations in countries which have favourable CFC rules. Choosing the appropriate measure to implement will make Ireland a more attractive place in which to invest.

Article 5 of the ATAD provides that Member States will be obliged to impose an exit tax (a tax on the difference between the market value of the assets and the value of the assets for tax purposes) on the occurrence of a number of circumstances, but broadly where a company ceases to be resident in a Member State.

Ireland already imposes a substantially similar tax known as the exit charge. Upon the cessation of Irish tax residence, the company is deemed to have disposed of and immediately reacquired all of its assets at market value. Any chargeable gains in respect

\(^{15}\) [https://www.bna.com/uk-wont-adopt-n73014448826/]

\(^{16}\) *Cadbury Schweppes plc and Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue* (C-196/04)
of such assets will therefore crystallise at the time of cessation of residence. However an exemption is currently afforded to ‘excluded companies’.

The ATAD would in effect do away with the ‘excluded companies’ provision. On implementation this could mean that all companies which ceased to be resident could face an exit tax charge at an effective 33% rate of Capital Gains Tax (CGT) as matters currently stand. Investors, when planning an in country investment will consider their exit strategy should they ever need, for whatever reason, to withdraw its investment in that country. Therefore such a charge may discourage future investment in Ireland due to the prospect of potentially significant CGT becoming payable. That said, the Article does not interfere with a Member States’ sovereign right to set its own tax rate. The setting of an appropriate ‘exit tax rate’ would provide certainty for international investors and make Ireland a more attractive destination for increasingly mobile FDI.

Of course, Brexit is a key concern. There are many provisions within the law which looks to countries being a member of the EU or at least the EEA. One example of this is the legislation dealing with groups for capital gains tax purposes whereby all companies within that group must be resident in the EU or an EEA state with which Ireland has a tax treaty. Where an asset is transferred within a group and that company leaves the group with that asset within 10 years then the deferred capital gain may crystallise for capital gains tax purposes. Post Brexit it is conceivable that such groups may suffer such a charge in the absence of relieving legislation where a group is no longer in point at that time. Given our key economic ties with the UK then relieving legislation would be necessary for this and indeed withholding tax on certain annual payments e.g. interest etc.

3.3 Increased Competitiveness

Countries are increasingly competing for mobile FDI and Ireland has been highly successful in that regard. FDI accounts for about a quarter of overall Irish economic activity by some measures, and the majority of gross value added in the business economy17. Corporate tax policy has been, and should continue to be, a key driver in Ireland’s success in this regard. However we believe the time is right to introduce changes to the corporate tax code to enhance its competitiveness for indigenous entities. We have set out a number of recommendations below.

3.3.1 Rate Change

Although not part of this consultation’s remit given that it focusses on regime, it is timely to look again at our corporate tax rate. US President Donald Trump has indicated his desire to reduce the U.S. corporate tax rate by more than half to 15 per cent. There has been speculation that ultimately this may end up around 18-20 per cent, but this still represents a significant reduction on the current rate. There is also the potential of the "border tax" for Irish exporters to contend with. Meanwhile UK Prime Minister Theresa May in her Brexit speech said she envisaged a Britain that “would have the freedom to set the competitive tax rates and embrace the policies that would attract the world’s best companies and biggest investors to Britain”. The two core aspects to Mrs. May’s statement concerned the virtues of an attractive tax rate, and an attractive tax regime. This is similar to the pillars of our own corporation tax strategy ‘rate, regime and reputation’.

Further, Mrs May noted in her speech that “...we will take back control of our laws and bring an end to the jurisdiction of the European Court of Justice in Britain....And those laws will be interpreted by judges not in Luxembourg but in courts across this country”.

Tax decisions from the European Courts say that national laws must comply with EU laws. However once outside the EU and following their enactment of the “Great Repeal Act”, the UK may not be restricted by EU State Aid considerations which prevent Member States from benefitting certain business or sectors through State action. Similarly for the four EU freedoms allowing free movement of goods, people, capital and services. The downside for the UK will be the well-rehearsed “passporting” difficulties that will restrict the ability of UK-based financial services businesses to operate in the EU. This may allow Ireland benefit from relocations given its position as an English speaking gateway to the EU. However the UK may become a significantly more competitive jurisdiction from a corporate taxation perspective.

In light of developments in the UK and U.S. a rate reduction would send a strong message that Ireland values FDI here and want to ensure that international (and all) companies based in Ireland can continue to benefit from locating operations here. Ireland’s power to adjust our corporation tax rate remains a sovereign right, and one which we should consider using if and when necessary.

3.4.2 Common Consolidated Corporate Tax Base

The government has already sent a strong message to the EU in connection with its proposed Common Consolidated Corporate Tax Base (CCCTB). Denmark, Malta, the Netherlands, Sweden and the UK have given similar responses. The CCCTB as currently proposed effectively takes profits from each member country and allocates these profits around Europe for tax purposes based on sales by destination, assets and employees by location. This would be detrimental to our economy and tax regime for both FDI and indigenous industry operating across borders. This proposed EU tax regime would rewrite tax law. Under CCCTB Ireland would no longer be able to attract FDI on the basis of having a different tax regime, as all EU Member States would have the same regime. In Ireland’s “reasoned opinion” submitted to the EU it was noted that the proposal offended the concept of “subsidiarity” within the EU treaty itself. The CCCTB is also fundamentally at odds with the BEPS project which the government has supported and is committed to implementing, and as Minister Noonan noted “no man can serve two masters”. We therefore recommend that the government continue its engagement with the CCCTB process but ultimately maintain its fundamental objection to same.

3.5.1 International Tax

The importance of MNCs to the Irish economy has been well documented. Approximately 80 per cent of corporation tax receipts received are from the multinational sector. One in five Irish employees are employed by foreign MNCs18. Ireland’s positioning in the global business marketplace for MNCs depends on having:

- A competitive corporate tax rate and appropriate regime for the management and use of Intellectual Property taking into account the status of major competitor locations in the EU (e.g. UK, The Netherlands) and outside the EU (Singapore, Switzerland, Malaysia).
- Tax relief for interest on debt financing which is easily administrated and is in line with international best practice.
- Tax measures providing for clear, efficient and comprehensive relief for double taxation suffered on dividends, interest, royalties and foreign branch profits.

