



The Consultative Committee of Accountancy Bodies-Ireland

Chartered Accountants Ireland
The Association of Chartered Certified Accountants
The Chartered Institute of Management Accountants
The Institute of Certified Public Accountants in Ireland

CCAB-I Pre Budget Submission 2010

**Supporting Indigenous Industry and Foreign Direct
Investment to Create Jobs**

SUMMARY OF KEY PROPOSALS

Senior executives should be encouraged to re-locate to Ireland, to lead investment and job creation. We advocate refinements to the existing remittance basis.

Section 3

While recognising that all taxpayers must shoulder an additional burden of taxation compared with previous years, a maximum effective tax rate should be introduced.

Section 4

We need to further develop Ireland's R&D regime, not merely through extending the relief offset rules, but also by a programme of information and administrative coordination. ***Section 5***

BES and Seed Capital Relief should be more accessible and more widely available to help our indigenous industry over the credit crisis. ***Section 6***

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1 ABOUT CCAB-I

The Consultative Committee of Accountancy Bodies – Ireland is the representative committee for the main accountancy bodies in Ireland. It comprises Chartered Accountants Ireland, the Association of Chartered Certified Accountants, the Institute of Certified Public Accountants in Ireland, and the Chartered Institute of Management Accountants.

This year's pre-Budget submission from the CCAB-I has as its main focus the use of the Tax System to create jobs. This can be achieved by introducing business aligned tax policy which follows through in its delivery from the legislation to its application for every taxpayer trying to make a living in Ireland today.

Most of the content of this submission is new, reflecting CCAB-I's reaction to the changing economic climate. In certain instances we have developed further a number of the proposals made in our submission for Budget 2009.

2 INTRODUCTION

Irish economic recovery over the history of the State has always been driven by commercially aligned tax policy. The tax policy which took Ireland out of the bleak economic chasms of the past was consistently radical and daring in its pro business approach. Bold pro business policies must be introduced now rather than further down the line of crippling national debt.

In this time of economic downturn it is understandable to revert to tactical day to day tax raising measures to deal with the exchequer crisis of the month. However, commercial strategic tax planning is a vital route to sustainable economic recovery. It is not a luxury we consumed in the good times but must regret now.

The CCAB-I recommends that broad thinking tax policy should be applied to the sole purpose of job creation by:

- taking a fresh look at ways to incentivise decision makers to locate to Ireland. Tax policy needs to change tack and concentrate on attracting and retaining the decision makers, who will then in turn create jobs from the corporate executive down to school leaver.
- resisting the temptation to place the entire tax burden on the high earner. We need to provide some context to

the high earner on where their tax liability will stop, and retain them as they deploy their skills in Ireland.

- encouraging entrepreneurship as the basis of a solid indigenous industry. After all, those setting up a business in these uncertain times deserve nothing less than a supportive tax framework to build economic success and tax revenues for the future.

3 USE TAX RESIDENCY RULES TO ENCOURAGE JOB CREATION

<p>The internationally based decision maker must be rewarded for doing business in Ireland.</p>

3.1 Key Executives – Incentives to Locate in Ireland

3.1.1 Context

Foreign Direct Investment with longevity involves the re-location of the key executives and decision makers to Ireland. When the top executive is working on the ground in Ireland then he/she is more likely to make long term commitments to building business resources in Ireland such as job creation, infrastructural investment and marketing Ireland as a key place of business. The premise is therefore simple but true; encourage the top executive to re-locate to Ireland, and real investment and job creation will follow.

Unfortunately, tax policy in Ireland over the last number of years has disbanded the very mechanisms which worked very well in encouraging the decision makers to locate in Ireland. Other EU Member States have recognised the importance of these people to the national economy and have introduced tax policy to make their jurisdiction attractive to key executives. The Irish approach is

perceived as the polar opposite, with complicated and cumbersome tax rules for foreign workers coupled with ineffective attempts to provide limited exemptions to a minority.

3.1.2 The French Impatriate Model

The French Government has recently introduced tax rules to encourage the location of key foreign executives and decision makers to France. This “impatriate regime” is aimed at managers and employers sent to work in France by a non-French employer to perform a professional activity for a limited period of time. The impatriate must take up French tax residence and not have been a French tax resident during the five-year period preceding the start of his duty in France.

