Building Ireland’s Future
Pre budget perspectives 2017
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Still, the glass is more than half-full for Ireland. While a degree of expected weakness has clearly manifested in the UK (though so far the worst predictions have not come true), eurozone growth has surprised to the upside and has been resilient in the face of Brexit. In addition, Irish growth in exports to non-European Economic Area countries (and particularly the United States) has remained at heightened levels.

Ireland’s success in attracting foreign direct investment – controversially cast into the spotlight by the whopping 26.3 per cent GDP growth experienced last year (which was largely illusory insofar as it was primarily due to technical factors and a few specific transactions) – as well as a stronger domestic economy – has fuelled strong, sustainable growth and fed an uptick in consumer spending and confidence that has only had a slight wobble so far following the Brexit vote. The underlying growth (excluding the one-off factors that pumped up the GDP numbers last year) of the real economy is anticipated to be in the region of four per cent or slightly more for 2016, which by comparison to other economies, is a strong performance.

This puts the Irish Government in a sound financial position, with slightly higher-than-expected ‘fiscal space’ (i.e. room to spend money and/or reduce taxes under the eurozone’s complex spending rules). However, with the uncertainty that prevails around the strength of the eurozone and wider global economy, and the longer term impacts of Brexit, caution is required in framing the 2017 Budget position, where spending and tax measures will need to be carefully and strategically considered to drive further growth, stability and economic recovery.

**Taxation**

Against a backdrop of political uncertainty in the first half of the year, we also witnessed important developments on the tax front. The OECD’s BEPS initiative steams ahead, while the Panama Papers revelations cast an unexpected spotlight on the financial dealings of thousands of clients of an obscure Panamanian law firm. The European Commission also unveiled a new Anti-Tax Avoidance Directive, and the drive for enhanced tax transparency has resulted in proposals at EU level for public country-by-country reporting. From a local perspective, tax has been an enduring topic of media scrutiny and public debate, with significant focus on Ireland’s securitisation and funds regimes, the impact of the EU state aid investigations, including the decision in relation to Ireland, which is being appealed. The renegotiation of the Ireland/U.S. tax treaty has also been announced, and whether the results of the U.S. Presidential election will have an impact or otherwise on any U.S. tax reform remains to be seen.

We would expect to see consultation in the short to medium term on a range of new tax measures that will need to be incorporated into...
the Irish regime over the next number of years. In our view, this should be combined with a more holistic and strategic review of Ireland’s corporate tax regime, to ensure that Ireland is positioned to retain and attract ongoing investment from international and domestic sources. The strategy of “playing fair but playing to win” will really need to come into its own, and Ireland should be open to taking bolder moves, particularly given the potential corporate tax strategy that the UK may pursue in a world post-Brexit.

For Budget 2017, the Government will need to strongly reinforce its commitment to Ireland’s low corporate tax regime, including the three key components of Rate (i.e. the 12.5% corporation tax), Regime and Reputation identified in its Corporation Tax Strategy.

Deloitte has been active in suggesting ways that the Government can make Ireland even more business friendly (e.g. we lodged a submission to the Government’s Public Consultation on Share-based Remuneration, which can be downloaded here: http://www2.deloitte.com/ie/en/pages/tax/articles/share-based-remuneration.html). However, this year our expectations are that only modest changes will be on offer. This is largely due to the fact that the Government is expected to devote some of its fiscal firepower to deal with the housing crisis and other social needs, with 2/3rds of the fiscal space expected on the expenditure side (with the remaining 1/3rd available for tax measures). In addition, Government is likely to take a cautionary approach, given political and economic uncertainties, and is likely to want to keep some of its powder dry in the off chance of a speedbump down the line.

So, what will Budget 2017 mean for Ireland’s economy and for firms and individuals here?

Indigenous economy
We expect some small fixes to help encourage Irish entrepreneurs, but nothing like what is necessary to ratchet up Ireland’s competitiveness to a new level.

Income tax
We expect to see modest improvements to the taxation of individuals’ incomes, though again this year most of the benefits will likely be weighted towards middle class and lower-income earners.

While this will have modest, positive benefits for consumer spending, we would strongly caution against any further narrowing of the personal tax base. The taxation of work in Ireland is marked by a narrow base and high effective tax rates by international standards, a critical issue which Ireland will need to address to ensure that it can retain and attract talent to work in Ireland. Indeed, a recent IMF report highlighted this problem and concluded that Ireland’s narrow tax base places, “a large tax burden on middle-income households, undermines female labor force participation, creates welfare traps for low-skilled workers, and discourages high-skilled worker migration to Ireland.”

