



## **The Cost of Doing Business**

Submission to the Joint Committee  
on Jobs, Enterprise and Innovation

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## The Cost of Doing Business

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#### Background: Why costs and competitiveness matter right now

With both threats and opportunities on the horizon for Ireland and Irish businesses, the need to examine the barriers and cost burdens of doing business is now more important than ever.

Given the scale and threat of Brexit to Ireland, and its impact on all counties across the country, the Irish Tax Institute undertook a detailed analysis of the tax policy and tax administration system and its impact on Irish businesses of all sizes from a cost burden and blocker perspective. Naturally, the role of SMEs cannot be overstated, especially in the context of regional employment. They account for more than 70% of employment in all counties except Dublin, and they are the largest employer segment in Dublin, at 53%<sup>1</sup>.

We believe it is not just a matter of reducing costs and burdens so that we can meet the challenges and threats to Irish businesses arising from Brexit and other global uncertainties. We must also look at how the reduction in administrative burdens and costs can help make Ireland more competitive and better positioned to grasp the global changes and opportunities that are emerging, such as the digitisation of the world economy and the rapid growth in services as a share of world trade.

For example, a recent global report, *Digitizing Europe*<sup>2</sup>, has named Ireland as one of nine European front-runner countries that could see the largest benefits from a more digitised European economy because we are geographically small, with limited domestic markets, but are well digitised. There are however, challenges for some SMEs with reports showing that “less than one-third of Ireland’s SMEs are capable of processing e-commerce, and almost 25% have no website at all.”

The *Digitizing Europe* report has highlighted tax policies among the measures that are key to the successful digitisation of the nine economies, including Ireland. It highlights share options regimes, tax measures for angel investors, an attractive capital tax environment and measures that promote entrepreneurial activity. Tax burdens must be removed if Ireland is to achieve its full potential in this high growth area.

The role of tax policy in driving entrepreneurship was also clearly outlined by the IMF recently<sup>3</sup>. The IMF believes that high taxes can reduce the incentive to innovate and the entrepreneurial spirit; the design of growth friendly tax policy favouring entrepreneurship is something that is required.

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<sup>1</sup> CSO Statistical Release, Business Demography 2014 (6 July 2016).

<sup>2</sup> [Digitizing Europe, Why Northern European Frontrunners Must Drive Digitization of the EU Economy \(May 2017\)](#)

<sup>3</sup> [V. Gaspar and R. de Mooij, “Imagine What Fiscal Policy Could Do for Innovation”, IMFBlog](#)

## Costs for Irish businesses – the tax policy and tax administration challenges

The tax-related costs to Irish businesses arise from:

1. Tax policy – high taxes that place extra costs on business and make them uncompetitive, and
2. Tax administration – burdens and uncertainties in the tax administration system that lead to higher costs for business

Given the challenges and opportunities that lie ahead, the greatest cost of all lies in the opportunity lost to Irish businesses should we fail to have a tax policy and tax administration strategies that do not best serve the needs of Irish business. The impact of this will be felt in terms of their competitiveness, attractiveness, resilience and ability to compete internationally in the export market.

## Priority issues for Irish businesses and the respective challenges in Ireland's tax system

In June 2017, the Irish Tax Institute published a 140-page report titled 'A future tax strategy to grow Irish indigenous exports'. In making its 20 recommendations, the Institute first identified the key drivers that are critical to grow Irish businesses and the Irish economy. The drivers that are critical for growing revenues, expanding businesses and creating high quality jobs are:

1. highly skilled talent and expertise
2. innovation and R&D
3. access to capital investment and finance for growing and scaling businesses
4. new customers and markets

In many important respects, Ireland's tax policies are not fully aligned with the needs of the indigenous sector and will not drive the shift in behaviour that is required to meet the new global challenges and capture new global opportunities.

While our 12.5% corporation tax rate is highly valued by many Irish businesses, we have a pattern of sustained high rates across a range of other taxes that are also critical for growth and we have tax reliefs that are either not available or not accessible to Irish SMEs. This is creating challenges.

