South Block
Longboat Quay
Grand Canal Harbour
Dublin 2

+353 1 663 1700
www.taxinstitute.ie

Minister Paschal Donohoe TD
Department of Finance
Government Buildings
Upper Merrion Street
Dublin 2

21 June 2019

Finance Bill 2019 Submission

Dear Minister

We set out in this submission a number of legislative changes for consideration in the drafting of Finance Bill 2019.

The submission focuses on various technical amendments to the legislation, which we believe are required to mitigate certain 'unintended consequences' arising from recent legislative changes. Our recommendations are broadly grouped into five key areas. These are;

1. Measures to support the growth of the indigenous sector
2. Measures to alleviate the potential impact of a 'no deal' Brexit
3. Measures to provide tax certainty for business
4. Measures to help address issues in the housing sector
5. Tax technical matters arising from recent decisions of the High Court

The submission does not include recommended legislative changes required to address certain limitations in the Key Employee Engagement Programme (KEEP), Revised Entrepreneur Relief, the Employment and Investment Incentive (EII) scheme and the R&D tax credit. We have set our recommendations to improve the effectiveness of these reliefs in our responses to the Department of Finance public consultations undertaken in May and June.

These reliefs are instrumental in supporting the growth of Irish SMEs and we urge that the necessary legislative steps are taken to encourage a greater take up of the R&D tax credit by SMEs and to enhance KEEP, Revised Entrepreneur Relief and EII in Finance Bill 2019.

Furthermore, the submission does not address the legislative changes required to implement further provisions of the European Anti-Tax Avoidance Directives (ATAD 1 and ATAD2)[1] regarding hybrid mismatch and interest limitation rules, nor does it address the proposed changes to Ireland's transfer pricing rules.[2] We have submitted our recommendations on both of

[1] Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market and Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries.
[2] Part 35A 1997

these key tax policy areas in our responses to the two Department of Finance public consultations held earlier this year.

Given the significance of these anticipated changes to the corporate tax code, we highlighted in our submissions in January and April 2019, the importance of consulting widely, not only on the policy choices but also on draft legislation and Revenue guidance well in advance of the measures commencing.

As a broad range of taxpayers will be affected by these changes, it is essential that all stakeholders are given the opportunity to consult on draft transfer pricing legislation, anti-hybrid and interest limitation rules in advance of the publication of the Finance Bill in October.

We would welcome the opportunity to discuss the matters raised in this submission with you or your officials.

Yours truly

Marie Bradley

Marie Bradley
President

Institute Recommendations

Our recommendations for Finance Bill 2019 are grouped into five key areas below. We have provided further detailed analysis of each technical matter in the Appendix to this submission.

1. **Measures to support the growth of the indigenous sector**

1.1. Enhancements to the KEEP, Revised Entrepreneur Relief and the EII scheme
The Programme for a Partnership Government recognises the importance of supporting the capacity and performance of Ireland's enterprise sector. The effectiveness of tax measures, such as the KEEP, Revised Entrepreneur Relief and the EII scheme are central to the growth of the indigenous sector. We have separately made detailed recommendations on how to address certain limitations within each of these reliefs in Finance Bill 2019 when submitting responses to the public consultations undertaken by the Department of Finance in May 2019.

1.2 The potential impact of section 135 TCA 1997 on the sale of a family business/SME
Considerable concerns continue to exist regarding the potential effect of section 135 (3A) Taxes Consolidation Act (TCA) 1997 on scaling up and passing on of businesses in the SME sector, in the absence of a statutory *bona fide* test.

Even though Revenue guidance may confirm that *bona-fide* financing arrangements are outside the scope of the provisions, as noted in your letter of 5 June 2019 to the Institute, this is not expressed in legislation. Therefore, it cannot be relied upon by taxpayers in the event of the matter being disputed and subject to an appeal.

In our view, inserting a legislative exclusion for *bona fide* commercial transactions into section 135 TCA 1997 is required, to provide the necessary level of certainty to taxpayers and their advisers when considering their exit options, notwithstanding the existence of Revenue guidance.

2. **Measures to alleviate the potential impact of a 'no deal' Brexit**

The Miscellaneous Provisions (Withdrawal of the United Kingdom from the European Union) Act 2019 (the Withdrawal Act) was enacted on 17 March 2019 in preparation for the possibility that the UK fails to agree a deal for their departure from the European Union. This would result in the UK no longer being an EU Member State and therefore becoming a 'third country', and outside the Single Market and Customs Union.

We understand from discussions at the Tax Administration Liaison Committee (TALC) that it was intended that the Withdrawal Act would cover only those measures which would have an immediate impact in the event of a 'no-deal' Brexit and that other Brexit-related tax issues would be addressed in Finance Bill 2019.

We have identified several circumstances that are not covered by the Withdrawal Act, which we believe should be included in Finance Bill 2019 in order to ensure that the status quo for taxpayers will be maintained in the event of a 'no-deal' Brexit. These circumstances are set out in detail in paragraph 2 of the Appendix.

3. Measures to provide tax certainty for business

Political, economic and trade changes beyond our control are causing significant uncertainty in the Irish business environment. We have outlined below six key areas where we believe amendments are required to existing legislation in order to provide the necessary certainty for business in applying tax rules.

3.1 Determination of residence for tax purposes

Often it is necessary to consider whether a company is "*by virtue of the law of [a territory], resident for the purposes of tax in [the territory]*" when determining eligibility for particular reliefs.[3] We recommend that wording could be introduced into the TCA 1997 to clarify that a company that is resident in a territory for the purposes of a double tax treaty with Ireland shall be considered to be resident "*by virtue of the law of*" that territory.

3.2 Separate trade requirement under section 291A TCA 1997

Section 291A TCA 1997 provides relief for companies for expenditure incurred by a company on intangible assets after 7 May 2009. However, the current provisions require taxpayers to treat income derived from an intangible asset which qualifies for the relief, as income from a separate trade. In our view, the requirement to artificially segregate single trades under section 291A TCA should be removed. The determination of what might be a just and reasonable way to apportion such costs is subjective and can add considerable complexity to the regime, which is administratively burdensome, resulting in significant compliance costs for taxpayers.