Other economic priorities
Finally, if I can highlight one point to take away from all of these developments this year, including Brexit, it is that any opportunity Ireland has to attract inward investment/re-investment, and encourage Irish business and entrepreneurs to scale and grow their business in Ireland, depends not only on appropriate tax policies and other business incentives, but also on solving some glaring social issues, two of which are particularly relevant to the attraction of foreign direct investment to Ireland. The shortage of housing is the most immediate one and the one the Government has really taken on as a challenge with its Rebuilding Ireland report, though urgent action is now needed to boost supply. However, Ireland also needs to do even more than solving the housing crisis to foster a truly competitive climate for international talent to relocate here and bring with them the jobs that result from large-scale FDI; this includes everything from reducing the tax burden on workers, to making it easier to compensate talent via shares, as well as investing in more schools offering programmes of an international stature.

This year’s budget will be judged by the business community on how well it addresses these essential priorities. We at Deloitte look forward to Budget day, when the Government’s plans for Building Ireland’s Future, starting with the year ahead, are made clear.

Lorraine Griffin
Head of Tax
In response to changes in the global tax framework, companies across the world are reviewing their global operations to ensure that they comply with both EU and OECD standards. As a result, it is vital that Government policy supports initiatives that help Ireland remain an attractive destination for investment, and to do so in a way that is compatible with the priorities established under the OECD's Base Erosion and Profit Shifting (BEPS) project and the EU Anti-Tax Avoidance Directive (EU ATAD). Although we do not expect to see any significant changes in Budget 2017 in the area of Foreign Direct Investment (FDI), we would like to see an increased focus by the Government over the next number of years on certain key areas so that Ireland remains competitive in this ever-changing global tax landscape.

Environment post BEPS, EU ATAD and Brexit

There is no doubt that competition for FDI will intensify as a result of the OECD’s Base Erosion and Profit Shifting (“BEPS”) project. Indeed, Brexit may also put pressure on certain aspects of Ireland’s offering. In this context, Ireland needs to review its overall offering in terms of attracting FDI, while still complying with EU and OECD requirements.

Talent has become one of the key assets of most businesses. Following BEPS and the EU ATAD, where substance is of primary focus, the ability of a business to attract and retain talent is vital. However, Ireland has one of the highest effective marginal tax rates internationally, with personal tax rates of over 50 per cent (and with high rates kicking in at a relatively low level) that significantly reduces Ireland’s ability to attract highly skilled and senior-level individuals. Other jurisdictions where the total income tax and national insurance burden is lower have a competitive advantage in this regard. In the FDI sector, where tax equalisation is often applied (i.e. where an employer guarantees an employees’ net income), this high income tax ends up being a cost to the employer, which can reduce Ireland’s attractiveness as a location for FDI. In order to remain competitive, the Government should focus on reducing the marginal tax rate for all taxpayers below the 50 per cent rate and introduce additional incentives to attract talent to Ireland.

Over the coming months, the UK authorities are likely to try to provide reassurance and bolster public and business sentiment following the UK’s decision to exit the EU (“Brexit”). Indeed, it has already been indicated that in order to offset any slowdown in the UK market, the UK will actively pursue tax strategies to attract and retain FDI. In particular, a further potential

Louise Kelly
Partner, International Tax
Tel: +353 1 417 2431
Email: lokelly@deloitte.ie

Karen Frawley
Partner, International Tax
Tel: +353 1 417 2613
Email: kfrawley@deloitte.ie
As the international tax landscape continues to change, in our view, it is vital that the Government seeks to ensure Ireland’s competitive tax regime is retained and that Ireland continues to be a location of choice for FDI. The Government needs to be strong and innovative in refining its offering.

Our view

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Our prediction

• We do not expect to see any significant changes in Budget 2017 in the area of FDI, but would welcome some commitment by the Government to increase its focus on Ireland’s offering as a location for FDI.

• We would expect the Government to initiate a consultation process in relation to the implementation of the EU ATAD.
In June this year, the ECOFIN unanimously approved the Anti-Tax Avoidance Directive ("ATAD"). Minister Noonan referred to the directive as a “finely balanced compromise” and one which Ireland could support. The ATAD rules have to fit within each Member State’s separate corporate tax systems, with implementation remaining with Member States given that they “are better placed to shape the specific elements of those rules in a way that fits best their corporate tax systems”. The ATAD outlines actions in five areas, which are discussed below:

- Hybrid mismatches
- Interest restrictions
- Controlled Foreign Companies ("CFCs")
- A general anti-abuse rule ("GAAR")
- Exit taxation.

**Hybrid mismatches**
The ATAD includes an anti-hybrid mismatch rule to tackle mismatches in the legal characterisation of a financial instrument or entity between Member States, if such a mismatch results in a double deduction or a deduction without inclusion. In case of a double deduction, a deduction shall only be given in the Member State where a payment has its source. In case of a deduction without inclusion, the Member State of the payer should deny the deduction of such payment. The Council added a statement to the ATAD in which the European Commission is requested to come up with a proposal by October 2016 in relation to hybrid mismatches with third countries that is consistent with and no less effective than the rules recommended by the OECD's BEPS report on hybrid mismatches, with a view to reaching agreement by the end of 2016.