Ambition has been the central theme of many of the strategic plans published in 2016 and 2017. For example, Enterprise Ireland<sup>4</sup> has set out major strategic ambitions to increase client exports by €5bn to €26bn per annum by 2020.

In its Enterprise 2025 policy document<sup>5</sup>, the Government outlined its ambitions for Ireland's enterprises, including:

- to have Irish-owned companies reach 60% export intensity by 2020
- to broaden the base of Irish owned exports beyond UK markets by €5-€6 billion
- to increase the number of Irish-owned companies of scale by 30%
- to increase the number of enterprises surviving to 5 years by 25%.

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<sup>4</sup> Enterprise Ireland, "Enterprise Ireland Strategy 2017-2020" (15 May 2017).

<sup>5</sup> Department of Jobs, Enterprise and Innovation, Enterprise 2025: Ireland's National Enterprise Policy 2015–2025, Summary Report (November 2015).

Ambition is a shared effort that involves everyone: policy-makers, legislators, taxpayers, entrepreneurs, representative bodies and business organisations, State agencies and Revenue authorities. The Institute's report has specifically focused on the important tax policies and tax administration changes that we believe will contribute to achieving this ambition.

## 20 Irish Tax Institute Recommendations to reduce costs and improve competitiveness and resilience of Irish businesses

### 1. A new tax strategy for the Irish indigenous sector

The urgency and importance of a new growth and exporting strategy for Irish business requires:

- a. A tax policy strategy that encourages ambitious behaviour by Irish businesses and removes any blockers/costs that prevent this ambition; and
- b. That this is implemented and administered in a seamless way that is easy to understand and apply, that reduces costs and is barrier free for SMEs.

### 2. Extensive Government information campaign

An early and extensive information campaign should be rolled out for Irish businesses explaining both the tax policies in the strategy and how they will be administered.

## New tax measures for Ireland's capital gains tax (CGT) regime

### 3. Ireland's 33% CGT rate is the fourth highest rate in the OECD and it is having a negative impact on investment in Irish business.

This is a matter of real concern because investment in innovation, talent and equipment is essential if Irish businesses are to increase their level of exports abroad. By contrast, Germany outstrips the rest of the EU with its excellent record of business investment and its export prowess – it has a CGT rate of 25%. As well as hampering investment, the high rate of CGT is also dampening business activity in the Irish market and creating reluctant business owners who may hold onto businesses beyond the point where they have the capacity to grow them to the scale required in a new global exporting environment. The CGT rate needs to be reduced to a level that is closer to the median CGT rate amongst OECD countries, currently at 23%.

We know that Irish SMEs are more reliant on bank finance than those in other EU Member states and that they need to diversify into other equity sources of finance. The Government has recognised the need to develop appropriate alternative funding mechanisms to support companies over the coming years. This makes the capital gains tax environment critical.

High CGT rates in Ireland are a matter of real concern because investment in innovation, talent and equipment is essential if Irish businesses are to increase their level of exports. German *Mittelstand* companies are renowned for their levels of long-term investment, ensuring that German companies are among the highest-performing globally.

Those countries with targeted tax strategies for investors have seen direct results: venture capital investments in Israel were 14 times the level of those in Ireland in 2014, while the UK had the highest level of venture capital investment in Europe in 2015.

4. Revised Entrepreneur Relief, whilst welcome, is tightly restricted to owner managers and locks out much needed external investors from the possibility of availing of the lower CGT rate. This disparity should be removed. The €1m lifetime threshold for Entrepreneur Relief also needs to be increased to a minimum level of €10m to compete effectively with other countries for international capital.

## Tax measures for R&D and innovation

Innovation and new product development must underpin export growth. The importance placed on innovation is evident in its listing as one of four essential pillars in a new national exporting strategy, ‘Enterprise Ireland Strategy 2017–2020’<sup>6</sup>. It is key to deepening “resilience” in our enterprise base. International research reinforces this, showing that consumer companies have “become dependent on innovation for growth” and that new products alone account for 15-20% of annual sales in leading consumer companies. The reality in Ireland is that innovation and new product development are nowhere near where they need to be among SMEs if we are to achieve the important goal of product diversification.