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• Appropriate treasury vehicles to manage cash, foreign currency and derivatives in line with global capital market practices.

3.5.2 Reform of the tax deduction provisions for interest on borrowing.

The ease of access to capital in global capital markets and related tax deductibility of such interest and financing costs is of critical importance in facilitating MNCs doing business and using Ireland as a hub for operations. It is also important to financing operations that purchase and invest in corporates e.g. private equity operations and venture capital operations.

Countries are concerned about unrestricted tax deductible borrowings in eroding the in-country tax base. These concerns are reflected both in the BEPS Actions and in Article 4 of the ATAD by imposing, subject to certain exceptions e.g. group wide tests and a 30% EBITDA limit on the amount of deductible interest. However, in our view, Ireland as an open economy must facilitate inter-alia free movement of capital in a manner that encourages domestic corporates and MNCs to consolidate their operations into Ireland while contributing to the Irish exchequer returns.

To this end we suggest the Department of Finance maintain its position that countries like Ireland, which already have strong targeted rules, will be able to defer the interest restriction rules of ATAD Article 4 until 202419. The question arsing here is arguably not whether Ireland imposes a 30% EBITDA restriction on interest but rather whether our interest rules are “equally effective” as such a rule. To understand this requirement one must understand the purpose of the ATAD provision which arguably is to deter excessive interest deductions being attributed to particular companies in various jurisdictions. A full interest deduction is allowed to standalone entities and arguably a similar approach is allowed for highly leveraged groups. Recital 6 in the ATAD notes “In an effort to reduce their global tax liability, groups of companies have increasingly engaged in BEPS, through excessive interest payments. The interest limitation rule is necessary to discourage such practices by limiting the deductibility of taxpayers’ exceeding borrowing costs.” Therefore, the provision is one of deterrent.

For example, Ireland currently affords relief under TCA 1997 section 247 on interest incurred on borrowings used to acquire and interest or lend to other companies. It is widely acknowledged that the qualifying conditions within section 247 are complex and difficult to satisfy. The related section 249 TCA 1997 provisions, also referred to as the ‘recovery of capital rules’ are similarly complex. These intricate rules act as a deterrent in bringing about excessive interest into Irish groups. Therefore, there are arguments in this instance that such a provision may be an “equally effective” deterrent in ensuring genuine debt is brought into Ireland as that brought about by ATAD Article 4. Similar arguments exist for trading deductions given the substantial anti-avoidance provisions that exist in, inter alia, TCA1997 s817C, s840A etc.

3.5.3 IP Amortisation

Ireland is considered a favourable location for holding and exploiting IP. Relief is granted through section 291A TCA 1997 which provides for capital allowances on such assets being spread over 15 years or the accounting life of the intangible asset. The abolition of capping provisions which applied prior to Finance Act 2014 were welcomed by MNCs and makes Ireland a more competitive jurisdiction in which to hold IP. It is important however that Ireland continues to take measures to remain a favourable location in this regard.

**IP Allowances and Group Restructuring**

At present TCA 1997 Section 291A allowances are not available on IP which has been acquired from a group company, and that particular group company has claimed relief from capital gains tax on the transfer. This means that any potential allowances are foregone.

Given that companies are looking to restructure their global IP in light of the BEPS measures which will require the alignment of profits with substance, Ireland should remain mindful that is has a unique opportunity to enhance its attractiveness as an IP holding and exploitation location. All measures should be taken to ensure companies choose Ireland as a location for the IP post restructuring.

**Accounting Amortisation**

The majority of Irish companies who prepared accounts under ‘old Irish GAAP’ were obligated to convert to FRS 100/101/2012. These new accounting standards require companies to ‘fair value’ certain assets, including IP. In effect this means that such assets may no longer be amortised on an annual basis, and thus companies who claimed relief under TCA 1997 section 291A on the amortised basis may lose the relief if the law was to remain as is. In our view such companies should be permitted to continue claiming capital allowances in line with the expected life of the asset under the prior accounting standard but this would require a legislative amendment. Such an approach has precedent in that securitisation legislation was amended on the advent of IFRS to allow companies remain with their previous accounting practice for tax purposes as opposed to that reflected in their financial statements to ensure that fair value movements on certain financial assets and liabilities could be ignored until the respective asset or liability was realised.

We also recommend that a separate elective treatment in line with TCA 1997 section 765 be extended to TCA 1997 section 291A. TCA 1997 section 765 provides that capital expenditure on scientific research may qualify for a 100% allowance. However, there are clawback provisions under section 765 whereby in the event that an asset representing capital expenditure on scientific research ceases to be used for such research, then an amount equal to the lower of the amount of the allowance claimed on that asset or the value of that asset at the time that it ceases to be so used, is to be treated as a trading receipt, at the time of cessation of use for the research. Adopting such an elective treatment for IP within may simplify certain financial accounting deferred tax positions which can arise in a company’s financial statements as a result of the capital allowances granted under TCA 1997 section 291A. This is one of the main issues facing companies which are seeking to bring IP into Ireland. This is not a tax issue but rather an accounting issue such that those affected companies’ effective tax rates would be materially affected and that indicator is a decisive factor for shareholders. Reducing this accounting difficulty could serve to increase Ireland’s attractiveness for such activities.

**3.5.4 Research and Development Tax Credits**

From a Research and Development (R&D) tax credit perspective, the following points have been identified as challenges experienced by R&D tax credit claimant companies, which hamper the competitiveness of the scheme:

- An inconsistent approach by Revenue in querying and auditing R&D tax credit claims, somewhat due to each region being responsible for their own coordination and management of R&D tax credit audits. Some Revenue districts may have dedicated teams for dealing with aspect queries and some
may not. In addition to this, approaches and interpretations can differ from inspector to inspector within regions.