3.3. Direct demergers

The tax outcomes for shareholders are different depending on whether a direct demerger is implemented by way of an income distribution or a capital reconstruction, even though the commercial result of the demerger for shareholders is the same. We recommend that the differentiation between direct demergers that are implemented via an income distribution or a capital reconstruction should be removed.

3.4 The interaction between section 79C TCA 1997 and the close company surcharge

It is understood that foreign exchange gains realised by certain holding companies that are taxed under the provisions of section 79C TCA 1997 may fall within the scope of 'investment income' for close company surcharge purposes and that that is an unintended consequence of the legislation. We recommend that a new subsection be inserted into section 79C as follows: *"Any income chargeable under Case IV of Schedule D by virtue of this section shall not be taken into account in computing 'investment income' for the purposes of section 434*."

3.5 Professional subscriptions

To ensure that Ireland continues to promote the highest professional standards and continuous learning to support business, we urge that the statutory basis for exemption from BIK under section 118 (5E) TCA 1997 is reinstated for professional subscriptions.

3.6 Proportionality of penalties and interest

We recommend that the proportionality of fixed penalties should be re-examined to ensure that they do not result in disproportionately harsh treatment of taxpayers who

[3] For example, this is the test applied under section 246(3)(h)(I) TCA 1997 and under section 626B(2)(b) TCA 1997

make innocent mistakes. In our view, the rate of interest imposed on the late payment of tax should reflect the actual cost to the Exchequer and be tracked to prevailing ECB market rates.

4. Measures to help address issues in the housing sector

In light of the current housing crisis, we recommend two legislative changes to the *Residential Development Stamp Duty Refund Scheme (SDRS)*, which we believe would encourage the supply of housing available for rental and reduce the cost of certain homes for buyers.

The SDRS provides for a 4% stamp duty refund for land that is subsequently developed for residential purposes.[4] One of the conditions to qualify for the refund is a requirement that housing units account for at least 75% of the total surface area of the land. However, in many cases it is not possible to meet the 75% test due to the requirements of Local Area Plans. In our view the alignment of the SDRS with Local Area Plans would encourage residential development in certain areas by reducing the costs of construction of residential units on that land.

A further condition of the SDRS is that construction of a development must be completed within two years. In many instances this is an unrealistic timeframe, with the result that the SDRS is unavailable and there is a consequential increased cost for the purchaser of the residential unit. We would suggest an extension of the current timeframe for completion of the construction of residential developments from two to three years.

5. Issues arising from recent High Court decisions

Two High Court decisions in 2019, both of which were held in favour of the taxpayers, have raised concerns regarding their impact on related legislative provisions that were not considered by the court.

5.1 Payment in respect of a 'qualified adult'

The High Court decision in the *O'Neill*[5] case considered the issue of who should be taxed on the additional payment to the contributory State pension, known as the 'qualified adult' payment. The court determined that the dependent (i.e. the 'qualified adult') is the beneficial owner of the payment and therefore is the taxable person.

In contrast, section 126(2B) TCA 1997[6] provides that where there is payment in respect of a 'qualified adult', the payment shall be treated as a payment to the pension holder for income tax purposes and not the 'qualified adult'. This means that a 'qualified adult' cannot avail of an increased income tax standard rate band or PAYE tax credit in respect of the additional payment.

Section 126(2B) TCA 1997 clearly conflicts with the High Court decision and the Social Welfare Consolidation Act 2005 (as amended), which explicitly provides that the amount of the increased pension is payable directly to the 'qualified adult'. We believe that section

[4] Section 83D Stamp Duties Consolidation Act 1999 (as amended)
[5] *Michael O'Neill v The Revenue Commissioner*s [2018] IEHC 388
[6] Inserted by Section 12 Finance (No. 2) Act 2013

126(2B) TCA 1997 is inequitable, and therefore, we recommend that the provision should be deleted.

5.2 Dwelling House Exemption from Capital Acquisitions Tax

Finance Act 2016 inserted a new section 86(2)(c) Capital Acquisitions Tax Consolidation Act (CATCA) 2003, which requires the dwelling house that is subject to a claim for dwelling house exemption should be the only dwelling house that a successor is beneficially entitled to at the date of the inheritance.

As a result of the High Court decision in the *Deane*[7] case, it would appear that any beneficiary who inherits a dwelling house under the residuary clause in a will cannot satisfy this condition. Furthermore, it is questionable whether any beneficiary of a specific bequest of a dwelling house under a will can satisfy the condition.

Therefore, it would appear that only when a beneficiary is a joint owner of a property at the date of death and the property passes by survivorship, that the beneficiary will be able to avail of the dwelling house exemption. We recommend that section 86 CATCA 2003 is amended to ensure that the circumstances where dwelling house exemption applies are clearly defined in the legislation.

[7] *Leanne Deane v The Revenue Commissioners* [2017] No. 279R

Appendix

1. The potential impact of section 135 TCA 1997 on the sale of a family business/SME

The passing on of family businesses and management buy-outs (MBOs) involving ‘close companies’ continue to be impacted by the anti-avoidance provision contained in section 135 (3A) TCA 1997, which was inserted by Finance Act 2017.[8]

Subsection 3A is an anti-avoidance provision which applies to situations involving close companies. However, as the vast majority of companies in the SME sector are ‘close companies’, so the impact of the provision has been extensive.

Subsection 3A now imposes income tax treatment on selling shareholders in any situation where Revenue take the view that a company has retained profits in excess of the company’s commercial needs, rather than allowing those shareholders to obtain capital gains tax (CGT) treatment.

Unlike other anti-avoidance provisions in Irish tax legislation, section 135 TCA 1997 does not include a *bona fide* test. It is normal practice in targeted anti-avoidance legislation to exclude transactions effected for *bona fide* commercial reasons, so as to avoid any unintended consequences that could arise as a result of the legislation.