Only 1% of small firms and 16% of medium firms consider themselves to be R&D active, low percentages in the context of our national ambitions. Older companies are driving the recent increases in R&D activity, but innovation in younger companies has flatlined since 2009. The 1% figure is a concern in the context of IMF findings<sup>7</sup> which show that SMEs are the drivers of change in innovation and National Competitiveness Council findings<sup>8</sup> which indicate that new start-ups are more inclined to engage in more radical innovations.

Overall, R&D expenditure in Ireland still falls some way short of the EU average and well short of countries such as Sweden, Germany and France. It is largely carried out by foreign multinationals. Without the innovation expenditure of the foreign-owned sector, Ireland would be the lowest overall performer in the EU in terms of share of GDP.

Ireland has an attractive R&D tax credit regime, but administration barriers are weighing heavily on its success in terms of the low take-up among SMEs. Irish Tax Institute research shows that 75% of Irish companies are aware of the R&D tax credit and 20% have availed of it. However, of those that availed of it, 47% said that the process was difficult to prepare for and administer. Only 35% of companies surveyed said that they intend to use it in the next 18 months, although this would rise to 62% if there was more clarity around the criteria for qualification.

5. Limits in the R&D tax credit regime for outsourcing restrict collaboration amongst Irish businesses and crucially between businesses and third level institutions. No outsourcing restriction is required under the OECD Modified Nexus rules for the Knowledge Development Box (KDB) and, since the rules of both regimes should be aligned, the outsourcing restrictions in the R&D tax credit regime should be removed.
6. At a time when all global indicators tell us that growth depends on innovation, every effort should be made to remove administrative blockers for businesses that need to claim the R&D tax credit. Only 1% of all small firms in Ireland consider themselves to be R&D active. If

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<sup>6</sup> Enterprise Ireland, “Enterprise Ireland Strategy 2017-2020” (15 May 2017).

<sup>7</sup> V. Gaspar and R. de Mooij, “Imagine What Fiscal Policy Could Do for Innovation”, [IMFBlog](#)

<sup>8</sup> National Competitiveness Council, Benchmarking Competitiveness: Ireland and the United Kingdom, 2017

we are to be truly innovative and global we must improve this performance and no stone should be left unturned in supporting SMEs to claim the R&D tax credit. This includes:

- A new SME friendly guidance campaign supported by dedicated Revenue support lines for SMEs with dedicated Revenue experts.
- A Revenue Centre of Excellence which deals with all taxpayer issues concerning the R&D tax credit regime.
- Sectoral specific guidance for each industry sector such as food & drink, ICT, bio-medical etc., all of which engage in very different R&D processes.
- A Revenue pre-approval process that would bring much needed certainty for taxpayers and subsequently prevent disagreements and costly future audits.
- Expert checks on the science element of R&D that are grounded in commercial reality rather than focused on academic concepts of “new to the world”. Regardless of how innovative a food company might be, it is very difficult to invent a food that is completely new to the world.

7. Revenue’s guidelines on the KDB are very comprehensive at 82 pages. However, a separate and less complex set of guidance is needed for SMEs, which have much more straightforward operations.

### **The personal tax environment and talent – tax measures**

High tax rates are also evident in the personal tax landscape, despite the backdrop of skills shortages and a very real and intense competition among countries for talent. Employees in Ireland have some of the highest effective tax bills in the world as salary levels rise above the average wage. The global shortage of talent is making its impact felt in Ireland and elsewhere, with 81% of Irish CEOs<sup>9</sup> now believing that the lack of availability of key skills is a top business threat to growth.

For example, over 2,800 ICT-related vacancies are listed on TechLifeIreland.com, a national website to attract technology talent into the country. Indeed, across the EU, 40% of companies recruiting ICT specialists are reporting problems finding candidates with the required skills, which is an indicator of the challenges facing high-growth sectors in our economy. The availability of skills is also a challenge for the knowledge-intensive advanced manufacturing sector, with reported skill shortages across a wide range of roles including chemical engineers, biochemists, biotechnology technicians and scientists.