**Interest limitation rule**
Exceeding (or net) borrowing costs, such as interest expenses, will only be deductible up to 30% of a taxpayer’s earnings before interest, tax, depreciation and amortisation (EBITDA). Apart from that, a taxpayer may be given the right to fully deduct exceeding borrowing costs if it is, in short, not part of a group. In the alternative, a taxpayer may be given the right to deduct exceeding borrowing costs below a €3 million threshold, which should be considered for the entire group. The ATAD contains the option for Member States to choose between two different group exclusion provisions based on either an “equity/total assets” ratio or a group EBITDA test. The ATAD allows for:

(i) grandfathering loans concluded before 17 June 2016 (and not modified thereafter); and
(ii) an exclusion for third-party loans used to fund a qualifying long-term public infrastructure project. Additional flexibility is provided to Member States to carry forward non-deductible exceeding borrowing costs. Certain financial undertakings can be excluded from the interest limitation rule. Member States that have national targeted rules for preventing Base Erosion and Profit Shifting (BEPS), which are equally effective as those in the ATAD, can still apply those rules until the end of the first fiscal year following the date of publication of the agreement between the OECD Member States on a minimum standard with regard to BEPS Action 4, or, at the latest, until 1 January 2024. In that regard, an Irish Department of Finance press release recently noted, “The provisions on interest deductions are deferred until 2024 for countries, like Ireland, that already have strong targeted rules”. That view may have to be confirmed at EU level.

**Exit taxation**
Member States should introduce an exit tax for certain predefined situations, including transfers to other Member States and third countries. The ‘recipient’ Member States shall accept the value determined by the ‘exit’ states as the base of the assets for tax purposes unless this does not reflect market value. If a taxpayer fails in its obligation regarding the payment of annual instalments of the exit tax,
then it becomes recoverable immediately. Certain asset transfers, like the transfers related to the financing of securities and transfers that take place in order to meet prudential capital requirements, which are set to return to the Member State of the transferor within a period of 12 months, are not subject to exit tax. Ireland has a longstanding exit charge provision that can apply a capital gains tax charge on companies moving their tax residence out of Ireland, subject to exceptions. These exceptions have not been provided for as part of the ATAD such that significant change will be brought to our law as a result. However, there is a derogation in the ATAD allowing the application of the exit charge to commence on 1 January 2020, thereby allowing companies additional time to consider their position as a result.

**General anti-abuse rule**

The GAAR is envisaged to cover gaps that may exist in a Member State’s anti-abuse rules. Ireland has had a GAAR since 1989 and such provisions were completely overhauled by Finance Act 2014. The new provisions now have a broader in scope and application than that proposed under the draft directive.

**Controlled foreign company rules**

The CFC rules attribute to a taxpayer company predefined categories of non-distributed (passive) income, or non-distributed income from non-genuine arrangements, of a greater than 50 per cent controlled, low-taxed, direct or indirect foreign subsidiary of the taxpayer/parent company. The ATAD also includes permanent establishments in scope of the CFC rules and determines that a subsidiary/permanent establishment is a CFC if the actual corporate tax paid by that entity is lower than the difference between the tax that would have been paid on the same profits in the Member State of the parent company and the actually paid corporate tax in the source state. Given that Irish legislation currently does not have CFC rules, there will be an obligation on Ireland to introduce such CFC rules into Irish tax legislation by 2018 and to take effect from 1 January 2019.

The ATAD seeks to provide a minimum level of protection and Member States can take actions beyond its wording. It indicates that Member States shall adopt and publish the laws and regulations necessary to comply with its rules by December 31, 2018 at the latest. Consequently, entry into force of the ATAD is required from January 1, 2019. In relation to exit taxes, Member States are granted a one-year delay. In relation to the interest limitation rule, Member States that have national targeted rules for preventing BEPS and which are equally effective as article 4 in the ATAD can still apply those existing targeted rules until the end of the first fiscal year following the date of publication of the agreement between the OECD Member States on a minimum standard with regard to BEPS Action 4, or, at the latest, until 1 January 2024.

**Our view**

The ATAD could be seen as a first step toward harmonisation in the context of the fight against base erosion and profit shifting. For Ireland, measures such as the anti-hybrid rules or the GAAR provisions will have less of an impact based on Ireland’s current tax regime. However, the interest, exit tax and CFC changes will have an impact on the overall tax environment for businesses operating in Ireland, or seeking to invest in Ireland, once adopted and once they have become effective. The ATAD does not affect country tax rates, so Ireland’s 12.5 per cent corporate tax regime is not affected by these proposals. The general focus of the OECD BEPS and EU ATAD initiatives on aligning taxing rights with where substance and real economic activities occur is positive in the context of Ireland’s 12.5 per cent tax regime, which is substance based. However, the ATAD will bring about significant changes to our tax law and complexity levels therein. Against this rapidly changing international and EU tax landscape, which will have an impact on Ireland’s tax regime, it does mean that the Government should assess Ireland’s overall tax framework on a holistic basis, and in particular from a corporate tax perspective. While the Government aims to ensure that Ireland is compliant with BEPS and EU rules, it would also be important to ensure that we continue to “play fair but play to win” as part of our international tax strategy.