The tax incentive takes the form of a partial exemption from income tax for the portion of the impatriate’s salary compensating him/her for the transfer to France or an exemption on 30% of the global remuneration of the impatriate.

The “impatriate regime” is selective in that it applies to individuals who:

- provide an exceptional economic contribution to France, or
- perform specific activities, or

- contribute more than €770,000 to SMEs located in the EU.

Every country's need to attract in decision makers and key executives for the benefit of the economy is illustrated by the existence of this form of "impatriate regime" in France.

3.1.3 Remittance Basis – UK

Ireland abolished its remittance basis in 2006 albeit with a partial reintroduction in 2008. At the time of writing, it could not be expected that any official figures to indicate the level of takeup of the 2008 regime would be available. Evidence from CCAB-I members does however suggest that any initial takeup has been low, due to the highly restrictive nature of the scheme.

A major reform of the UK remittance basis of taxation was introduced with effect from 6 April 2008 which represents a significant change to the way income and gains remitted to the UK are treated. We set out the essential elements of the UK scheme here, as we believe that a parallel arrangement is needed in Ireland.

Non UK domiciled taxpayers who avail of the UK remittance basis of taxation are subject to UK tax on their offshore capital gains and offshore investment income only to the extent such gains and income are remitted to the

UK¹. In addition earnings from a foreign employer, where the duties of such employment are performed wholly outside the UK, are only subject to UK tax to the extent they are remitted to the UK. Unlike the Irish partial remittance arrangements, the country of domicile of the taxpayer is not relevant to the relief.

Taxpayers who do not avail of the remittance basis are subject to UK tax on their worldwide income and gains.

Non UK domiciled taxpayers, who are “long term UK residents”, must make an annual claim and pay a STG£30,000 levy to access the remittance basis of taxation. A taxpayer is regarded as a “long term UK resident” if they have been resident in the UK at any time in at least 7 years out of the previous 9 years. Generally such taxpayers must also give up their entitlement to tax free allowances.

The £30,000 annual levy does not apply where the taxpayer is not regarded as a long term UK resident. However the entitlement to tax free allowances is lost.

If the taxpayer’s total unremitted offshore income and gains in any tax year is less than Stg£2,000, the remittance basis is automatically available. The taxpayer is not required to make a claim or pay the £30,000 levy and retains his or her tax free allowances.

¹ Similar rules can apply where the individual is non ordinarily resident. However there are some distinctions made between the taxation of income and of capital gains.

The net effect of the £30,000 UK annual levy is to ensure that a proportion of unremitted income falls into the charge to tax. This approach is not unreasonable, and indeed was adopted under the Irish partial remittance system introduced last year. The difference, of course, is that under the Irish system, a higher proportion of unremitted income falls into the charge to tax. Not only that, the taxpayer who can claim under the Irish system must earn a significant salary before any tax benefit of the remittance basis can apply.

We suggest that the Irish remittance basis, as currently constituted, cannot succeed as long as:

- The restrictions on the domicile of the claimant (i.e. outside of the EEA yet within a DTA territory) persist and
- The income threshold before which the relief cannot apply remains so high (i.e. €100,000) but with only partial relief thereafter

3.1.4 Proposal for Irish “Impatriate” regime

An Irish incentive system needs to be as straightforward, transparent and competitive as possible. CCAB-I advocates no restrictions on the domicile of the claimant, balanced with a threshold minimum amount of tax to be paid.

Furthermore income thresholds should be replaced by a minimum tax. It seems to us that an appropriate minimum for this purpose might be €30,000.

3.2 Residency for Irish Tax Purposes

The focus of Irish tax policy over recent years, has been to introduce measures to keep Irish citizens within the Irish tax net who might otherwise use the tax residency rules to avoid or minimize their liability to Irish tax. This approach is apparently supported by recommendations made by the Commission on Taxation Report². Indeed, the Proposed Renewed Programme for Government³ has alluded to reform of the residency rules to “ensure that those who benefit from living in Ireland are subject to taxation in Ireland”.

However, Ireland already has a particularly robust regime for tax residency rules. The concept of “ordinarily resident”, as it applies to the charge to income tax and capital gains tax, has been refined over many years. By now it has all but eliminated many of the perceived abuses associated with a residence test which relies solely on physical presence in the State.