- No direct process/route for claimants where they disagree with decisions formulated by the district expert. Currently, an internal review is undertaken by Revenue who either uphold or reject the inspector’s decision (of which no report is made available). Given that appeals are resource intensive in terms of cost and time, a transparent escalation process in advance of appeal stage is required.
- Lack of sector specific guidance from Revenue, which would give clarity to claimants across a variety of industries, such as biopharma, IT, etc., covering both scientific/technical and expenditure aspects of these different sectors.
- Change in Revenue’s interpretation of eligible expenditure. Since the R&D tax credit legislation was first introduced, 10 Revenue R&D Guidelines have issued in the intervening 13 year period. A difficulty faced by some claimant companies is the approach taken by some inspectors to retrospectively apply varying interpretations of eligible spend. This is especially challenging where recent interpretations published by Revenue contradict previous agreement with Revenue on eligibility of costs.
- Inconsistency by experts in assessing the “Science Test” – which can be subjective depending on the expert engaged by Revenue.
- Difficulty and length of time in bringing audit cases to a close efficiently along with keeping the claimant company aware of the status of the query/points arising from Revenue audit.

The importance of Ireland’s overall R&D tax offering remaining competitive applies to both the scheme itself and the claim environment in which it operates. A fundamental cornerstone of Revenue’s Customer Service Charter is the requirement for consistent and equitable treatment of all taxpayers whereby “Revenue will administer the law fairly, reasonably and consistently and will seek to collect no more than the correct amount of tax or duty.” Companies that can more reliably avail of the R&D Tax credit are in our view more likely to invest in R&D.

In further assessing the competitiveness of Ireland’s corporation tax offering, the R&D tax credit regime is vital in incentivising economic growth and foreign direct investment to Ireland. When evaluating Ireland’s regime in an international context, both the UK and Canadian equivalents are worth noting.

HMRC have issued clear and transparent guidance on the R&D regime which provides a level of confidence to UK claimant companies in terms of costs that are eligible for inclusion. Recent enhancements to the UK scheme include the introduction of the Research and Development Expenditure Credit (RDEC) regime which is intended to make the relief more visible to decision makers, increase the impact of the relief in generating R&D activity in the UK and improve the attractiveness of the UK as a location for R&D investment. Furthermore, the UK government has in the case of the SME scheme regularly increased the tax benefit over recent years. Other countries have in turn reacted similarly to this schemes competitiveness.

Also relevant in comparative terms is the Canadian scheme. Canada supports for R&D is delivered through direct and indirect funding. 70% of funding is in the form of tax credits in accordance with the Scientific Research & Experimental Development tax incentive program (SR&ED). SR&ED funding is approximately $3 billion per year to over 20,000 taxpayers. Whilst funding is available to taxpayers that carry on business in Canada, enhanced rates are available for Canadian-controlled private corporations (CCPCs) that meet certain criteria.
3.5.5 Holding company regime and Double Tax Relief Reform

MNCs may decide to establish a holding company for a range of reasons. For example, a holding company may be an efficient way to manage a group of subsidiaries in a particular region by centralizing financing, licensing and management activities. Choosing the appropriate location for a holding company is a complex procedure—involving consideration of business, economic, logistical and operational requirements. The tax attributes of the location are also a relevant factor. For example, how income and gains of the holding company will be taxed and the effective tax rate, substance requirements, withholding tax exemptions and depth of the jurisdictions treaty network are all important considerations. Ireland is generally seen as an attractive holding company location\(^\text{20}\). However, in an increasingly competitive tax sphere Ireland should take steps to ensure it remains an attractive location in which to place a global holding company.

An Irish resident company is taxable on its worldwide income and gains. TCA 1997 Schedule 24 provides various mechanisms for computing double taxation relief due on non-Irish sources of income, for example dividends, royalties, income from foreign branches, etc. The mechanisms for relief differ depending on the type of income received and its source, i.e. treaty versus non-treaty countries. These mechanisms can be complex in practice which may make them less attractive than those offered by other jurisdictions such as the Netherlands. We have set out a number of examples below and the reader is also referred to Appendix A where we have outlined the complexity of certain of the reliefs afforded under TCA 1997 Schedule 24.

**EU Source Dividends**

In the respect of EU-source dividends, Ireland offers an effective exemption for such dividends via 12.5% tax rate and a foreign tax credit system. The foreign tax credit is usually sufficient to eliminate any Irish tax which would otherwise be payable. However, the requirement to perform the relevant double tax computations and track pooled credits, deductions etc. requires detailed and technical analysis. This relief system represents a compliance burden on companies but serves to generate no additional tax revenue for the Exchequer.

**Foreign Royalty Income**

Broadly, “pooling” means the ability for any unrelieved foreign tax to be pooled together and offset against other similar forms of income thereby reducing the overall corporation tax liability a company may have on multiple sources of a similar type of income. However, the pooling provisions differ between the sources of income. For example, TCA 1997 Schedule 24 para. 9F allows for the pooling of excess credits arising on relevant interest. However, there is no equivalent pooling relief in respect of excess credits on relevant royalties rather a pooling of deductions applies which is less valuable.

**Leasing Income Relief**

Under TCA 1997 Schedule 24 para. 9DC unilateral credit relief on certain leasing income may be given for withholding tax suffered in countries with which Ireland does not have a tax treaty. The relief allows for a reduction in Irish corporation tax on relevant leasing income in respect of the relevant foreign tax borne. Where foreign tax is incurred in respect of a separate stream of leasing income, and that tax cannot be fully relieved against the corporation tax attributable to that stream of leasing income in the current year, then the excess foreign tax may be carried forward for relief against income from

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\(^{20}\) https://www.taxjournal.com/articles/comparative-analysis-tax-jurisdictions
the same stream of leasing income in future years. However, in practice this relief is of limited use. We therefore recommend that the credit be made available also against tax arising on the future sale of the aircraft giving rise to such leasing income, i.e. that the credit be claimable on the balancing charge arising or gain on sale. Extension of the credit for this purpose would make Ireland a more competitive jurisdiction for aircraft lessors.