Considerable concern continues to exist regarding the potential effect of section 135 on scaling up and passing on of businesses in the SME sector, in the absence of a statutory *bona fide* test. Feedback from our members is that the provision is still causing uncertainty in circumstances where owners of family businesses or SMEs are implementing transactions, notwithstanding the existence of Revenue guidance.[9]

Even though Revenue guidance may confirm that bona-fide financing arrangements entered into by a purchaser relating to the acquisition of shares are outside the scope of the provisions, as noted in your letter of 5 June 2019 to the Institute, this is not expressed in legislation. Therefore, it cannot be relied upon by taxpayers in the event of the matter being disputed and subject to an appeal. In fact, the Appeal Commissioners have expressly stated that their jurisdiction does not extend to supervising the administrative actions or any purported inequity in the application of the tax code by Revenue.[10]

In our view, inserting an exclusion for *bona fide* commercial transactions into section 135 TCA 1997 is essential, to provide the necessary level of certainty to taxpayers and their advisers, when implementing transactions involving the disposal of shares in a company with cash on its balance sheet.

[8] Section 430 TCA 1997 defines a close company as an Irish resident company that is under the control of 5 or fewer participators, or by participators who are directors, whatever the number.
[9] eBrief 03/18: Tax and Duty Manual 06.02.05 – Section 135 TCA – Anti-avoidance, Part 6/Chapter 2, January 2018
[10] Tax Appeals Commission determination 20TACD2018 regarding Income Tax

Institute Recommendation:
Considerable concerns continue to exist regarding the potential effect of section 135 (3A) TCA 1997 on scaling up and passing on of businesses in the SME sector, in the absence of a statutory bona fide test. In our view, inserting a legislative exclusion for *bona fide* commercial transactions into section 135 TCA 1997 is required, to provide the necessary level of certainty to taxpayers and their advisers when considering their scaling options, notwithstanding the existence of Revenue guidance.

2. Measures to alleviate the impact of a 'no-deal' Brexit

We understand from our discussions with Revenue at TALC that it was intended that the Withdrawal Act, which was enacted on 17 March 2019, would cover only those measures that would have an immediate impact in the event of a 'no-deal' Brexit and that other Brexit-related tax issues would be addressed in the Finance Bill.

We have identified several circumstances that are not covered by the Withdrawal Act, which we believe should be included in Finance Bill 2019, in order to ensure that the status quo for taxpayers will be maintained in the event of a 'no-deal' Brexit.[11] These are as follows:

Distribution treatment – Section 130 TCA 1997

Section 130(2)(d)(iv) TCA 1997 reclassifies interest payments made by an Irish company to a non-resident company as a distribution, in circumstances where (subject to certain conditions) the companies are 75% associated.

Section 130(2B) TCA 1997 disapplies distribution treatment where the interest payments are made to a company that is resident in a Member State in certain circumstances. However, in the context of a 'no deal' Brexit, this disapplication will no longer apply to interest payments made by a company to an associated company resident in the UK. Interest paid on existing and new loans with UK lenders which are currently eligible for relief as a charge on income will therefore no longer be deductible.

In addition, section 130(3) TCA 1997 provides that, where a company transfers assets or liabilities to its members or vice versa and the value of any new consideration provided by its members is less than the market value of the benefit transferred, the excess is treated as a distribution.

However, such transfers between Irish resident companies are not treated as distributions, where one company is a subsidiary of the other or both are subsidiaries of another company which is resident in a "relevant Member State". "Relevant Member State" is defined for this purpose as an EU Member State or an EEA country with which Ireland has concluded a DTA.

[11] The non-discrimination article contained in the Ireland/UK Double Taxation Agreement may ensure that the status quo is maintained post-Brexit for certain taxpayers. However, it is generally only relevant in circumstances where less favourable tax treatment applies as a result of some or all the share capital of an Irish company being held directly or indirectly by a UK company. Therefore, as the non-discrimination article will not maintain the status quo for all taxpayers, specific amendments to domestic legislation are required.

Institute Recommendation:
In order to retain the status quo in the context of a 'no-deal' Brexit, we recommend that section 130(2B) and section 130(3) be extended to ensure that UK resident companies remain included.

Group of companies - Section 616 TCA 1997

Section 616 TCA 1997 defines a group of companies for the purposes of many provisions that deal with the taxation of chargeable gains. Broadly, section 616 provides that a principal company and all its effective 75% subsidiaries form a group, with a 'company' being defined as one which is tax-resident in a "relevant Member State" (subject to certain exceptions outlined below). "Relevant Member State" is defined as an EU Member State or an EEA country with which Ireland has concluded a DTA.

In the event of a 'no-deal' Brexit, UK companies will cease to be tax-resident in a "relevant Member State" and will thus cease to be part of a 'group of companies' under section 616 TCA 1997.

Specific exceptions to the definition of 'group of companies' are contained in section 617 (transfer of assets) and section 623 (company ceasing to be a member of group). For the purposes of these sections, only a 'group of companies can include a company that is resident in any country with which Ireland has concluded a DTA for the purpose of these sections only. Companies that are resident in the UK will therefore remain included for the purposes of these sections.

However, the definition of a group of companies as set out in section 616 will have an impact for many other sections in the TCA 1997. For example:

- Section 618 TCA 1997 which relates to the transfer of trading stock within a group. While transfers of assets will continue to be within section 617, transfers of trading stock in the circumstances set out in section 618 would not.

- Section 625 TCA 1997 applies where a subsidiary company ceases to be a member of a group of companies and another company (the 'chargeable company') had, within the previous ten years, disposed of shares in the subsidiary company in the course of an amalgamation or reconstruction in the group. Where the section applies, the chargeable company is deemed, at the time of the amalgamation or reconstruction, to have disposed of and immediately reacquired the shares in the subsidiary company at market value.

  It would appear that section 625 would have immediate effect in the event of a 'no-deal' Brexit, where the subsidiary company that was party to an earlier amalgamation or reconstruction is UK resident and ceases to be a member of the group of companies as defined by section 616 TCA 97.