Irish SMEs need the best human capital and talent to build strategic management expertise, innovation and R&D capability and to drive export-led expansion. This means being able to attract talent and afford the hiring of that talent. SMEs must compete with larger companies for talent, and 38% of them do not believe they can compete with larger companies when trying to recruit the best candidates.

8. Ireland’s urgent skills gaps and our capacity to address them is not helped by our high effective tax rates above the average wage. A phased plan is needed to reform the overall shape of our personal tax system. This includes a review of our high marginal tax rates, the breadth of our tax base and the entry points to income tax, USC and PRSI.

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<sup>9</sup> PwC, “Shaping Ireland’s Future Talent Landscape: 2017”, PwC HRD Pulse Survey.

9. A workable share-based employee remuneration scheme is also required for SMEs that would enable them to attract and retain the best talent in Irish businesses. The UK Enterprise Management Incentive (EMI) is a good model to consider – capital gains tax is payable by the taxpayer when they sell their shares and have the funds to pay the tax. A simple administrative process for collecting the information and paying the tax due is an important element of any new scheme.
10. Entrepreneurs are the job creators of Ireland and personal tax disparities that require them to pay higher taxes than PAYE taxpayers should be removed. This includes the additional 3% USC rate they pay on income above €100,000 and the €700 lower tax credit they receive.
11. The Special Assignee Relief Programme (SARP) helps businesses to attract international talent to work in Ireland. Many other countries have similar talent regimes. However, Ireland's SARP regime cannot be used by most Irish businesses because the relief only applies to staff assigned to Ireland from another group company abroad. The conditions of SARP should be reviewed to include new hires, so that Irish companies can avail of the regime.
12. Uncertainty about the tax treatment of travel expenses is creating concern and cost for many home workers, freelancers, employers with staff sent abroad to build the business and those dealing with the new working patterns of the modern world. Legislation in this area urgently needs to be brought up to date to deal with this issue.

### **Tax measures to expand export markets**

13. The Foreign Earnings Deduction (FED) reduces the income tax bill of employees travelling to develop export markets in thirty countries including the BRICS, some Middle Eastern, South American, Asian and African countries. With Irish companies needing new export markets more than ever, the range of qualifying countries should be reviewed and broadened.
14. There are also some significant gaps in Ireland's Double Taxation Agreement (DTA) network across Latin America, Africa and Southern Asia. These DTAs are critical for cross border trade as they prevent double taxation. Negotiating a DTA requires commitment and cooperation from both countries but, nonetheless, all efforts possible should be applied to address these gaps.
15. Irish companies sending employees abroad for short term visits often experience burdensome administrative difficulties when dealing with tax, payroll and double taxation issues. A new streamlined approach to these tax compliance issues is needed, complemented by further specialised Revenue support.

### **Income tax measures to support investment**

16. The Irish market contains a limited number of individuals who have funds to invest in business through the Employment and Investment Incentive (EII). At a time when these

businesses need a diverse range of finance, the annual cap of €150,000 per annum for these investors is further limiting the funding available for companies through the scheme. The equivalent UK EIS scheme has a Stg£1million investment limit and the limit for the Irish scheme should be increased to an equivalent amount.

17. As well as being capped, the EII income tax relief for investors is also split into two tranches – 30% in the year of investment and an additional 10% after three years, if the company meets certain employment targets. This concept of a split relief has been a feature of the EII relief since it replaced BES in 2011. However, it significantly reduces the attractiveness of EII and should be removed.
18. The EII rules require the investor to hold less than 30% of the company shares, effectively denying relief to the founder shareholder who may want to inject more funding into the business. This restriction does not apply in the UK and should be removed from our regime.
19. The Start-Up Refunds for Entrepreneurs (SURE) scheme should be extended to include new business founders who were previously self-employed and starting up another business. Presently only PAYE taxpayers can avail of the scheme and this disparity should be removed.
20. Dividend income in Ireland is taxed at high marginal personal tax rates of up to 55%, which does not encourage equity investment in Irish business. Most countries internationally tax dividends at a lower or flat rate. We recommend a flat rate of taxation of 20% on dividend income.