There is also currently no similar carry-forward provisions under TCA 1997 Schedule 24 paras. 9D and 9F in respect of withholding tax suffered on interest income which is treated as trading income of the Irish company.

Foreign Branch Exemption

A number of countries, such as the UK, operate a foreign branch exemption to eliminate double tax. As Ireland competes to attract companies seeking to set up European headquarters, together with those companies considering relocating from the UK post Brexit, a branch exemption would be an attractive proposition.

Recommendations

A ‘participation exemption’ currently exists in a number of EU jurisdictions, such as the Netherlands, where dividends and capital gains tax on the sale of shares in both domestic and foreign subsidiaries are exempt from corporate income tax if certain requirements are met. Ireland currently applies the participation exemption to the sale of certain shares in countries based in EU member states, and domestic source dividend income is also exempt from corporate income tax in Ireland. We suggest that TCA 1997 Schedule 24 is simplified to extend the participation exemption to EU source dividends. The absence of Controlled foreign Company (CFC) rules has previously been put forward by policy makers as a rationale for adopting a “tax and credit” provision for dividends as opposed to an exemption provision; with the forthcoming legislation to implement the CFC rule in the ATAD then this defence may no longer hold. As such, the inclusion of a participation exemption for foreign dividends would add to Ireland’s attraction for holding and other investment companies to be based here.

We also recommend a broad simplification of TCA 1997 Schedule 24 to provide the same level and mechanism of relief irrespective of the type of income. We do however recognise that distinctions may remain necessary in distinguishing between reliefs afforded to treaty and non-treaty sources of income.

3.5.6 Updates to the participation exemption

The current EU Participation Exemption is transposed in Irish legislation in TCA 1997 section 626B. This relief grants an exemption from corporation tax in the case of gains arising on the disposal of shares in an EU / DTA jurisdiction. At present this relief only extends to those shares which were, at the time of the disposal, related to businesses which are mainly involved in the carrying on of a trade or trades. With effect from 1 April 2017, the UK have removed the general requirement that the company sold must be a trading company/trading group member after the sale. It is however retained where the sale is to a related party and additionally where a trade has been transferred into the company within the last 12 months. This prevents a trade from being combined with non-qualifying assets in an effort to make the whole sale exempt.

Ireland should consider following the UK’s treatment in this regard, to ensure Ireland remains a competitive holding company location. Further, with simplicity comes certainty of application.
3.5.7 Reduced compliance burden

It is widely noted that Ireland ranks highly globally in terms of the overall ease of paying tax\(^2\). However, Ireland should be proactive in ensuring that measures are introduced to help companies efficiently handle the increased compliance burden that has arisen as a result of the implementation of the BEPS process and global tax reform generally.

For example, since 2012 certain companies have faced the obligation to deliver iXBRL tagged Financial Statements, Detailed Profit and Loss accounts, FATCA Returns, CRS Returns and Country-by-Country Notifications / Reports. These returns can be detailed, complex and may take significant time and expertise to complete. These new returns also represent a substantial cost for companies.

While we acknowledge a number of these returns are international requirements we urge that steps be taken to make such returns as quick and seamless as possible. This may include rolling up certain returns into the existing Form CT1. For example, 46G or Dividend Withholding Tax (DWT) forms where no payment is required by the company may be suitable for inclusion in the CT1.

In practice there also exists a lack of consistency over the time taken to process a tax registrations. In particular this varies by industry, tax head and Revenue district. For example VAT registrations currently take between six and eight weeks to process, but sometimes significantly in excess of this. In our experience certain districts request significantly higher amounts of supporting documentation than others. We recommend consistent guidance and maximum timelines to process tax registrations are implemented across all districts as this is a key compliance issue for businesses establishing in Ireland.

3.5.8 Loss Reform

The UK has recently introduced draft legislation to reform the UK’s treatment of corporation tax losses\(^2\). A key aspect of these changes are greater flexibility in the use of brought-forward losses against companies’ profits. It will be possible to offset brought-forward losses arising from 1 April 2017 against taxable profits of different activities of the company and the taxable profits of group members. Companies will also have total flexibility on how current year reliefs are set against trading and non-trading profits.

There will however be a restriction on the amount of profits that brought-forward losses can be set against. For profits from 1 April 2017 only 50% of profits will be able to be relieved by brought forward losses subject to a group-wide annual de minimis of £5 million. Subject to availability of losses, the annual £5 million allowance can be allocated between group members and income sources at the group’s choice.

For UK companies and groups the new measures will allow for significantly greater flexibility in use of brought-forward losses. This should help to avoid losses being “stranded” in companies where they cannot be used, and this will benefit groups forced to change their business models or revise activities to reflect wider changes in the economic environment.

These measures in principle increase the attractiveness of the UK as a base from which to operate. However, the measures have been criticised for being overly complex\(^2\).
Ireland should therefore strongly consider reforming its corporation tax loss rules to remain competitive with the new UK reforms, while going further and improving on the UK reforms by introducing rules which are less complex and easier for companies to implement in practice.

### 3.6 Domestic Sector

As noted above, the Irish government has been highly successful in attracting FDI. While FDI should remain a cornerstone of Irish economic policy, we believe it is appropriate that focus be brought to using corporate tax policy as a means to grow the domestic sector. Whilst SMEs represent only a small portion of the corporate tax take annually, over 900,000 people are employed by Irish SMEs.24 Striking a balance between foreign and domestic direct investment is key to ensuring future economic stability. We have outlined certain measures below which would serve to increase the competitiveness of the Irish tax corporation tax code for the domestic sector. The reader is also referred to this firm’s submission in relation to the Tax and Entrepreneurship Review undertaken by the Department of Finance.25 A select number of the recommendations from the submission are included in Appendix II.