- Section 586 TCA 1997 (which deals with company amalgamations by exchange of shares) and section 587 TCA 1997 (which deals with company reconstructions and amalgamations) both contain provisions that apply where the companies in question are members of a group of companies, as defined by section 616 TCA 1997. We note that the Withdrawal Act amends section 80 SDCA 1999 (Reconstructions or Amalgamations of Companies) to ensure that UK-based acquiring companies can continue to be able to avail of stamp duty relief. There would appear to be no reason why the CGT provisions should not be similarly amended.

Institute Recommendation:
To ensure that the provisions set out in sections 618, 625, 586 and 587 TCA 1997 can continue to apply to groups with UK tax-resident members, and in particular to ensure that section 625 TCA 1997 does not give rise to a clawback, in the event of a 'no-deal' Brexit, we recommend that the meaning of 'company' and 'relevant Member State' within section 616 TCA 1997 are amended to ensure that the UK remains included in the event of a 'no-deal' Brexit.

Exit Tax – Part 20 Chapter 2 TCA 1997

Section 627 TCA 1997 contains provisions that impose an exit charge on companies that are resident in another "Member State" in respect of certain assets transferred from a permanent establishment in Ireland. There is no definition of "Member State" provided, however, section 627(1)(c) provides that "*a word or expression that is used in this Chapter and is also used in Article 5 of the Directive shall have the meaning in this Chapter that it has in that Article*".

The Directive referred to is Council Directive (EU) 2016/1164 of 12 July 2016. Therefore, it would appear that the meaning of "Member State" should be taken from this Directive, which would of course exclude the UK in the event of a 'no-deal' Brexit.

Section 629 TCA 97 contains an option to defer the payment of an exit charge, spreading the payment over six instalments. The option to defer is available only where the relevant transfer is to a "relevant territory". "Relevant territory" is defined in section 629(1) as an EU Member State or a qualifying EEA country.

Institute Recommendations:
Depending on whether it is intended that the exit charge should continue to apply to UK resident companies that transfer assets from a permanent establishment in Ireland, consideration may need to be given to amending the scope of section 627 TCA 1997.

Furthermore, the definition of "relevant territory" in section 629 TCA 1997 may need to be amended to ensure that the UK remains included in the event of a 'no-deal' Brexit.

Double Tax Relief under Schedule 24 TCA 97

The application of a number of provisions in schedule 24 TCA 1997, which deals with Double Tax Relief, will be restricted in circumstances where a UK company is no longer resident in a "relevant Member State" (which is defined as an EU Member State or an EEA country with which Ireland has a DTA).

Irish parent companies would not be entitled to any additional foreign credit under paragraph 9I in respect of dividends received from UK resident companies, as a UK resident company would no longer qualify as a “source company”.

Several other provisions within schedule 24 are conditional on a company being resident in a “relevant Member State”. These include:

- Paragraph 9A: Unilateral Relief
- Paragraph 9B: Dividends paid between related companies: Relief for Irish and third country taxes
- Paragraph 9C: Non-Resident companies carrying on a trade in Ireland via a branch/agency
- Paragraph 9DA: Unilateral Relief (branch profits).

Institute Recommendation: We recommend that the definition of “relevant Member State” in schedule 24 TCA 1997 be amended to ensure that the UK remains included in the event of a ‘no-deal’ Brexit.

Securitisation – Section 110 TCA 1997

Section 110(5A) TCA 1997 provides that a deduction is available for profit-participating interest only in a number of qualifying circumstances, for the purposes of calculating the profits of specified property business. These circumstances include where the interest is paid to:

- a pension scheme or PRSA or an equivalent in a "relevant Member State"; or
- an individual who is a national of a "relevant Member State" or
- to a company formed under the laws of a "relevant Member State" (subject to certain conditions).

"Relevant Member State" is defined in section 110(5A) TCA 1997 as another Member State or an EEA State. In our view, the definition of “relevant Member State” should be amended to ensure that the UK remains included in the event of a ‘no-deal’ Brexit.

Institute Recommendation: "Relevant Member State" is defined in section 110(5A) TCA 1997 as another Member State or an EEA State. In our view the definition of “relevant Member State” should be amended to ensure that the UK remains included in the event of a ‘no-deal’ Brexit.

Shipping: Tonnage Tax – Section 697H TCA 97 and Section 697A TCA 1997

Section 697H TCA 1997 contains provisions which allow the distributions of an overseas company to be treated as “relevant shipping income”, in circumstances where over 50% of the voting power of the overseas company is held by one or more companies that are resident in a “Member State” as defined by section 697A TCA 97. We recommend that the definition of “Member State” be amended to ensure that the UK remains included in the event of a ‘no-deal’ Brexit.

Institute Recommendation:
We recommend that the definition of “Member State” in section 697A TCA 1997 be amended to ensure that the UK remains included in the event of a ‘no-deal’ Brexit.

Life Assurance Companies: Policyholders – Section 730D TCA 1997

Section 730D TCA 1997 contains provisions regarding the treatment of gains arising on a chargeable event relating to a life policy. Section 730D (2A) TCA 1997 allows Revenue, subject to certain conditions, to grant approval to life companies excluding them from the requirement to obtain non-resident policyholder exit declarations, where the business is written through a branch in an offshore state or the business is written on a freedom of services basis and the policyholder resides in an offshore state. Offshore state for the purposes of section 730D is defined as an EU or EEA State.

If life assurance companies are permitted to sell life policies into the UK post-Brexit (the regulatory position in currently unclear), subsection (2A) will not apply and it will be necessary for the companies to obtain individual non-resident declarations from policyholders.

Furthermore, as the status of existing approvals, once the UK leaves the EU, is unclear this provision could have an immediate impact on business already written, where exit tax would have to be deducted, if exit tax declarations are not obtained and there is a doubt over whether the approval already granted still applies.

Institute Recommendation:
We recommend that the definition of “offshore state” for the purposes of section 730D TCA 1997 be amended to ensure that the UK remains included in the event of a ‘no-deal’ Brexit.

Real Estate Investment Trusts (REIT) – Part 25A TCA 1997

In order to be regarded as a REIT or group REIT, a company or a principal company of the group must meet certain conditions. One of these conditions is that the company must have its shares listed on the main market of a recognised stock exchange of a Member State.