# Additional Day to Day Tax Administration Issues – The Cost Impact

## 1. Reduced compliance costs

Ireland maintained its position in 2016 as the easiest country in the EU in which to pay business taxes.<sup>10</sup> Keeping this focus on making tax compliance as easy and cost effective as possible plays an essential role in maintaining the competitiveness of Irish business and securing our attractiveness as a good place to do business for foreign direct investment. Revenue should continue to identify areas where the tax compliance process can be simplified to drive cost from the system to the benefit of both Revenue and the taxpayer. In doing so Revenue enhances the competitiveness of Irish businesses and further highlights Ireland as an attractive location for FDI or start-ups who are deciding where to locate.

Tax compliance is particularly burdensome for smaller businesses and the introduction of additional compliance costs should be avoided as far as possible. Where such measures are being considered, a cost-benefit impact analysis should be conducted before any significant additional compliance obligations are introduced, for example, the further extension of the iXBRL filing requirement. If the result of that cost-benefit analysis is that new obligations are warranted, then resources should be set aside to provide appropriate supports to assist taxpayers such as training on the new requirements. Taxpayers should not be required to purchase new software packages to remain compliant.

To give impetus to a renewed focus on taxpayer compliance costs, we would like to see measurable targets for a reduction in compliance costs included in Revenue's strategy. A 25% target was achieved by Revenue for the period 2008-2012 and a specific target may be appropriate once again.

## 2. Certainty and consistency of treatment

Revenue has a very important role to play in providing taxpayers with as much certainty as possible on their tax affairs. In the Institute's view, there are two important aspects to this role:

- providing "best in class" tax technical support to taxpayers and tax advisers; and
- providing clear and transparent information about Revenue's compliance model.

### *Providing "best in class" tax technical support*

Irish businesses, large and small, are facing difficult trading circumstances for the foreseeable future. International competitiveness is rising and taxpayers and their advisers are working hard to maintain and improve tax compliance rates that are already very high by global standards. These businesses deserve to be at the heart of a Revenue customer service model that aims to provide a standard of technical support which is "best in class" internationally.

To achieve this, we believe that there needs to be an increased focus on the resourcing and delivery of Revenue's tax technical supports, and in particular the current model for the Revenue Technical Service (RTS) needs to be reformed. Businesses need a timely, efficient and responsive technical service to obtain certainty on their tax position when entering into commercial

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<sup>10</sup> PWC/World Bank Paying Taxes Report - 2016

transactions. The current design of the RTS does not allow for direct interaction with a Revenue subject matter expert and this directly impacts on the quality and timeliness of the service provided. Direct interaction between tax advisers and Revenue's tax technical experts is essential in order to resolve complex technical issues efficiently. Such a channel of direct communication would also enhance consistency in responses, and aid collation of responses as part of Revenue's knowledge management procedures.

The tax affairs of larger businesses are particularly complex and this complexity is likely to increase in light of the changing global tax rules and an increased emphasis on transparency. A relaunched Revenue Cooperative Compliance Framework needs to focus on providing an open, responsive engagement platform resourced by dedicated relationship managers who are commercially aware and will liaise with these larger taxpayers and their advisers.

Revenue invests considerable resources in providing published guidance, regular published precedents, website information, and Revenue contact points through technical eBriefs/Tax Briefings etc. The Institute will continue to work closely with Revenue to provide input and feedback on the content and delivery of this important material.

Technology has been transformative in making tax compliance in Ireland easier and less costly for taxpayers as well as for Revenue. The Institute acknowledges the fact that by embracing technology Revenue will be able to reduce administration costs and provide more targeted interventions, but at what cost to the taxpayer. Technology can never replace the need for personal interaction to assist certain taxpayers or to resolve complex tax matters and we would like to see the importance of continued human contact included as a key principle in any strategic goals governing the use of technology by Revenue.