#### 3.6.1 Notional Equity Deduction

As part of the Common Corporate Tax base (CCTB) the EU Commission proposes a notional interest deduction on equity. This Allowance for Growth and Investment will allow businesses to deduct a notional yield on equity increases after the CCTB rules enter into force. Equity reductions eliminating the amounts on which the allowance is given should in turn give rise to taxable amounts.

The notional yield will be calculated based upon the Euro area 10 year government benchmark bond yield in December of the year preceding the relevant tax year, increased by a risk premium of 2 percentage points (a floor of 2% will apply where the benchmark bond yields are negative).

While we remain strongly opposed to the CCTB we believe the notional equity deduction is a positive measure which would remove the disadvantage for companies that are not heavily geared currently face. This measure becomes particularly pertinent when the difficulties Irish companies face relative to their European peers when accessing credit are considered, and the fact that 37% of Irish SMEs have no debt. 26 27

#### 3.6.2 Better utilisation of start-up losses

Typically, taking the situation of a single start-up company rather than a group of companies including a start-up company, where the start-up company incurs losses during the start-up phase relief does not become available until that company becomes profitable. Had the business been operated as a sole trade, relief for the losses would have been available against the individual’s (and their spouses’, if applicable) total income at their marginal rates of income tax.

With a tax policy objective in mind of maximising the funds available for re-investment in the company, we would recommend that a mechanism be introduced whereby, by election, start-up companies could be treated as transparent for tax purposes for the first three years on the condition that: the cash benefit realised through the utilisation of

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24 https://www.isme.ie/advice/sme-facts-faq#employed
losses generated, relief for which is claimed by the shareholders against their gross income at their marginal rates, be re-invested in the company to fund future growth. The election would last for the first three years, with the option to cancel the election to be treated as transparent upon payment of a penalty.

This mechanism creates a channel whereby start-up companies can realise a cash benefit for their losses to ease the cash-flow burden during the start-up phase and, in our view, should be given consideration. The penalty mechanism is needed to avoid potential abuse.

3.6.4 Refundable start-up credit

Giving relief from corporation tax is of little benefit to start-up companies that are loss making, as the benefit of such relief would only get realised if and when those companies become profitable. However, if the cash value of the relief could be realised by the start-up companies concerned via some form of refundable start-up company credit, then this would greatly enhance the effectiveness of the relief and make it more relevant to dealing with the commercial difficulties (which to a large extent revolve around cash flow) faced by start-up companies.

There is a precedent for such a form of refundable tax credit in the R&D legislation and we would propose that the refundable start-up credit could be claimed in the company’s corporation tax return each year.

3.6.5 Refund of Employer’s PRSI paid

A further recommendation that could be considered would be to allow start-up companies to apply for a refund of 50 per cent of employers’ PRSI paid in the first three years, or to simply reduce the employers’ PRSI payable by start-up companies during this period by 50 per cent so that the cash benefit can be realised in real time.

3.6.6 Review of the Close Company Surcharge

We appreciate the purpose of the close company surcharge as being essentially anti-avoidance legislation designed to reduce the attractiveness of the retaining income within a corporate vehicle. However it also penalises successful businesses and restricts the use of funds which could be used to reinvest and grow family businesses. To this end, we suggest the government consider reducing or removing the close company surcharge in respect of surchargeable funds which have been reinvested into the business.

3.6.7 Entrepreneur Relief

Entrepreneur Relief is a welcome measure designed to promote entrepreneurship by offering a reduced rate of CGT on certain qualifying disposals. A qualifying group means a group where the business of each 51% subsidiary (other than a holding company) consists wholly or mainly of carrying on a qualifying business. As per the Revenue guidance, this means that relief would not apply where there is a dormant company in a group or where one of the subsidiaries is not a trading company.

From a practical perspective, often groups are left with dormant or otherwise inactive companies for commercial reasons, such as the use of a company to hold group IP, legacy planning, etc. An example of this issue often seen in practice is where companies are incorporated with the sole purpose of protecting a trade or business name. Registration of a business name is perceived to offer insufficient protection so otherwise dormant companies are maintained so as to provide the level of protection required to prevent unauthorised use of a trade or business name by third parties. Revenue
guidance means in this respect means that the relief is more difficult to avail of in practice. An update such that the relief would not apply where the companies had less than €100 gross assets, rather than where dormant companies exist within the group, would address concerns regarding potential abuse of the relief, whilst simultaneously recognising the commercial reality that groups may be required to maintain otherwise inactive companies.

We would also welcome clarity as to the extent of relief which will apply in instances where the group holding company rents property to its trading subsidiary where that trading subsidiary uses the property wholly or mainly for the purposes of its trade, and the group is otherwise a wholly or mainly trading group.

3.6.8 International Approaches

Many other EU jurisdictions offer favourable corporation tax measures that serve to boost the SME sector. We have outlined a sample of these below which may warrant consideration.

United Kingdom – Annual Investment Allowance

This relief operates to allow businesses to claim an annual investment allowance of 100% on the first GBP 200,000 tranche per annum of capital expenditure incurred on qualifying expenditure from 1 January 2016 (previously GBP 500,000). This is restricted to a single allowance for groups of companies or associated businesses. Where businesses spend more than the annual limit, any additional expenditure is dealt with in the normal capital allowances regime, entering either the main rate or special rate pool, where it will attract writing-down allowances at the 18% or 8% rate respectively.

Spain – Capitalisation Reserve Credit

This measure aims to strengthen Spanish entities’ net equity by keeping retained earnings undistributed. The capitalisation reserve will permit a tax deduction for 10% of the increase in net equity in a particular tax year, provided the company maintains the net equity increase during the following five years (except in the case of accounting losses) and books a distributable reserve for the same amount. The deduction may not exceed 10% of the taxable base before the deduction, adjustment for deferred tax assets and the use of net operating losses.