Section 705A TCA 1997 defines a “recognised stock exchange” as being a stock exchange in a Member State, which is regulated by the appropriate regulatory authority of that Member State.

Institute Recommendation:
We recommend that the definition of a “recognised stock exchange” in section 705A TCA 1997 be amended to ensure that UK stock exchanges remain included in the event of a ‘no-deal’ Brexit.

Irish Real Estate Funds (IREF) – Part 27 TCA 1997

Where an IREF has transferred some or all its IREF business to a specified company before 1 July 2017, then the tax arising on the IREF taxable event can be deferred, subject to certain conditions, for a period of up to 10 years under section 739V TCA 1997.

One of the events under which the tax becomes due and payable is where the company ceases to be resident in the EU or an EEA country. Therefore, it would appears that this section could have immediate effect in the event of a 'no-deal' Brexit, where an IREF has transferred an IREF business to a company that is UK resident.

Institute Recommendation:
In our view, the meaning of "specified company" and the provisions of section 739V(4)(d) TCA 1997 should be amended to ensure that UK resident companies remain included in the event of a 'no-deal' Brexit.

In addition, section 739K(1) TCA 1997 also includes a definition of "*specified person*" for the purposes of Part 27, Chapter 1B. Tax arises on the happening of an IREF taxable event in respect of a specified person. The definition of "*specified person*" excludes:

> *"a pension scheme, undertaking or company equivalent to those referred to in paragraphs (a) to (c), authorised by a Member State or an EEA state and subject to supervisory and regulatory arrangements at least equivalent to those applied to those pension schemes, undertakings or companies, as the case may be, in the State"*

Institute Recommendation:
We recommend that the meaning of Member State for the purposes of Part 27, Chapter 1B be widened to ensure that a pension scheme, undertaking or company, which is authorised by the UK and which fulfils all other legislative requirements, will not be regarded as a "*specified person*" in the event of a 'no-deal' Brexit.

<u>Rate applicable to certain deposit interest received by individuals – Section 267M TCA 1997</u>

Section 267M TCA 1997 provides that EU-sourced deposit interest will be taxed at the reduced rates set out in section 256 TCA 1997 (the DIRT rates), subject to certain conditions being met.

Institute Recommendation:
We recommend that section 256 TCA 1997 be amended to ensure that UK-sourced deposit interest continues to be taxed at the DIRT rates. in the event of a 'no-deal' Brexit.

<u>Relief for investments in films – Section 529B TCA 1997</u>

Chapter 1A of Part 18 provides for a withholding tax which must be deducted from payments made to non-resident artistes. A "non-resident" is defined for this purpose as an individual who is neither resident nor ordinarily resident in an EU Member State or an EEA country.

Institute Recommendation:
We recommend that the definition of "non-resident" be amended to ensure that UK resident individuals remain excluded for the purposes of the withholding tax in the event of a 'no-deal' Brexit.

Restriction of certain reliefs – Section 1032 TCA 1997

In general, non-resident individuals are not entitled to the personal allowances, deductions and reliefs specified in the Table to section 458 TCA 1997. However, section 1032 TCA 1997 provides that a portion of the allowances may however be available in certain circumstances, including where the individual is a citizen, subject or national of another EU Member State. In these circumstances, the portion is determined by the ratio of Irish sourced income to the total income of the individual.

In the context of a 'no deal' Brexit, British citizens not resident in Ireland will no longer be entitled to these personal allowances, deductions and reliefs, unless they meet one of the other conditions contained in section 1032(2).

Institute Recommendation:
In our view, section 1032 TCA 97 should be amended to ensure that British citizens continue to be entitled to specified personal allowances, deductions and reliefs.

EU Directives

Several measures are included in the TCA 1997 in order to transpose EU Directives into Irish law. This includes Part 21, Chapter 1 TCA 97 which deals with Mergers, Divisions, Transfers of Assets and Exchanges of Shares concerning companies of different Member States.

We note that the Withdrawal Act contains an amendment to section 87B SDCA 1999, so that UK-based companies acquiring Irish property, as part of a merger will continue to be able to avail of the stamp duty exemption. The non-availability of stamp duty relief would make mergers more expensive and thus less attractive.

In the event of a 'no deal' Brexit, the various corporation tax and CGT relieving measures that are provided in Part 21, Chapter 1 TCA 1997 would also no longer be available for transactions involving UK companies. We would suggest that consideration should be given to widening the definition of "company" and other references to "Member State" in section 630 TCA 1997, as appropriate, to ensure that UK companies remain included.

Institute Recommendation:
We would suggest that consideration should be given to widening the definition of "company" and other references to "Member State" in section 630 TCA 1997, as appropriate, to ensure that UK companies remain included.

Other relevant measures in the TCA 1997 include:

- Part 8, Chapter 6: Interest and Royalties Directive
- Section 831: Parent/Subsidiary Directive

To the extent that UK companies are no longer covered by the above provisions, this may give rise to the imposition of withholding taxes or may result in an increased administrative burden.

Institute recommendation:
We would suggest that consideration should be given to widening the definition of “company” in section 267G and section 831 TCA 1997, to ensure that UK companies remain included, in the event of a ‘no-deal’ Brexit.

Companies Act 2014

Section 137(1) Companies Act 2014 requires a company to have at least one director resident in an EEA state. This requirement is set aside only where:

- the company has put in place a bond (section 137(2) Companies Act 2014), or
- the company has obtained a certificate from the Registrar, stating that the company has a real and continuous link with an economic activity being carried out in Ireland (section 140 Companies Act 2014).

We understand that several Irish companies currently rely on a UK resident director to fulfil this requirement. Such companies would be in breach of Irish company law, in the context of a 'no deal' Brexit.

Institute Recommendation:
We would suggest that consideration should be given to expanding the scope of section 137(1) Companies Act 2014 to include a person who is resident in the UK.