**Our prediction**

Our law will have to be amended to deal with the ATAD and the Department of Finance should hold some form of consultation in connection with legislating for these significant changes.
The economic climate for businesses in Ireland is at a crossroads, a level of post-recession recovery in certain sectors, but there is still a lot more to be done to help businesses succeed in a climate of growing uncertainty arising from Brexit. In order to achieve the right balance between foreign direct investment and domestic enterprise, it is important that the taxation system supports entrepreneurs and adequately rewards the risks undertaken by entrepreneurs to develop successful businesses, provide employment and support their communities. In this regard, we note the following areas as key for supporting entrepreneurs from a taxation perspective.

**Accessing investment in the SME sector**

Establishing and operating a business in the SME sector often involves difficulties in the area of financing. At present, there is a certain degree of tax relief available to those wishing to invest in SME businesses. These include the Employment Investment Incentive Scheme ("EIIS") and the Start-up Refund for Entrepreneurs ("SURE"). Given the unique difficulty in raising finance in the SME sector, and the risk-averse nature of most investors, we suggest extending the scope of these reliefs so as to support investment:

- That the annual cap on the level of investment for any one individual under EIIS should be increased from the current €150,000 so as to allow businesses access to adequate funding and allow investors relief on their full investment
- That tax relief for EIIS should all be granted upfront in year one, as opposed to the current staggering of the relief
- That a CGT exemption should apply to the disposal of EIIS shares to reflect the level of risk undertaken in investing in the SME sector
- SURE provides relief in the form of a refund of PAYE paid over a number of years for those investing in a new business. This scheme should be extended to those who were self-employed in the years immediately preceding the investment and not just those who were engaged in PAYE employment, as in many cases new startups are established by those who have run businesses previously
  - SURE should also be extended to businesses in the professional services sector
  - SURE might also be extended to allow outside investors to invest in the business in a similar manner to the Seed Enterprise Investment Scheme ("SEIS") in the UK. This scheme allows investors to invest up to £100,000 in any given year and allows a tax credit of 50 per cent of this investment against the individual’s income
  - That a loan-finance scheme be available so that interest on loans to private business attract a lower rate of income tax.

**CGT on exit for entrepreneurs**

An ongoing issue of concern is the early exit of entrepreneurs once a business reaches a certain level in value. To encourage entrepreneurs to remain in their businesses for longer periods, we suggest the introduction of a tapered CGT rate that would reflect the length of time the individual has held the shares.
longer the shares are held, the lower the rate of CGT on exit. In our view, this would encourage entrepreneurs who have managed to develop successful businesses to stay on board with the business so their unique skill sets can continue to be applied for the benefit of the business, thus allowing the business to develop and expand further. This might offer additional benefits in retaining the headquarters of successful businesses in Ireland, as opposed to seeing them sold to companies based overseas, as is often the case.

The amendments to the entrepreneur relief in Budget 2016 were welcome, as they provided a somewhat more immediate and tangible benefit to entrepreneurs. However, the level of gain to which the relief applies (i.e. €1 million) is still significantly lower than would be desirable. When compared to the equivalent level of relief in the UK, which currently allows gains of up to £10 million to be subject to a lower rate of tax of 10 per cent, the Irish relief clearly falls significantly behind. Therefore, we would suggest the Government continue to extend the scope of this relief in the coming Budget to bring it further in line with relief applied in the UK.

**Our view**

To encourage entrepreneurs to stay with their business for the longer term, the CGT position should be amended by granting such individuals lower rates of CGT which are dependent on the length they have held their shares in the business. In addition, the SME sector needs better access to finance, thus extending the scope of EIIS and SURE to make investment in SME sector more attractive should be prioritised to stimulate the sector.

**Our prediction**

There may be minor adjustments to the CGT entrepreneur relief, but not sufficiently significant ones to bring it in line with the equivalent UK offering.
There continue to be significant disparities in the area of personal taxation that represent a barrier to investment by family businesses and to the transfer of assets to the next generation.

**Income tax, USC, PRSI**

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 introduction in Budget 2016 of the earned income credit for the self-employed is welcomed. However, the current level of €550 must be increased in line with the PAYE credit, which is currently significantly higher at €1,650.

- 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.
The proposal in the Government’s Income Tax Reform Plan regarding the tapering out of tax credits for certain high earners is not a welcome development, as this is further disadvantages both workers and entrepreneurs. We hope this proposal will not be introduced.

**CAT/CGT**

The continued high rates of Capital Acquisitions Tax ("CAT"), also known as gift/inheritance tax, and Capital Gains Tax ("CGT") persist in being a barrier to the transfer of assets to the next generation, as well as disincentivising people to dispose of investment assets, such as land that may be used for development purposes. Therefore, we would wish to see an immediate reduction in the rates of CAT and CGT.