Many of the arguments advanced which challenge the appropriateness of our residency rules overlook Ireland’s position as a responsible country within the international

² Commission on Taxation Report 2009, Recommendation 5.30, 5.31, 5.32

³ At page 4

community. We are bound by multilateral conventions and obligations – our memberships of the European Union, of the OECD and more generally our status as a developed first world economy rightly constrain our capacity to act unilaterally on matters of taxation. Simply put, we cannot impose a charge to tax which prejudices the legitimate claim to tax of another country.

We also enjoy the benefits of over 50 bilateral tax agreements, between Double Taxation Agreements and Tax Information Exchange Agreements. We have agreed to taxing rights with our major trading partners which cannot be broken by unilateral changes to domestic law. At a time when our international reputation counts for so much, unfounded claims to taxing rights will not be well received abroad.

A new claim to taxing rights, perhaps based for example on citizenship, would not be workable in the current climate of enhanced tax cooperation. Considerable progress has been made within the last 18 months within the OECD in facilitating the free exchange of information under Tax Information Exchange Agreements. Commitments have also been secured in regard to moving away from the kind of practices which are characteristic of territories regarded as tax havens.

The Commission on Taxation limited its proposals to adopting within domestic law certain of the criteria

applying to taxing rights which typically feature in our Double Taxation Agreements. These concern a taxpayer's centre of vital interests, and the availability of a place to live. Any attempt to extend our taxing rights unilaterally beyond adoption of these concepts in national law would be harmful to our international reputation.

3.3 Share Schemes

Share option schemes and other types of share based remuneration depend on a strong equity market for their success. Additional forms of taxation levied on such mechanisms (whose origin lies with tax effective remuneration) would be very disruptive.

In particular, the application of Pay Related Social Insurance to share schemes at a time of poor market conditions could well cost more in tax foregone than the measure would raise.

4 EQUITY IN THE TAX BURDEN – A MAXIMUM EFFECTIVE RATE

The top rate tax payer cannot shoulder the full burden of the exchequer deficit. A maximum effective tax rate should be introduced to put a gross liability cap on tax payable.

The introduction of new taxes such as the income levy, Non Principle Private Residency tax, along with increases in PRSI and Health levies have succeeded in retaining the progressivity of the system - the higher earner contributes the most.

The Commission on Taxation recommends keeping taxes on labour income low in order to reduce the cost of employment for the purposes of sustaining and stimulating demand for labour. It suggests that the loss in revenues to the exchequer from the economic downturn should be made good by further broadening of the tax base. However, further broadening invariably means introducing new categories of progressive taxes, a disproportionate amount of which will in turn be paid by the higher earners. So the cycle of placing the bulk of the ever increasing tax burden on high earners appears to have no limits.

The following table, derived from Dept of Finance budget documentation, illustrates the issue plainly.

Effective Tax Rates – 2007 to 2009

Single person, one income

GROSS	2007	2008	2009	2009 (supplementary Budget)	Last Comparable Year⁴
30,000	13.40%	12.90%	13.90%	16.90%	2005
40,000	19.70%	18.60%	19.10%	22.10%	2006
60,000	28.10%	27.50%	28.20%	31.70%	2004
100,000	34.20%	33.80%	34.60%	39.20%	2000
120,000	35.70%	35.40%	36.50%	41.10%	2000

There is a very real danger that the high income earner will leave Ireland in favour of more tax friendly jurisdictions. Such individuals are characterised by internationally sought after skills which can easily be relocated. If a tax exile phenomenon were to emerge, then Ireland's progress over the last twenty years would suffer a serious setback.

We therefore recommend the introduction of a maximum effective tax rate for high income earners. Such a measure would take account of all direct taxation such as income tax, capital taxes, the income levy, PRSI, the health levy, any new property or services taxes etc, and

⁴ The last year of assessment where the effective rates applied are comparable with current rates

apply a maximum effective rate to obtain a fair gross tax burden.

A maximum effective tax rate has been successfully applied in France and Sweden and such a system could also be introduced here to strike the right balance between exchequer requirements and the fair distribution of the tax burden on high earners.

5 RESEARCH & DEVELOPMENT

Key Recommendation - Bring national spending on R&D and innovation infrastructure up to international standards by allowing tax credit refunds for R&D tax credit.