3. Measures to provide tax certainty for business

Irish businesses need certainty over their tax affairs and in order to achieve this we need clear tax rules. We have outlined six key areas below where we believe that amendments are required to existing legislation in order to provide the necessary certainty for businesses in applying tax rules.

Determination of residence for tax purposes

Often it is necessary to consider whether a company is *"by virtue of the law of [a territory], resident for the purposes of tax in [the territory]”* when determining eligibility for particular reliefs. For example, this is the test applied under Section 246(3)(h)(I) TCA 1997 relating to the recipient of interest and under Section 626B(2)(b) TCA 1997 relating to the investee company.

There is a well-reasoned view that the provisions of a DTA form part of the law of the contracting states, with the result that a company that is resident in a territory under the terms of a DTA shall be considered resident "by virtue of the law of" that territory. This approach would appear to be accepted by Revenue in principle.

For example, Revenue’s Tax and Duty Manual 08-03-06, clarifies that certain interest paid to companies in Hong Kong (which operates a territorial regime) can qualify for relief under section 246(3)(h) TCA 1997, with the residence test being satisfied where the company is *"treated as a resident of Hong Kong for the purposes of the double tax treaty with Ireland".*

Due to the significance of this point for taxpayers and the Revenue, it would be helpful if clarification was given by way of legislative amendment. We would suggest that this could be achieved by inserting the following wording into sections 246 TCA 1997 and other relevant provisions:

> *"For the purposes of subsection (3)(h)(I), a company which is treated as a resident of a relevant territory under arrangements made with the government of a territory outside the State having the force of law by virtue of section 826(1) shall be regarded as a company which, by virtue of the law of the relevant territory, is resident in the relevant territory for the purposes of tax"*

The proposed amendment should remove any doubt that residence for the purposes of tax includes treaty residence. We believe that the proposed amendment would be in line with the approach to be adopted under the Multilateral Instrument, which means that many of Ireland's tie-breaker clauses will become Competent Authority based tie-breaker clauses, with the result that agreement can be reached between the authorities as to the residence of a person.

Institute Recommendation:
We would suggest that wording could be introduced into the TCA 1997 to clarify that a company that is resident in a territory for the purposes of a DTA with Ireland shall be considered to be so resident "*by virtue of the law of*" that territory.

<u>*Separate trade requirement under section 291A TCA 1997*</u>

Section 291A TCA 1997 provides relief for companies for expenditure incurred by a company on intangible assets after 7 May 2009. However, the current provisions require taxpayers to treat income, derived from the intangible asset which qualifies for the relief, as income from a separate trade. which in many cases is subjective and can add considerable complexity to the regime, as there is often no clear basis for making the necessary apportionments.

For example, if a company had existing manufacturing processes using intellectual property developed or acquired before 8 May 2009 and one of those processes is enhanced by intellectual property (IP) developed or acquired after 7 May 2009, then the profit from products that go through the enhanced process are required to be segregated from the total trade and treated as a separate trade.

If the production of products are regularly moved between different production lines, the extent to which sales are generated from products that have specifically been subjected to the enhanced manufacturing process might be extremely difficult to ascertain. However, the taxpayer is required to artificially segregate what is a single trade into two separate trades and apportion common costs between the two trades on a just and reasonable basis.

Another example would be where a company has both acquired IP, which qualifies for relief and internally developed IP, which frequently will not qualify for relief. Both types of IP are used to produce a medical device produced by the company. If a new machinery is acquired to manufacture the medical device, it is not clear how the cost of the new machinery should be apportioned if the internally acquired IP does not qualify for relief.

Institute Recommendations:
In our view, the requirement to artificially segregate single trades under section 291A TCA should be removed. The determination of what might be a just and reasonable way to apportion such costs is subjective and can add considerable complexity to the regime, which is administratively burdensome, resulting in significant compliance costs for taxpayers.

Direct demergers

Groups of companies may seek to restructure by means of a direct demerger for a number of commercial reasons. For example, to allow shareholders to invest independently in different companies within a group or to give a division the opportunity to grow in a new environment that is separate from the parent company's history and corporate image.

A direct demerger can be implemented under Irish law by a parent company transferring its shares in a subsidiary to its shareholders. However, this is deemed to be an income distribution for Irish tax purposes, subject to income tax, USC and PRSI. The dividend withholding tax implications of the deemed income distribution arising on a demerger are complex, as the distribution of shares in the subsidiary is in a non-cash form and therefore, must be re-grossed and funded by the parent company.

Alternatively, a capital reconstruction can be implemented to achieve a demerger. A new company is incorporated, which issues shares to the shareholders in return for the parent company transferring its shares in the subsidiary to the new company. Irish tax resident shareholders can avail of reorganisation relief,[12] so that there is no disposal for CGT purposes. The shareholders are deemed to acquire the shares in the subsidiary at the same time as their original shares in the parent company and the original base cost of the shares is apportioned between their shares in the parent company and the new shares in the subsidiary.

Therefore, the tax outcomes for shareholders are different depending on whether the demerger is implemented by way of an income distribution or a capital reconstruction, even though the commercial result of the demerger for the shareholders is the same.

In contrast, the UK does not differentiate between demergers implemented either by way of an income distribution or a capital reconstruction, provided certain conditions are met.[13] We recommend that the differentiation between direct demergers that are implemented via an income distribution or a capital reconstruction should be removed.

[12] Section 587 TCA 1997

[13] See section 1075 Corporation Tax Act 2010. The transaction is treated as falling within the UK reorganisation rules, so that the shareholders' original base cost in the shares of the parent company is apportioned between its shares in that company and the shares it receives in the subsidiary, as a result of the demerger. There is no disposal of the shares in the parent company for UK tax purposes.

Institute Recommendation:
We recommend that the differentiation between direct demergers that are implemented via an income distribution or a capital reconstruction should be removed. Each shareholder should be treated for capital gains tax purposes, as if the shares transferred to them, by way of a direct demerger, are acquired by them at the same time as they acquired the original shares in the parent company and for an appropriate portion of the consideration for the original shares in that company.