The current level of CAT tax-free thresholds remain at low levels compared to pre-April 2009 levels. The current situation means that even modest estates can result in significant inheritance tax liabilities, forcing the sale of the family home or other family assets. We would welcome the restoration of the CAT thresholds to the pre-April 2009 levels.

With regard to the transfer of family businesses to the next generation, the inclusion of the €3 million cap for CGT retirement relief should be reviewed. At present, a transfer of a family business to a child after the parent turns 66 years of age is capped at €3 million for relief purposes. There is no equivalent cap for CAT business relief. Given that the timing of such a transfer to the next generation will be significantly dependent on a wide range of commercial and family factors, the imposition of the cap after the age of 66 can mean that the parent does not transfer the business at all during their lifetime. The correct circumstances may not exist to transfer the business before the parent reaches 66 years, and any transfer thereafter would give rise to an excessively high liability to CGT (and as a transfer on death is not subject to CGT families have a financial incentive after the entrepreneur turns 66 to wait until their death whereas from a business perspective it might make more sense to effect the transfer earlier). We would like to see this age cap removed and the CGT relief brought in line with the existing CAT relief so that families can effect any transfer at a time that makes the most sense from a business perspective, without penalty.

There has also been a lot of commentary recently that the Government might reduce the relief available under the dwelling house exemption. If that was to occur a welcome trade off may be an increase in the CAT tax free thresholds.

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**Our view**

The continued disparity between employee and self-employed workers must be addressed. The burden on self-employed is much too high and is a barrier to entrepreneurship and the development of the SME sector.

As an incentive to employment, we would like to see the overall marginal tax rate for all earned income fall below the psychological barrier of 50 per cent.

**Our prediction**

We expect modest changes to the position of self-employed individuals (possibly an increase in the earned income credit). However, we anticipate the continued high marginal rate of tax for the self-employed earning over €100,000 to be continued into 2017. We also expect the CAT thresholds to be increased, although perhaps not to the pre-April 2009 levels.
Financial Services

Financial Services (FS), like other industries, is trying to digest, adapt and embrace the various changes to the tax environment as a result of European and OECD initiatives such as BEPS, the EU Anti-Tax Avoidance Directive (ATAD) and the EU Common Reporting Standard (CRS). Such changes come hot on the heels of the industry implementing FATCA reporting for the first time in 2015.

When one reflects that many of the tax changes envisaged by those new initiatives emanated in the last 12 months, the speed of change in the tax landscape is unprecedented. Compound that with the UK’s decision to leave the EU, the recently announced changes to securitisation (s110) and further changes signposted to Irish fund rules, and it is fair to say that FS is at a crucial state of its development from an economic, tax and political perspective.

To ensure Ireland remains a competitive environment for FS, there has been much written about changes that are needed to attract and retain senior FS executives and their business, such as enhancements to the Special Assignment Relief Programme (SARP), as well as a more practical tax framework to deal with deferred compensation arising under FS regulatory requirements. Such changes are needed, but of particular note are the recent draft amendments announced by Minister Noonan to the s110 legislation that took effect from 7 September, as well as the funds tax changes that are yet to be announced. Both sets of changes will be formalised in the Finance Bill.

In summary, the changes to s110 are targeted at investments deriving their value from Irish real estate-related assets. From 7 September 2016, only interest on profit participating notes in a s110 that is arm’s length, or is paid to certain investors, such as Irish corporates or EU investors that are fully taxable on the interest as part of genuine economic activities in their home country, is deductible.

One can understand why Ireland would seek to reclaim its taxing rights on Irish real estate in line with most global economies, but are the changes going to have unintended side effects?

A few facts that are relevant include:

01. Reputation and certainty – It is of vital importance for Ireland to have the highest standard of regulation, tax infrastructure and business environment in both funds and securitisation. That is the basis of our global reputation and is non-negotiable. Equally important is to give investors certainty.

02. The funds and the securitisation industries are different – A “fund” is commonly used to refer to any sort of financial structure; however, an Irish fund must be subject to the approval and prudential supervision of the Central Bank of Ireland, whereas a S110 is not. They are two very different structures, with different regulatory and tax frameworks.

03. The Irish funds industry directly employs 13,000 people and is recognised globally as the largest centre for the administration of alternative funds in the world, with 40 per cent of all alternative funds serviced here. There are over 6,000 Irish funds regulated and serviced in Ireland, with total assets under administration totalling €3.8 trillion. All parties that work with such Irish-regulated funds are themselves regulated – such as the investment manager, depositary and administrator. The funds industry has worked with the various stakeholders over the last 25 years such as the Central Bank of Ireland, Irish Revenue and the Department of Finance to ensure that the infrastructure is appropriate and best in class. This is reflected in Ireland’s being perceived internationally as a good place to do business and the regulated fund structure is key to attracting large institutional investors.
The tax infrastructure of a fund is that no Irish tax arises at the fund level, but instead the tax is suffered at the investment and investor level. The principle applied is that an investor should not be at a disadvantage by investing in a fund and so they are treated as if they invested directly in the underlying asset. For example, foreign tax may arise on foreign investments and then tax may also arise at the level of the foreign or Irish investor. Irish investors generally have tax at 41 per cent applied to their return from the fund (25 per cent tax for companies), with no tax applied to non-Irish investors (as they should be taxed in their home country). This is not an unusual framework and many countries with a funds regime have similar concepts.