Measures introduced by Finance (No 2) Act 2008 certainly went a long way towards encouraging the development of Ireland as a national and international centre for R&D.

However, Ireland of 2009 is a radically different economy to that of 2008. Therefore the R&D credit and refund mechanisms must be looked at again to come up with new ways of sustaining and enhancing the knowledge economy we have worked so hard to build up over the last decade.

5.1 Offset of R&D against Payroll Taxes

The recent Commission on Taxation Report⁵ recommended that companies should have the option of offsetting their R&D credits against employer PRSI. This measure would place Ireland high on the list of location of choice for international groups as investment decisions are made on “above the line” pre-tax comparison between competing locations. Ireland’s current R&D “below the line” refund mechanism is not part of the decision making analysis and

⁵ Commission on Taxation Report 2009, Recommendation 7.20

therefore puts us at a serious disadvantage in these competitive times.

To fully develop this argument, we suggest that an R&D offset mechanism should be available against PAYE and the income levy in addition to PRSI. As successful R&D is driven by the availability of highly skilled talent in the workforce, it makes sense to focus the R&D credit towards employee taxes. The ability to surrender the R&D Tax Credit against the payroll taxes in the year the credit is available would ensure a benefit where, in a startup phase, the capacity to use it against taxable profits might not be there.

This approach would also serve as a direct incentive towards labour intensive as well as capital intensive research and development.

5.2 Change from an Incremental base to a Volume Base

We have looked at ways of improving Ireland's competitiveness as a location of choice for international groups to place R&D spending. However, we also need to look at ways of encouraging R&D expenditure within a company with internally competing expenditure needs.

Currently the R&D credit is a function of increases in expenditure using 2003 as the base year of comparison. While the incremental approach was a fair means of encouraging year on year increased R&D expenditure, it is

not appropriate in a recession. Industry consensus supports the expenditure approach as outlined in the recent report produced by KPMG on Research & Development in Ireland⁶.

We therefore suggest that the volume based approach be introduced, if only for a limited period to address the current economic downturn to ensure that a company's competing resources are tax efficiently dedicated to R&D expenditure. If the volume based approach is adopted along with a Payroll offset mechanism, then Irish Tax Policy makers will give both national and international businesses the impetus to create sustainable high end quality jobs in Ireland.

5.3 Improve the Uptake of R&D Relief

Many Irish businesses are not aware of R&D relief or are unaware of how to go about successfully claiming the relief. KPMG's survey on R&D activities in Ireland shows that only 17% of companies surveyed claimed R&D relief. Further, apparently 9 in 10 companies surveyed felt that the R&D credit was not applicable or relevant to them.

Therefore, it is fair to deduce that information currently available on the R&D relief in Ireland is complicated and inaccessible to many businesses that need it the most in these difficult times.

⁶ KPMG "Take a Closer Look", a Survey of Business Attitudes to Research & Development in Ireland in 2009/2010

The Northern Ireland Tax Office of HMRC has identified a similar problem of poor information on R&D tax reliefs in Northern Ireland and has produced concise guidance material for small, medium and large sized businesses⁷. This information dissemination initiative is supported by public access to the R&D Specialist Units in HMRC.

We suggest that Revenue and Enterprise Ireland should actively target Irish businesses to first make it known that R&D relief exists. It should then provide user friendly information guides supported by expert advice within Revenue on how the relief works to improve the take up of R&D relief in Ireland.

⁷ Available on-line at <http://www.hmrc.gov.uk/nircto/invest-in-ni.pdf>

6 INDIGENOUS INDUSTRY

BES and Seed Capital Relief should be more accessible and more widely available to help our indigenous industry over the credit raising crisis.

As recognized by the Commission on Taxation Report, the Small and Medium Enterprise (SME) sector is “important to the Irish economy in terms of output, competitiveness and employment”. The importance of this sector cannot be stated often enough and establishing the bedrock of economic recovery depends very much on assisting Ireland’s entrepreneurs and risk takers with pro business tax policy.

As access to working capital has reached crisis point over the last year, BES relief and Seed Capital relief must now be reviewed and made more readily available to businesses. We suggest that the following measures should be introduced as a matter of urgency.