Interaction of the close company surcharge with Section 79C TCA 1997

Section 79C TCA 1997 provides that gains or losses arising from the disposal of foreign currency held in an Irish bank, by certain holding companies, are chargeable to corporation tax as Schedule D Case IV income, rather than CGT.

To prevent a consequent loss to the Exchequer, the amount of any currency gain brought into the charge to corporation tax is increased, so that the tax payable equates to the tax that would have been payable if CGT had applied. It is understood that foreign exchange gains taxable under section 79C TCA 1997 fall within the scope of "investment income" for close company surcharge purposes and that this was an unintended consequence of the legislation.

To address this unintended consequence, we recommend that a new subsection be inserted into section 79C as follows: "*Any income chargeable under Case IV of Schedule D by virtue of this section shall not be taken into account in computing 'investment income' for the purposes of Section 434.*"

Institute Recommendation:
It is understood that foreign exchange gains taxable under section 79C TCA 1997 fall within the scope of "investment income" for close company surcharge purposes and that this is an unintended consequence of the legislation.

To address this unintended consequence, we recommend that a new subsection 7 be inserted into section 79C TCA 1997 as follows: *"Any income chargeable under Case IV of Schedule D by virtue of this section shall not be taken into account in computing 'investment income' for the purposes of Section 434*."

Professional subscriptions

Section 118 TCA 1997 was amended in 2011, so that the payment of a subscription to a professional body by an employer on behalf of an employee is treated as a taxable benefit-in-kind (BIK), subject to PAYE, PRSI and USC.

Membership of professional bodies and the necessary adherence to codes of professional conduct, continuous professional development, lifelong learning and knowledge-development are important in the delivery of high-quality service and in growing the Irish economy. Now, more than ever, the promotion of the highest standards and continuous learning are essential to supporting businesses with international challenges and opportunities, such as Brexit. The skills of our professions in Ireland will be central to this country remaining agile and capable of dealing with change. We need a skilled labour force who are performing at the highest standards of quality, professionalism, knowledge and innovation.

In the best interests of the development and standards of Ireland's professions, we urge that the statutory basis for exemption from BIK is reinstated for professional subscriptions. This could be achieved by amending section 118 (5E) (c) to reactivate the relief.

Institute Recommendations:
In the best interests of the development and standards of Ireland's professions, we urge that the statutory basis for exemption from BIK under section 118 (5E) TCA 1997 is reinstated for professional subscriptions.

Proportionality of penalties and interest

The Institute fully appreciates the rationale for imposing penalties and charging interest on late filings. However, there are two important areas where we believe the level of sanction imposed is disproportionate to any error made. These are:

- *Fixed penalties*

  Tax legislation and regulations contain numerous fixed penalties. Fixed penalties regularly apply to breaches of administrative requirements in tax law, such as, notifications to Revenue, invoicing and the maintenance of books and records. The level of the penalty can be substantial, amounting to €3,000 or €4,000 for each instance of non-compliance, even when there is no loss of tax revenue to the Exchequer.

  In our view, the level of fixed penalties can often be disproportionate to the errors to which they relate. We believe that the penalty rates in legislation and regulations should be re-examined to ensure that they do not result in overly harsh treatment of taxpayers who make innocent mistakes.

- *Interest on delayed payment of tax*

  Interest is charged on the late payment of tax in Ireland at annualised interest rates of 8% and 10%, far in excess of the Irish mean interest rate, which was 3.3% in January 2019.[14] In contrast, HMRC in the UK currently imposes interest at a rate of 3.25% (i.e. 2.5% above the current Bank of England base rate of 0.75%.[15]) In applying the UK interest regime the rate applied by HMRC is tracked at 2.5% above Bank of England base rate.

  This is an issue that the Institute has raised on a number of occasions in the past as it continues to be challenging for taxpayers. It is right and proper that interest should be

[14] National Competitiveness Council Report: Cost of Doing Business in Ireland 2019, April 2019, p. 44
[15] https://www.bankofengland.co.uk/monetary-policy/the-interest-rate-bank-rate

imposed to recompense the Exchequer for the time delay in receiving any underpayment of tax and provide a level playing field for taxpayers who do not pay on time. However, current high levels of interest charged on the late payment of tax in Ireland far outweigh the cost to the State and, in some cases, are causing considerable hardship.

Institute Recommendations:
The proportionality of fixed penalties should be re-examined to ensure that they do not result in overly harsh treatment of taxpayers who make innocent mistakes. The rate of interest imposed on the late payment of tax should reflect the actual cost to the Exchequer and be tracked to prevailing ECB market rates.

4. Measures to help address issues in the housing sector

In light of the current housing crisis, we have outlined below some tax measures which we believe would encourage the supply of housing available for rental and reduce the cost of certain homes for buyers.

Residential Development Stamp Duty Refund Scheme

With effect from 11 October 2017, the rate of stamp duty on the acquisition of non-residential property increased from 2% to 6%. However, in recognition of the housing supply challenges and with a view to encouraging residential property development, a Stamp Duty Refund Scheme (SDRS) was introduced, in tandem with the change in stamp duty rate. Under the SDRS, a refund of up to 4% may be claimed in respect of land that is subsequently developed for residential purposes.

The 75% test

A number of conditions must be met in order to qualify for the 4% stamp duty refund, including a requirement that housing units (or the gross floor space thereof) account for at least 75% of the total surface area of the land. However, this 75% test is not aligned with the current focus of government to enable people to live closer to where they work. This is a key objective of Project Ireland 2040 and is evidenced in many Local Area Plans for urban areas across the country which frequently limit the floor area of developments that may be allocated to residential units to an amount much lower than 75%.

For example, various areas in Cork city have been designated as mixed-use land in order to create a socially inclusive urban quarter and to promote the development of residential property in Cork city centre. In order to achieve this purpose, the Local Area Plan for the South Docks in Cork prescribes ratios for the split of residential and commercial development across the various regions in the city. The maximum gross floor area that can be occupied by residential development is limited to 30/40/50%, depending on the area. Accordingly, due to the constraints of the Local Area Plan, a developer cannot meet the 75% test and therefore, is faced with a significant stamp duty cost. This cost is ultimately passed on to the purchasers of the residential unit.