France – Competitiveness and Employment Tax Credit

The French Competitiveness and Employment Tax Credit (CICE) is a tax credit available to French businesses. The CICE is based on wages that an entity pays to its employees over the course of the calendar year. The wages paid by the company are taken into account for the calculation of the CICE within the limit of 2.5 times the French minimum wage. The CICE generates a receivable against the French Treasury, which can be offset against corporation tax payable or refunded after three years.

Luxembourg – Global Investment Tax Credit

Luxembourg provides for two types of investment tax credits. First, a tax credit is available that amounts to 12% of the increase in investments in tangible depreciable assets made during the tax year. The increase in investment over a given tax year is computed as the difference between the current value of all qualifying assets and the reference value allocated to the same type of assets.
Independently, the company may benefit from a 7% tax credit on the first EUR 150,000 of qualifying new investments and a 2% tax credit on the amount of new investments exceeding EUR 150,000 in tangible depreciable assets.

**Hungary - Development Tax Allowance**

Hungary offers a development tax allowance for companies investing in new facilities, expanding existing facilities or making a fundamental change in production or services. The incentive comes in the form of an exemption of 80% of the corporation tax payable for 10 years following the year the relevant project is completed. Several requirements must be met to qualify for the allowance, including an investment of at least HUF 3 billion (circa €9.6m) or HUF 1 billion in regional areas (circa €3.2m).

**3.7 Other Measures**

Although not part of this consultation’s remit, it must be noted that the corporation tax code cannot be successful at attracting FDI or growing indigenous industry in isolation. Whether it is foreign executives choosing Ireland as a base of operations, or an Irish entrepreneur setting a first enterprise, corporation tax is only one of a number of factors influencing their decision to invest. We therefore submit the below as key considerations as part of wider reform.

**3.7.1 Income Tax Reform**

The marginal rate of income tax for employees under PAYE is 52 per cent on all employment income in excess of €70,000. For the self-employed, the marginal rate on earnings over €100,000 is 55 per cent. High levels of tax on self-employed earnings are a barrier to entrepreneurship and do not reflect the risk being undertaken by entrepreneurs in setting up and developing a business. The current high levels of taxation on earned income act as a disincentive to stimulating both international and domestic business activity within Ireland, and make it harder to attract and retain highly skilled individuals needed to support current levels of foreign direct investment. We would like to see these high levels of income tax dealt with as a priority by the Government, with a view to reducing the maximum marginal income tax rate on all earned income below 50 per cent.

The continued disparity between employees and the self-employed is, in our view, damaging to the SME sector (and entrepreneurship generally) as it acts as a disincentive to setting up new businesses and does not reflect the risk taken by entrepreneurs in establishing new businesses, which create employment in Ireland. Further measures that would help to correct the imbalance could include:

- For the self-employed, the entry point for PRSI is significantly lower than for employees. This is more acutely felt in the context of startup businesses, where the business owner can earn a very modest amount in the initial years and thus such charges have a tangible impact on cashflow. At present, the entry point for self-employed individuals is €5,000, whereas employees do not pay PRSI until they earn over €18,000 per annum. This disparity should be amended to lessen the burden on startup businesses.

- The three per cent surcharge on self-employed earnings over €100,000 should be removed. As it stands, it is a barrier to ambition and creates an inequality in application (i.e. of marginal taxation on employment income versus self-employment income). This surcharge should be restricted to passive investment income only.
3.7.2 Share Options

Another area of Irish tax policy that can act as a barrier to enterprise is the current tax rules relating to share based remuneration.

Share options are widely used by companies to incentivise and motivate employees however the current Irish tax treatment applicable to such share options is not as closely aligned to incentivising employees as it could be given that employees are subject to Irish income tax rates on any share option gains triggered on exercise of the underlying options. The underlying objective behind the granting of share options to employees can be to incentivise employees to work to the goals of the company and to increase shareholder value as the holders of the share options will then be entitled to participate in this value increase through the exercise of their share options. However, the fact that any share option gain triggered will attract the marginal rates of income tax in the hands of the employees can act as a dis-incentive for the employees.

In reality, employees have accepted, as part of their remuneration, share options in the company and have therefore taken on a level of commercial risk in the sense that if the company does not generate increases in shareholder value over the vesting period of the options then the share options have little or no value for the employees. In this situation, the employees are likely to be de-motivated as they may have been better off accepting an additional salary payment subject to full PAYE, PRSI and USC deductions at source rather than the share options.

If, on the other hand, any share option gains realised by the employees attracted a final rate of tax on income equivalent to the Irish CGT rate of 33%, this would act as a further motivator for the employees to maximise shareholder value in line with the company’s goals and objectives. Additionally, the employees would perhaps be happier to accept the commercial risk associated with the share options in the knowledge that any share option gains would attract the lower final rate of tax on income of 33%.

We would therefore recommend that, in order for share options to fulfil their commercial purpose of acting as an incentive for employees to maximise shareholder value, a final rate of tax on income equivalent to the Irish CGT rate should apply to share option gains realised on exercise. Furthermore, we are of the view that, in order to avoid a potential for abuse, the value of share options awarded on grant should not exceed 10% of the relevant director/ employees’ gross salaries. This would also avoid the development of salary sacrifice arrangements with the aim of converting a higher income tax liability into a lower income tax liability under this proposal for a final rate of tax on income equivalent to the Irish CGT rate on exercise of the underlying share options. Furthermore we would recommend that this proposed tax treatment apply equally to Restricted Stock Units (RSUs) which are a common form of stock based compensation used in the modern era.

We acknowledge that there was an Approved Share Option Scheme legislated for under Section 519D and Schedule 12C of the Taxes Consolidation Act 1997 which was abolished from 24 November 2010. This gave income tax relief on the exercise of share options subject to a number of conditions. There was limited take up of approved share options due to the onerous conditions and, therefore, if the re-introduction of a similar initiative is contemplated as a result of this review in order to provide income tax relief on the exercise of certain share options for entrepreneurs, it will be imperative that the conditions are less restrictive.