### **3. PAYE Modernisation – the cost impact**

Revenue is currently redesigning the PAYE regime. With effect from January 2019, employers will be required to report PAYE information to Revenue in "real-time" i.e. each time they pay their staff. This is a fundamental change to the current regime, as payroll information is currently reported to Revenue annually (via the P35 process). As such, it will present significant challenges for employers, who will have to incur additional costs in reporting information to Revenue on a more frequent basis.

Revenue has been engaging with stakeholders over the last six months to gain a fuller understanding of the payroll process and the Institute meets regularly with Revenue to discuss the development of the new regime. The members of the Irish Tax Institute interact with the PAYE system daily in their capacities as employers, payroll service providers and tax advisers. As such, they have a broad and unique perspective on its operation which informs our engagement with Revenue.

#### **Key Guiding Principles**

The Institute believes that there are a number of guiding principles in developing the new regime, which we outline below. In formulating our views, we have also reviewed the UK PAYE real-time information (RTI) post implementation review and considered the feedback provided by

businesses in the UK on their experience of RTI. Their feedback provides a useful insight into some of the issues that could arise in an Irish context and some ways in which possible difficulties could be addressed or avoided.

**a. Minimising employer costs**

It is clear from the proposal that there will be significant costs for businesses in migrating to a real-time PAYE reporting regime. These initial costs will include investment in technology, staff training, updating employee data and a revision of payroll procedures. The UK experience is that there are also significant ongoing operational costs with real-time reporting, due to more regular interaction with HMRC and dealing with errors in the processing of payroll information.

The Institute would like to see a full cost/benefit analysis undertaken which addresses the costs and benefits for taxpayers as well as for Revenue in moving to a real-time regime. If the project proceeds after the analysis has been completed, then every effort should be made to minimise additional compliance costs for business and to counterbalance these costs with tangible and measurable benefits such as faster PAYE refunds and fewer errors in tax credits.

*Exemption for micro-businesses*

The increased frequency of PAYE reporting envisaged in Revenue's proposal will create a significant additional administrative burden, particularly for micro-businesses with one or two employees. Many of these micro-businesses have limited or no assistance in dealing with their payroll. Real-time reporting will significantly increase the amount of time that they will need to spend on PAYE administration. A micro-business that currently files returns four times a year under quarterly filing arrangements could be required to file up to 53 returns with Revenue.

In addition, there are many small businesses in rural areas with limited broadband access that will not be able to easily comply with the digital requirements.

Considering these factors, our view is that micro-businesses should be completely excluded from any requirement compelling them to participate in real-time reporting.

**b. Careful on-line design with full agent access**

The main difficulty experienced by employers in implementing RTI in the UK has been dealing with erroneous underpayments of PAYE on HMRC's records. These underpayments have often arisen because of incorrect processing by HMRC of the data submitted to them. This includes the allocation of payments to the wrong period, duplicate employment records arising when employees change jobs or marital status and mismatches between HMRC records and employer records. It would also seem that inadequate IT specifications by HMRC also contributed to the high error rate.

Considerable time and costs have been incurred by HMRC, employers and advisers in rectifying these errors and we believe that the best way to minimise such errors in any Irish regime would be to develop ROS so that:

- Revenue, employers and tax agents can all view the same information contained on the real-time returns
- There is scope to review and amend PAYE data before it is submitted
- There is a mechanism for self-correcting errors. In the current regime, employers have up to 15 February in the following tax year to review and amend their PAYE returns, through the P35
- Employers and tax agents can allocate PAYE payments to the appropriate PAYE periods
- Revenue develops functionality to eliminate the risk of duplicate records. This could include enabling employers to notify Revenue of leavers in advance of their departure or developing system checks to identify duplicate data.

Tax agents play a critical role in the operation of the PAYE regime, both in assisting employers to deduct and return the correct tax due and in completing employee tax returns. This role will become even more important in a real-time environment when there is a shorter period to report to Revenue and when inaccuracies may trigger a Revenue query or intervention. For agents to be able to perform this work in the new regime, they will need full access to a client's PAYE employer/employee online records.