Revenue's guidance allows for the stamp duty refund for the residential element of a mixed-use development, where the residential and commercial parts of the development are completed in separate phases with separate commencement notices. However, due to the nature of inner-city construction sites, it is often impractical and uneconomical for such sites to be developed in separate phases and therefore, no relief will apply.

The alignment of the SDRS with Local Area Plans would remove the current barrier for residential development in certain areas. This would encourage greater supply of land which has a significant residential element and also reduce the costs of construction of residential units on that land.

Completion within two years

Another condition which must be met in order to qualify for the SDRS is that construction must be completed within two years of a local authority acknowledging a commencement notice or a 7-day notice as valid.

In practice, this is an extremely short timeframe for completion for most developments and despite best efforts being made, it is not possible to meet this timeframe in many instances, with the result that the SDRS is not available. This results in a consequential increased cost, ultimately borne by the purchaser of the residential unit. We would suggest that an extension of the current timeframe for completion of the construction of residential developments from two years to three years.

Institute Recommendations:

We recommend that the SDRS be aligned with Local Area Plans to remove the current barrier for residential development in certain areas. This would encourage greater supply of land, which has a significant residential element and also reduce the costs of construction of residential units on that land.

Currently, construction of a development must be completed within two years in order to avail of the SDRS. In many instances this is an unrealistic timeframe, with the result that the SDRS is unavailable and there is a consequential increased cost for the purchaser of the residential unit. We would suggest that an extension of the current timeframe for completion of the construction of residential developments from two years to three years.

5. Issues arising from recent High Court decisions

Two recent High Court decisions, both of which were held in favour of the taxpayers, have raised concerns regarding their impact on related legislative provisions, which were not considered by the court.

Section 126(2B) Taxes Consolidation Act 1997

The Social Welfare Consolidation Act 2005 (as amended) (SWCA 2005) allows for an increased contributory pension payment, during a period where the pension holder wholly or mainly maintains a 'qualified adult' (who is typically the spouse of the pension holder). The SWCA 2005 provides that the amount of the increased pension is payable to the 'qualified adult' or a person nominated by them.

The High Court case of *Michael O'Neill v The Revenue Commissioners*[16] considered the issue of who should be taxed in respect of this qualified adult payment; the pension holder or the 'qualified adult'. The court determined that it was the dependent adult who was the beneficial owner of the payment and therefore was the taxable person. The consequence of this decision was that the spouse was entitled to an increased income tax standard rate band and a PAYE tax credit in respect of the dependant adult payment.

Revenue has expressed the view at TALC that the High Court decision has no application for tax years post 2013, because of the application of section 126(2B) TCA 1997 (as inserted by section 12 Finance (No. 2) Act 2013). Section 126(2B) provides that where there is payment in respect of a 'qualified adult', that payment should be treated as income of the pension holder for income tax purposes. This means that a 'qualified adult' is not entitled to benefit from an increased income tax standard rate band or PAYE tax credit, for the 'qualified adult' additional payment for tax years post 2013.

Section 126(2B) TCA 1997 clearly conflicts with SWCA 2005 and the high court decision in the *O'Neill* case, which explicitly provides that the amount of the increased pension is payable directly to the qualified adult, who is beneficially entitled to it. In our view, section 126(2B) TCA 1997 is inequitable and therefore, we would recommend that the provision should be deleted.

Institute Recommendation:
In our view, section 126(2B) TCA 1997 conflicts with the Social Welfare Consolidation Act 2005, which explicitly provides that the amount of the increased pension is payable directly to the qualified adult. In our view, section 126(2B) TCA 1997 is inequitable and therefore, we would recommend that the provision should be deleted.

Dwelling House Exemption from Capital Acquisitions Tax (CAT)

Dwelling house exemption under section 86 CATCA 2003 provides relief from CAT where a home is passed on death, provided certain conditions are met. The recent High Court case of *Leanne Deane v The Revenue Commissioners*[17] related to the availability of dwelling house exemption, where a taxpayer inherited the family home and a 50% interest in four other residential properties, under the residuary clause of her father's estate.

The court considered whether the taxpayer satisfied the criteria set out in section 86(3)(b) CATCA 2003, which requires that the taxpayer is not beneficially entitled to any other dwelling-house at the date of the inheritance. The "date of the inheritance" is defined as "the date of the latest death which had to occur for the successor…to become beneficially entitled in possession to the benefit". Therefore, the general position is that the date of inheritance will also be the date of death.

[16] [2018] IEHC 388]
[17] [2017 No. 279 R]

The High Court determined that the taxpayer did not become beneficially entitled to any interest in any of the dwelling houses in the estate until after the date of death (and therefore after the date of the inheritance) and at the earliest when the net value of the estate was established. Therefore, the taxpayer qualified for dwelling house exemption, as she was not entitled to any other dwelling-house at the date of the inheritance.

Finance Act 2016 amended section 86 CATCA 2003 and the relevant subsection (section 86(2)(c) CATCA 2003) which now requires that the dwelling-house that is the subject of the claim for relief should be the only dwelling house the successor is beneficially entitled to at the date of the inheritance.

Following the High Court decision in the *Deane* case, it would appear that any taxpayer who inherits a dwelling house under the residuary clause in a will cannot satisfy this condition, as they will not be beneficially entitled to the property at the date of the inheritance. Furthermore, it is questionable whether any beneficiary of a specific bequest of a dwelling house under a will can satisfy the test set out in section 86 CATCA 2003.

Consequently, it would appear that only when a beneficiary is a joint owner of a property at the date of death and the property passes by survivorship, that the beneficiary will be able to avail of the Dwelling House Exemption. We recommend that section 86 CATCA 2003 is amended to ensure that the circumstances where dwelling house exemption applies are clearly defined in the legislation.

Institute Recommendation:
Following the High Court decision in the case of *Leanne Deane v The Revenue Commissioners,* we recommend that section 86 CATCA 2003 is amended to ensure that the circumstances where dwelling house exemption applies are clearly defined in the legislation.