It should be noted that the UK operate certain Enterprise Management Incentives (EMIs) which are tax advantaged share options. They are designed to help small, higher risk companies recruit and retain employees who have the skills to help them grow and
succeed. They are also a way of rewarding employees for taking a risk by investing their time and skills to help small companies achieve their potential. Tax advantaged share options with a market value of up to £250,000 may be granted to a qualifying employee of a qualifying company, subject to a total share value of £3 million under EMI options to all employees. The shares must be in an independent trading company that has gross assets of no more than £30 million. The grant of the option is tax-free and there will normally be no tax or National Insurance contributions for the employee to pay when the option is exercised. There will normally be no National Insurance contributions charge for the employer. A CGT charge arises on the ultimate disposal of the underlying shares. This regime has greatly enhanced employee ownership in UK start-ups and aided entrepreneurs in attracting top talent and we would therefore recommend that consideration is given to the introduction of a similar initiative in Ireland.

In addition, there is a level of bureaucracy around share schemes that all companies have to deal with but which dis-proportionately effect start-ups and entrepreneurs. Two examples include the requirement for a trust company for the “clog shares” arrangement under Section 128D of the Taxes Consolidation Act 1997 and also the wide impact of the convertible securities legislation under Section 128C of the Taxes Consolidation Act 1997. Our recommendation is that action is taken to remove this increased bureaucracy which has the effect of increasing costs for smaller companies operating share schemes.

A separate point worth noting under this heading is that relating to the tax treatment of ‘long options’ with a vesting period in excess of 7 years which under current Irish tax law could attract an income tax charge up front on the granting of the share options concerned if they are offered at a discount. This can be viewed as a particularly punitive provision from the perspective of start-up companies in, for example, the pharmaceutical or technology space which can typically go through an investment period in excess of 7 years until shareholder value is created given that the business is based on the success of the underlying research and development taking place. In this context, it is relevant to note that the Australian Government has recently announced the extending of the maximum time for tax deferral on share options from 7 to 15 years, which is aimed at giving companies more time to build their businesses and succeed. We would recommend that Ireland follows suit in this regard and introduces a similar change in law to recognise the investment period required for certain start-up companies.

3.7.3 Schooling

International schools are a subject of discussion for over 25 years, since the inception of the IFSC. We note the economic benefits of having schools recognised globally of being at an international standard, which is evidenced in the UK educational system, where large numbers of Chinese, Russian and middle-Eastern families educate their children at UK based fee paying schools that are able to direct the children to US universities or their equivalent. We believe that there is a requirement and a desire for government to facilitate the development of an international school in Dublin, that would be open to all children and which would as part of its remit support a major scholarship initiative for underprivileged children.

3.7.4 Housing

Ireland is currently experiencing a significant shortage of housing stock. This shortage represents a critical threat to Ireland’s competitiveness internationally, particularly at a time when Ireland is endeavouring to attract UK business post-Brexit. It is estimated that there is a requirement for approximately 25,000 units to be built annually. However, figures show that only an estimated 14,800 units were completed in 2015, a
shortfall of 41%. There are now 12% fewer homes to rent year-on-year, and Dublin rents increased by 11.7% in 2016 alone.

3.7.5 Access to Credit

There have been concerns for a number of years as to the availability of credit to the SME sector in Ireland. Irish SMEs are twice as likely to report issues accessing credit relative to their German equivalents. Irish SMEs have also reported increase in the cost of credit, whereas on balance their Eurozone peers report a decrease in their interest expenses.

An alternative to debt funding from financial institutions would be to introduce a special loan finance arrangement whereby individuals can lend money to SMEs in the EU (and based on the EU definition of an SME) and provided certain safeguards are in place (for example, market interest rates are applied), then the individual will be taxed on the coupon received at the standard rate of income tax (i.e. 20 per cent) as opposed to the marginal rate of income tax (i.e. up to 55 per cent).

This alternative funding option for SMEs is vital as while the Employment and Investment Incentive is a welcome source of finance for SMEs, the unfortunate reality is that, from an investor’s perspective, the shares acquired under this scheme rank behind trade creditors on liquidation. This results in a significant concern regarding the security of the investment. The loan finance arrangement should alleviate these concerns.

In addition, many potential investors have capital held in deposit accounts, et cetera, which give a particular rate of return. This loan finance initiative should act as an incentive to ‘relocate’ those funds into ‘active’ investments with the potential for a higher market rate return taking account of the additional risk being borne by the investors.

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28 https://www.scsi.ie/documents/get_lob?id=1136&field=file
4.0 Question 4

What is your view of sustainability of corporation tax receipts over the short to medium term?

Ireland’s corporate tax policy has been a cornerstone of its economic success for the past number of decades. It has allowed Ireland to compete internationally and has been a key factor in attracting the world’s largest companies to base major operations here. The percentage of tax take collected by Ireland in the form of corporate tax is similar to the EU average. However Ireland is heavily reliant on MNCs and FDI. In 2015 80% of our corporation tax was paid by foreign-owned companies, and just 0.2% of taxpayers contribute 64.2% of the government’s gross corporation tax receipts\textsuperscript{32}. Revenue has noted that the increase in corporation tax receipts between 2014 and 2015 can be explained by reference to broad based growth throughout most sectors of the economy, but the reliance on a small number of corporation tax payers remains clear.

The concentration of corporation tax revenue to just a small number of MNCs may pose a risk to the stability of exchequer revenue. For example where just one of those taxpayers has a poor fiscal year Ireland’s corporate tax revenue may be materially impacted. MNCs also generate vital VAT and PAYE revenue for the exchequer, while supporting hundreds of thousands of jobs both directly and indirectly. Therefore the corporate tax receipts generated by MNCs represent only one aspect of their importance to the Exchequer.