Currently the range of PAYE services accessible to agents is limited. For example, agents cannot access the online Jobs and Pensions system to register a new employment with Revenue nor can they submit a paper-based registration application for an employee. Tax agents do not receive a copy of the employee Balancing Assessment (P21) even though this is an essential piece of information in preparing the employee's tax return.

The Institute would like to see a review and enhancement of PAYE tax agent services undertaken as part of this project.

### **c. Flexibility to cater for differing work and employment patterns**

It is intended that PAYE information will have to be reported to Revenue at the same time as employees are paid. While this may be straightforward where all employees are paid at fixed intervals, it is likely to prove difficult for employers with non-standard pay arrangements, for example:

- Casual workers are often paid at the end of their shift, based on the hours that they have worked
- Employee bonuses earned in a given year are often paid after that year has ended. Currently, these payments are treated as prior year income as required under Section 112, Taxes Consolidation Act 1997 and included in the P35 as an adjustment to the prior year PAYE liability
- Expatriate and international assignee arrangements. Where an employee of a foreign company is working in an Irish entity there may be an Irish PAYE reporting requirement. However, Irish payroll providers are very unlikely to be aware of the payment at the time it is paid and therefore could not report it, at the point

of that payment. This could also occur where an outbound employee may be paid in the host country but remain on the Irish payroll for PRSI purposes. Where an employee is liable to payroll taxes in two jurisdictions simultaneously, a credit can often be claimed for the foreign PAYE liability in “real-time”. Consideration will need to be given as to how this facility will interact with the new regime.

In addition to the difficulties in applying the regime to employments with varied payment patterns, many small employers may find the reporting requirements challenging. Many small businesses do not have the resources to engage full-time payroll assistance and often provide their payroll information to their agents every 8 weeks or more to enable them prepare their payroll records and returns.

The new regime will need to have flexibility in the reporting deadlines to accommodate the practical issues outlined above.

#### **d. A simple and transparent mechanism to deal with disputes**

In the new regime, Revenue will be able to check the accuracy of PAYE returns earlier and on a more frequent basis. This is likely to lead to more queries from Revenue and thus more disputes in relation to PAYE matters. A mechanism needs to be put in place to enable matters to be resolved in a timely and efficient manner.

Currently the main channel to deal with queries on PAYE matters is MyEnquiries. Feedback from our members has been that queries directed through MyEnquiries are not always resolved in a timely manner. We would like to see clear published procedures for dealing with disputed payments and a fast track mechanism put in place to deal with PAYE issues.

#### **e. Phased introduction**

Revenue has consistently applied a phased approach to the implementation of new mandatory filing requirements, such as mandatory electronic filing and iXBRL. This approach should be continued with the introduction of any new PAYE regime. Notwithstanding that software may be able to automate the reporting process, employers will need time to adapt to the new regime and invest in personnel, training and the development of new payroll procedures. Larger businesses may have greater resources to adapt more quickly but they will also have unique challenges, particularly if they operate their own payroll in-house.

Migrating all employers to the new regime at the beginning of 2019 would also coincide with the normal year end requirements for 2018, putting unsustainable pressure on employers, payroll providers and Revenue alike.

It is clear from the UK feedback that small businesses have struggled with their obligations under RTI. HMRC has relaxed the rules for small businesses submitting reports on several occasions since 2013. It has also introduced dedicated supports for small business such as a free Basic PAYE reporting tool. Introducing the Irish regime on a phased basis would ensure that smaller business do not have to implement the regime until it has fully bedded down. This would also provide time for Revenue to identify and

develop the supports that will be needed for small business such as a free PAYE reporting tool, and tailored guidance.

**f. A full pilot programme**

The regime should be piloted for a year in advance of becoming fully operational. This would give both employers and Revenue sufficient time to fully test and develop confidence in its operation. The payroll process is a critical function within any business. Employees need to be able to rely on being paid on a consistent basis without delays and errors arising from incorrect processing of payroll information. Piloting the regime would also assist in identifying any teething issues and ways to streamline the reporting process.

Ideally, the pilot should involve a variety of employers from a broad cross section of businesses to ensure that all aspects of the system are fully tested.