**04. The securitisation industry** employs 1,000 people across the administrators, asset managers and trustees. Estimates of assets in Irish financial vehicle companies (FVC) are approximately €431 billion (as of 31 December 2015) with 23.6 per cent of European FVCs located in Ireland. While a number of service providers (such as asset managers and custodians) to s110s are regulated by the Central Bank, the s110s are not regulated (and are thereby different from funds). Similar to funds, the intention in the s110 is that tax is suffered at the level of the investment and investor jurisdictions so that there would be two levels of taxation rather than three. Irish investors are taxed on a self-assessment basis.

**05. It is simplistic to say that any structure that does not pay tax is “bad”.** If that were the case then all pension funds, sovereign funds (like NTMA and ISIF), charities and national entities (like NAMA) should also pay tax.

**06. Irish property investments** – Funds and s110s can invest in Irish and non-Irish assets. It is important to note that the majority of such structures do not have an Irish real estate investment focus. The focus of the draft s110 rules is to only target investments deriving their value from Irish real estate (a s110 cannot hold real property, so it may instead have purchased a mortgage book/loans from an Irish bank or NAMA, which is secured on Irish real estate). The difficulty with the current drafting is that it targets performing loans as well as non-performing loans.

While it might have wanted to target loans bought at a discount from NAMA, it also targets financing at full rates to property developers who cannot raise bank financing. In addition, the draft targets s110s that have any investment in an Irish property-related loan (for example, asset-backed securities or collateralised loan obligations), even if such loans only make up a small percentage of overall assets.

**07. Ireland needed funding** – Irish property assets had not traditionally been the investment focus of either funds or s110s. When the property market and the Irish banks imploded, there was a need for investment in both areas by non-Irish investors, as Irish investors (including the banks) no longer had the resources to do so. This resulted in a broadening of the investor base in Irish property beyond just Ireland. While it is true to say that some of that investment was by private equity houses, it is also a fact that global pension funds, life insurance companies and other collective investment structures made such investments.

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**Pre budget perspectives 2017 | Financial Services**

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**04. The securitisation industry** employs 1,000 people across the administrators, asset managers and trustees. Estimates of assets in Irish financial vehicle companies (FVC) are approximately €431 billion (as of 31 December 2015) with 23.6 per cent of European FVCs located in Ireland. While a number of service providers (such as asset managers and custodians) to s110s are regulated by the Central Bank, the s110s are not regulated (and are thereby different from funds). Similar to funds, the intention in the s110 is that tax is suffered at the level of the investment and investor jurisdictions so that there would be two levels of taxation rather than three. Irish investors are taxed on a self-assessment basis.

**05. It is simplistic to say that any structure that does not pay tax is “bad”.** If that were the case then all pension funds, sovereign funds (like NTMA and ISIF), charities and national entities (like NAMA) should also pay tax.

**06. Irish property investments** – Funds and s110s can invest in Irish and non-Irish assets. It is important to note that the majority of such structures do not have an Irish real estate investment focus. The focus of the draft s110 rules is to only target investments deriving their value from Irish real estate (a s110 cannot hold real property, so it may instead have purchased a mortgage book/loans from an Irish bank or NAMA, which is secured on Irish real estate). The difficulty with the current drafting is that it targets performing loans as well as non-performing loans.

While it might have wanted to target loans bought at a discount from NAMA, it also targets financing at full rates to property developers who cannot raise bank financing. In addition, the draft targets s110s that have any investment in an Irish property-related loan (for example, asset-backed securities or collateralised loan obligations), even if such loans only make up a small percentage of overall assets.

**07. Ireland needed funding** – Irish property assets had not traditionally been the investment focus of either funds or s110s. When the property market and the Irish banks imploded, there was a need for investment in both areas by non-Irish investors, as Irish investors (including the banks) no longer had the resources to do so. This resulted in a broadening of the investor base in Irish property beyond just Ireland. While it is true to say that some of that investment was by private equity houses, it is also a fact that global pension funds, life insurance companies and other collective investment structures made such investments.
Our view

• The reputation of Ireland and its financial industry is paramount and cannot be compromised.

• Changing the rules for investors mid-cycle creates uncertainty. At a time of global crisis, we welcomed international investors into Ireland (when the banks needed repairing, NAMA needed purchasers and our financial status meant that no-one wanted to lend or invest in Ireland), but is it fair that we now change the rules under which they invested? While such investment was made with a view to a profit, with any investment there is a risk attached and the investments made could equally have been loss-making.