Separately, the impact of the BEPS project and ATAD is being debated at board level and a number of scheduled investment decisions have been placed on hold until ‘the dust has settled’ and clarity is available. Future investment decisions may be made based on tax competitiveness, and those countries which adopt less onerous BEPS and ATAD provisions will become more attractive jurisdictions in which to do business. It is unclear at this point the extent to which Ireland will benefit or be disadvantaged by such future investment decisions, but it is important that steps are taken to ensure Ireland does not lose its competitive edge through the unnecessary adoption of certain BEPS and ATAD provisions. We refer the reader to our comments in response to Question 2 and Question 3 in this regard.

What is clear however is that Ireland must move to diversify the split of corporate tax revenue. The looming prospect of President Trump’s corporation tax reform and the UK’s push to become a more tax competitive jurisdiction are just two of the direct threats to Ireland’s attractiveness as a jurisdiction to invest in. However Ireland is an example of a country which has successfully used corporate tax policy in developing its economy and should be continued to incentivise and grow the indigenous SME sector. A rise in corporation tax receipts from the SME sector would be an ancillary benefit, increased employment and national prosperity would be the true benefits of a strong indigenous SME sector. Such corporate tax incentives for the SME sector do not necessarily require sweeping overhaul of the corporate tax code. Changes both large and small can help the sector grow, and we refer the reader to our proposals in Question 3 in this regard.

### Appendix I – Reliefs Afforded under TCA 1997 Sch 24

The purpose of the below table is to demonstrate the complexity relief from double taxation available under TCA 1997 Schedule 24 Relief, and the inconsistency of treatment depending on the type of income, its source country, the percentage shareholding, etc.

<table>
<thead>
<tr>
<th>Income</th>
<th>Credit</th>
<th>Credit Pooling / Carry Forward Excess</th>
<th>Additional Foreign Tax Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dividends - EU / DTA (^1)</td>
<td>Yes</td>
<td>Yes, subject to conditions</td>
<td>Yes</td>
</tr>
<tr>
<td>Dividends – EU / DTA (^2)</td>
<td>Yes</td>
<td>Yes, subject to conditions</td>
<td>No</td>
</tr>
<tr>
<td>Dividends – Non EU / Non DTA (^3)</td>
<td>Yes</td>
<td>Yes, subject to conditions</td>
<td>No</td>
</tr>
<tr>
<td>Foreign Branch – EU / DTA &amp; Non DTA</td>
<td>Yes (^5)</td>
<td>Yes, subject to conditions</td>
<td>No</td>
</tr>
<tr>
<td>Interest (Trading) – EU / DTA (^4)</td>
<td>Yes (^6)</td>
<td>Pooling allowed but no carry forward possible</td>
<td>No</td>
</tr>
<tr>
<td>Interest (Trading) – Non EU / Non DTA</td>
<td>Yes (^6)</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Royalties – EU / DTA</td>
<td>Yes (^6)</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Capital Gains – EU / DTA</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
</tr>
</tbody>
</table>

1. Subject to a minimum % shareholding requirement in the applicable DTA
2. Where the minimum % shareholding in the applicable DTA is not met, but the shareholding is ≥5%. Where the dividend arises from a ‘portfolio investment’, i.e. less than ≥5%, the dividends will be exempt from tax where those dividends form part of the trading income of the company
3. Minimum 5% shareholding required
4. Minimum 25% connected party relationship required
5. Where branch profits are trading profits. Where branch is non-trading generally no relief is available
6. Credit relief is available but income must be apportioned
7. Pooling of deductions is available
Appendix II – Entrepreneurial Reliefs

As noted above, the reader is referred to our previous submission made in respect of a public consultation on Tax and Entrepreneurship. 33

A significant number of the recommendations set out in therein are equally applicable in the context of the current submission. A select number of these recommendations are set out below.

1. **20 per cent tax rate on certain dividends**

   A 20 per cent tax rate should be provided on dividends, subject to a €100,000 per annum limit once the business has been in existence for five years, which would:
   a) encourage entrepreneurs to grow their business for five years; and
   b) retain cash for re-investment in the company during this start-up period.

2. **Capital Gains Tax (CGT) Tapering Relief**

   With a view to designing a tax system that encourages individuals to stay in business for longer, CGT tapering relief should be introduced for individuals who have worked full time in the business for over five years, as follows:
   
   - 0 – 5 years – 33 per cent rate of CGT
   - 5 – 10 years – 16.5 per cent rate of CGT
   - 10 years and over – 8.25 per cent rate of CGT.

   This relief would encourage entrepreneurs to ‘stay the course’ and scale their business internationally thus creating a better prospect of replicating the Kerry, CRH and Glanbia success stories.

3. **100 per cent rollover relief**

   100 per cent rollover relief should be provided for entrepreneurs that exit the business earlier, but who re-invest 75 per cent of the proceeds in shares in another trading company, the disposal of which would be within the CGT charge.

4. **Removal of Employed v Self Employed Disparity**

   A self-employed person with before-tax profits of less than the industrial wage for the year of assessment (€35,768 for 2014) should be granted a self-employed credit of the same amount as the PAYE credit that the individual would have been entitled to had they been in a PAYE employment.

5. **Universal Social Charge**

   There is currently an additional 3 per cent USC charge levied on self-employed individuals earning in excess of €100,000 compared to an equivalent PAYE taxpayer. This additional levy does not reward entrepreneurial success, but rather in effect penalises our successful entrepreneurs.

Such tax disparity has been criticised in a 2013 ESRI report which questions the raison d’être on this additional tax burden on self-employed individuals. It has also been criticised by numerous groups and bodies concerned in this sector for its discriminatory effect.

We would recommend that this USC differential be eliminated so as to reduce the tax burden for Irish entrepreneurs so that they can continue to grow their business and be treated in a similar fashion to a PAYE taxpayer. As noted from a prior public consultation document, there are only 28,200 tax cases relating to this 3 per cent levy; so, given the small proportion of individuals affected by this additional levy, their success should be rewarded and not effectively penalised.
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