Applying the correct tax deduction is dependent on having the correct data for the employee. It will be necessary for both employers and Revenue to review the quality and completeness of employee data and this exercise would need to be carried out in advance of the pilot.

**g. A well-planned communication and support strategy**

A well-planned strategy for communicating with stakeholders and a package of Revenue supports will be required. Businesses will need time to prepare for the real-time regime including investment in IT, training of staff and the revision of payroll procedures. The communication plan should commence at least one year before the regime becomes operational and could include:

- Written communication from Revenue to every employer in the State about the new regime
- Increased resourcing of the Employer Helpline to deal with employer queries about the preparations required
- Open and ongoing engagement with the profession
- Tailored communications and supports for small businesses as the regime is rolled out to assist them comply with the requirements.

## 4. Interest and penalties – the cost impact

*Extract from the Irish Tax Institute's Finance Bill 2017 Submission*

### Interest on underpaid tax and penalties

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

#### a. 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 overdraft rate, which was 2.4%<sup>11</sup> in 2016. In contrast, HMRC in the UK currently imposes interest at a rate of 2.75%, i.e. 2.5% above the current Bank of England Base Rate of 0.25%.<sup>12</sup> In applying the UK interest penalty regime the rate applied by HMRC is tracked at 2.5% above BoE base rate.

This is an issue that the Institute has raised on a number of occasions in the past but continues to be challenging for taxpayers. It is right and proper that interest should be 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. The Government has been using best endeavours to reduce interest rates charged by commercial banks, in line with rates set by the European Central Bank and we believe the same principles should be applied in this instance.

#### b. Penalties

There are two areas of the penalty code which we believe are disproportionate in their effect, namely penalties for late filing of iXBRL accounts and certain penalties relating to Relevant Contracts Tax (RCT) payments. In both instances, the penalties were introduced as part of major initiatives in recent years to digitise the tax system.

Large corporates who do not qualify for audit exemption are required to file financial statements in iXBRL format within three months of the corporation tax deadline for the tax year concerned. Preparing iXBRL accounts is a difficult and time-consuming process.

The penalty for any later filing of iXBRL accounts is based on the total underlying tax liability, rather than being a fixed charge penalty. If iXBRL accounts are submitted late, a surcharge of 10 percent is imposed on the corporation tax liability, even where a company has filed its corporation tax return and paid its corporation tax liability in full and on time. For example, if a company has a corporation tax liability of €500,000 which it pays on time but files its iXBRL accounts for the accounting period a week after they are due, a surcharge of €50,000 will be imposed.

In our view, the imposition of the 10 percent surcharge on companies that have a strong compliance record for filing corporation tax returns and making tax payments on time is

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<sup>11</sup> National Competitiveness Council Report: Cost of Doing Business in Ireland 2017, June 2017, p. 48

<sup>12</sup> <http://www.bankofengland.co.uk/Pages/home.aspx>

not proportionate to the administrative error made. This is particularly harsh when the taxpayer has filed its tax return and paid the tax liability on time with no loss to Revenue.

In contrast, the penalty in the UK is £200 if the return is filed within 6 months of the deadline. After this date, a tax-geared penalty applies, but it is levied on the tax outstanding, rather than the total tax liability.

When RCT was moved to an online system, a “payment geared” penalty of between 3 and 35 percent, was introduced to apply to certain payments made by principal contractors to sub-contractors in the construction sector. A further penalty of €3,000 can also apply for not following correct RCT procedures. In this case, a penalty regime that is based on the total payments made rather than the RCT liability is also disproportionate.

The matter of proportionality of interest and penalties is particularly important in light of the introduction of the new ‘real-time’ PAYE regime for employers from 1 January 2019 – a transition that will be very challenging for taxpayers.

**Institute Recommendations:**

- 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.
- Penalties for the late filing of iXBRL financial statements and for RCT payment errors, should be fixed penalties rather than tax-geared/payment-geared penalties respectively.
- Consideration should also be given to the proportionality of interest and penalties given the introduction of the new ‘real-time’ PAYE regime for employers from 1 January 2019.





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