6.1 Remove Onerous Administration Burden on Accessing Relief

The Commission on Taxation recommends that the administration burden placed on companies seeking benefit from the schemes is onerous and must be reviewed⁸.

⁸ Commission on Taxation Report 2009, Recommendation 8.53

Our members work with the SME sector in respect of financial, taxation and accounting issues. The problems with navigating the maze of administration to access BES relief and Seed Capital Relief and indeed in securing tax refunds is a constant problem. We propose that the approach adopted by The Northern Ireland Tax Office of HMRC for business in Northern Ireland should be adopted by the Irish Revenue to remedy this problem. In particular, Revenue should work with Enterprise Ireland to:

- give early certainty on the tax consequences of commercial transactions that affect the proposed BES or Seed Capital relief investment
- facilitate direct access to Revenue's tax specialists in the area of BES/Seed Capital relief
- provide a local point of contact for advice and help with claiming BES/Seed Capital relief
- fast track the service where time is important

6.2 Extend the range of businesses eligible for BES/Seed Capital Relief

CCAB-I supports the extension of BES/Seed Capital relief to a broader type of business. In addition to specified industries, BES has traditionally been available to

companies which would have been regarded as manufacturing under the "old" 10% rate rules provided that those companies had received employment grant aid.

Employment grant aid has become a less prevalent element of the industrial environment in recent years. At this stage the employment grant criterion may be excluding worthy businesses, which would qualify in all other respects, from the relief. We urge removing the grant aid criterion in favour of a certification process which does not necessarily entitle the company to the receipt of grants.

We point to recent statements by the EU Commission in response to the use of taxation measures to improve the supply of capital. In September of this year the German Government received approval under the EU State Aid rules for modifications to its MoRaKG legislation, which is similar in substance (though not in detail) to Irish BES. Competition Commissioner Kroes said that "I am pleased that Germany intends to give tax breaks to stimulate private investors to offer more risk capital."

6.3 Target high end software/computer sectors, internationally traded services & IP Intensive business

The Department of Finance in conjunction with the Department of Enterprise, Trade and Employment and the Revenue Commissioners conducted a review of the BES

scheme⁹ in 2006. As part of the review, almost 1,400 companies who had availed of the scheme were surveyed. 58% of the respondents to the survey categorized their qualifying trade as that of manufacturing.

While manufacturing is a good job generating sector, it is somewhat at odds with the general national policy for job creation and sector growth in high end computer services, software development, IP intensive business and international services. These services only make up 42% of the qualifying trades profiled under the Department of Finance's 2006 survey. The requirement that internationally traded services and computer services must also qualify for grant approval for BES relief vetting process is inconsistent with the emphasis placed on the need for growth in these sectors by national policy.

We recommend that these sectors should have access to BES relief with minimal impediments to qualification.

6.4 Exit Mechanism for Seed Capital and BES reliefs

Seed capital relief and BES relief are both predicated on the requirement for the investor to purchase shares in the company and hold those shares for a five year period. While this requirement is commercially appropriate for BES

⁹ Department of Finance Publications "2006 Review of Business Expansion Scheme & Seed Capital Relief

investments (BES is by in large aimed at third party investors), it is not a tax efficient or a commercially appropriate means for the owner manager to invest in his or her company. The exit mechanism for the investment does not support his or her long term involvement with the business.

In general, owner managers of SMEs make a personal investment in their business by way of a loan to the company. If a share investment is made then they must either liquidate or sell the shares in order to realize a return on their investment. The BES rules and Seed Capital rules for owner/managers of SMEs therefore require such individuals to dispose of the business they have worked hard to build up in order to get a return on their investment. We strongly recommend that the rules for BES/Seed Capital investments by the owner/manager should allow for investment by way of loan to facilitate the long term development of the business and involvement of the entrepreneur.

6.5 Reform of the Patent Income Regime

We recommend that the current regime should be maintained as at present. However, a further refinement could be instituted whereby dividends can be paid to shareholders who are directly involved in the innovation process. Such dividends would be subject to a 12.5%

withholding tax rate, with that tax constituting the final liability.

This approach will be attractive in the commercial environment where the remuneration for an innovator and their team can be directly linked to the commercial return being made from their underlying work. However it would not be sufficient to implement this measure on its own, as this would be to the detriment of innovation within the public, and in particular, the university sector.