• The current s110 drafting excludes investors such as Irish-regulated funds and EU life and pension funds, but permits non-EU funds that are not regulated. One hopes that the legislation is amended to address this, but in the meantime blue chip Irish and EU investors are in limbo, with a lack of clarity on the operation of the rules resulting in uncertainty.

• The pricing of property transactions on sales from NAMA reflected the understanding that there would not be tax in the structures. A knock-on effect would mean an impact on the pricing and returns from Irish property, therefore potentially having a negative impact on the Irish property market.

• It is imperative that wholesale damage is not done to an industry that employs 13,000 people; not because it is not popular to make tax changes, but because there is a fundamental need for the fund industry in a global context. Given the pensions time bomb, the funds industry has a pivotal role to play in savings and investments, for pension schemes, institutions and individuals alike. Any measures taken in respect of funds need to be well thought out and easy to operate and understand, without compromising on the overall tax efficiency of such funds in a global context.

• Non-bank financing is needed and securitisation is acknowledged by the EU as part of the Capital Markets Union initiative as a suitable non-bank source of funding.

Our prediction

While it is likely that there will be further amendments to the draft s110 rules, the thrust of it will remain the same to target Irish real estate related assets. Hopefully, the amendments will address some of the matters highlighted above.

There will be changes in the Finance Bill for funds, and ideally they should be easy to understand and apply, and not damaging to the overall industry. A pragmatic solution might be to apply a withholding tax only on payments from subfunds deriving their greater value from Irish real estate, with exemptions where investors are taxed in the EU on such returns. This is not just a domestic media and political matter. We have an international market that will lose confidence in Ireland if we create uncertainty and are seen as a country that changes its tax rules mid-cycle. There must also be a suitable timeframe from which such changes would take effect, so as to allow funds to put systems and controls in place to deal with the proposals.

Ireland is under the spotlight but when the spotlight fades, we want an FS industry that continues to shine.
Real Estate

**Residential property**
It’s anticipated and likely that we will see some tax changes this year, particularly around the tax treatment of the residential property sector. The Ministers for Housing and Public Expenditure & Reform launched an action plan in July to address the chronic shortage of housing. A growing population with solid economic activity also requires adequate infrastructure to support the growth of the country in the years ahead.

There have been calls for a reduction in the rate of VAT on new homes to nine per cent from its current 13.5 per cent, even for a short time, to support new entrants into the market. Such a reduction could be given either by reducing the price of a new sale or in the form of a rebate to a purchaser of a new home akin to the Home Renovation Scheme introduced a few years ago. However, it should be uncapped and an upfront refund rather than spread over a two-year period, so that it is effective and helps the buyer to finance their home purchase. There were some calls for a zero per cent rate for a short period, which has some support, but would require EU Commission approval.

In addition to the above, it may be that the first time buyer grant of the past may be reintroduced for a period to assist with saving the deposit or indeed the Minister may focus on Mortgage Interest Relief, which has previously helped people starting off in the market. Ultimately, if people own a home, they have equity in the longer term and are less dependent on the State for future support to help them pay rent.

There is also a view that private landlords of residential properties have been struggling to stay in the market, with many exiting as prices came back from the lows of the crash. New property taxes and reduced interest relief have made it difficult to make any profit and fund loan repayments, even where rents are viewed as high.

**Commercial property**
The commercial property market has really re-established itself strongly with the support of international investors who have invested both directly and through our three REITs. It is important that this market becomes stronger in areas outside of Dublin and appropriate infrastructural and FDI supports need to be front of mind so that we encourage new investment and further job growth in the country as we aim for full employment.

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**New property taxes and reduced interest relief have made it difficult to make any profit and fund loan repayments, even where rents are viewed as high.**

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**Padraic Whelan**  
Partner, Tax  
Tel: +353 1 417 2848  
Email: pwhelan@deloitte.ie
Our view

We believe that there will be changes, but it is difficult to predict how much or how far the Minister will go. It would be surprising if, at a minimum, the VAT rate is not effectively reduced on new homes to support first time buyers. There is a case for Mortgage Interest Relief to be reinstated at a reasonable level and it can be reviewed in due course, perhaps when the supply of housing is normalised so that we can more appropriately house our population, including those in need of social housing, first-time buyers and those returning to Ireland as our economy grows.

It’s also important for market stability and to ensure a well-functioning market that the private residential landlord isn’t discriminated against, so it’s likely we will see some change in this space.

Our prediction

We will likely see a VAT rate reduction on residential housing, coupled with some other supports both for the first-time buyer and the landlord community. We feel there are potentially going to be some changes for funds investors, but they will need to be well thought out and grandfathered in terms of effect so that no instability is created in the short term.

There has been some discussion around property funds and whether tax changes will happen following the changes to the s110 tax regime a few weeks ago. What is important to realise is that the funds have helped the recovery of the real estate market and will have priced in to their returns the effect of the tax regime they enter, which in turn dictates the amount they pay for real estate. In addition, we have competition from other European countries in attracting investment, and particularly from the UK, so any changes would need to be thought through carefully. In a post-Brexit world, it’s fair to say there is volatility to manage and we need to be mindful of the potential implications of Brexit on the sector and again of any unintended consequences of changes to our existing arrangements.
Global Mobility & Employment Taxes

There have been a number of consultations issued by the Department of Finance in 2016 and we would expect to see changes to legislation in response to the detailed submissions received on these topics. In addition, Brexit has presented a number of opportunities for Ireland Inc. to capitalise on the uncertainty in the UK and we are hopeful that the Government will make positive changes that encourage individuals to relocate to Ireland.

Share-based remuneration
Share-based remuneration has long proven to be an effective tool for rewarding employees. The provision of share-based remuneration incentivises employees, as the performance of the company has an impact on their return and the value of any shares they hold. It empowers employees by linking their reward to their employer's financial performance, leading to increased employee motivation. Positive employee performance can drive growth for the company, which has a positive impact on the economy overall and translates into increased employment and more revenue for the exchequer through increased tax-take.

The consultation focused on the benefit of existing reliefs, while also seeking to highlight barriers to effective share-based remuneration and solutions to overcome those barriers. Given the overall potential benefits, share-based remuneration can bring to the growth and development of companies, we consider it critical that the tax treatment of such remuneration is viewed as favourable from both an employer’s and an employee’s perspective.

The current Pay Related Social Insurance (PRSI) exemption on share-based payments is critical to the success of these share plans. However, from an employee’s perspective, the regime in Ireland is not as attractive as in some of our competitor jurisdictions due to Ireland’s high personal and capital gains tax rates.

Taxation of intermediaries
Intermediary and self-employment arrangements are very much a key feature of certain industries; for example, in various IT and innovation sectors. The nature of these industries is that personnel are required for maybe a short period of time or for a particular project only. The use of intermediary type structures and self-employment arrangements in these cases provides flexibility for both the end-users and the service providers. The end-users can have the resources and personnel they require at the times they need them and the service providers have the flexibility to work on various projects at the same time and to alternate between projects and clients, as appropriate. The market demand for such personnel means that such flexible working arrangements often suit both the service provider and the end-user.

Brexit
One of the main topics surrounding the Brexit vote has been the potential opportunity for Ireland to capitalise on any corporate decision to relocate functions and the associated employees. When it comes to income tax rates, one needs to break down the employee population into senior and middle management. Ireland does not compare as favourably for middle income earners due to the low entry point into our higher rate of tax. For high earners, the Special Assignment Relief Programme (“SARP”), which exempts a portion of income above €75,000 from income tax, along with the Remittance Basis of taxation provides a limited basis for a reduced effective tax rate. However, we still compare unfavorably to our competitors with regard to tax.
Our view

Share-based remuneration
We believe that share-based remuneration has a significant role to play in attracting and retaining key talent in companies based in Ireland, be they start-ups, established SMEs or MNCs. We would suggest that the Government consider implementing lower rates of personal tax and capital gains tax on share-based remuneration and the subsequent disposal of such shares. Some of the current share schemes in operation in Ireland are not working effectively and should be reconsidered in order to offer attractive, competitive alternatives to cash that can incentivise people to locate in Ireland.

Taxation of intermediaries
A flexible workforce is essential to attract MNCs and their projects to Ireland. Ireland is a popular hub in Europe for a large number of MNCs and tax should not interfere with such commercial reality.

Any moves to change the taxation of intermediaries and self-employed individuals could have a significant impact on the end-users of such services. The end-users could range from domestic Irish end-users to MNCs. The use of intermediary structures is prevalent internationally in, for example, the IT sector. Given that Ireland is a hub for many MNCs in the technology sector, careful consideration needs to be given to the wide range of stakeholders who could be affected by any changes to the taxation system.

Brexit
Brexit presents many possibilities for Ireland and decisive leadership is required to seize this opportunity through lower marginal tax rates, reduced bureaucracy with regard to mobile employees and enhancements to regimes designed to attract companies to relocate senior executives to Ireland.

From an individual’s point of view, particularly one who is considering moving from London, issues around housing and education are key drawbacks. While additional tax and higher housing costs can be picked up by the company for key mobile executives through tax equalisation, the relative lack of choices in international schools with associated facilities is something that requires immediate Government action.

Our prediction

We predict that there will be positive changes with respect to share-based remuneration, to potentially introduce enhancements to the Entrepreneur Relief or an introduction of a new type of share scheme akin to the Enterprise Management Incentives scheme in the UK.

On the flip side, we expect that there will be changes to current intermediary arrangements such that those using corporate entities to provide quasi-employment services will be adversely affected and potentially brought within the PAYE net.

Unfortunately, we do not foresee the radical positive changes to such schemes as SARP necessary to allow Ireland to take the best advantage of the opportunities posed by Brexit.
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