

Global Rewards Update: IRELAND

September 2009

COMMISSION ON TAXATION ISSUES RECOMMENDATIONS ON IRISH TAX SYSTEM – PROPOSED CHANGES TO TAXATION OF EQUITY AWARDS

BACKGROUND

In early 2008, for the first time in 20 years, the Irish Government established a Commission on Taxation ("Commission"). The Commission was tasked with reviewing the structure, efficiency and overall appropriateness of the Irish system of taxation. On September 7, 2009, the Commission published its report to the Irish Government, which addresses a wide range of issues in a number of different areas of taxation, including the taxation of equity awards.

The government retains the discretion to accept or reject any of the Commission's recommendations. Those recommendations accepted by the government, whether accepted in 2009 or after, will normally be announced in the Federal Budget in the year of acceptance. All recommendations announced in the Federal Budget will be subject to formal adoption by the Irish Parliament thereafter.

Several of the recommendations discussed below may be accepted by the government as early as this year, and announced in the Federal Budget on December 2, 2009. It is expected that any changes included in the December 2, 2009 Budget, and adopted in Parliament legislation, will be effective from January 1, 2010.

As mentioned, the Commission has recommended several changes to the Irish tax system, and those changes affecting approved and unapproved equity awards are addressed below. Of note, any changes announced in the December 2, 2009 Federal Budget would likely only apply to new

award grants (i.e. those made after January 1, 2010). There has been no guidance to date regarding the effect of these recommendations on currently outstanding awards.

TAXES PAYABLE IN IRELAND

Employees in Ireland are generally subject to the following types of tax on income received. The following are current rates for the 2009 calendar year:

- Income tax – Currently up to 41%
- Income levy – Currently up to 6%
- Pay Related Social Insurance (PRSI) – Currently 4% (up to an earnings ceiling of €75,036)
- Health levy – Currently up to 5%

Employers in Ireland are also subject to the PRSI tax, currently payable at a rate of 10.75%.

Individuals may also be subject to capital gains tax – Currently at a rate of 25%

To help offset some of the new burdens placed on employees and employers, discussed below, the Commission has proposed limited relief in the form of either lower employment tax rates, wider tax brackets, or increased tax credits.

UNAPPROVED PLANS

Current System

Unapproved share plans in Ireland are those plans which have not satisfied Revenue's stated requirements for "approved" plans, and do not benefit from the corresponding preferential tax treatment. While these plans are not considered approved, share-based awards granted under these plans nevertheless currently qualify for an exemption from the two types of employee social tax referenced above: i) PRSI, and ii) the health levy. Employers granting unapproved awards are also exempt from any PRSI contributions with respect to these awards. All awards granted under an unapproved plan are subject to income tax and the income levy, as well as capital gains tax where applicable.

Proposed Changes

The Commission's recommendations with respect to unapproved plans are straightforward, and call for an abolition of the employee and employer social tax exemptions. If approved, the recommendations would result in the imposition of both PRSI and the health levy on an employee's unapproved awards, with a resulting increase of up to 9% in the employee's effective

tax rate (4% PRSI + 5% health levy). In addition, the employer would be subject to a new 10.75% PRSI liability on unapproved awards. In sum, unapproved awards would be subject to income tax, the income levy, PRSI (employee and employer), the health levy, and capital gains tax where applicable.

Currently, employers are generally not required to operate income tax withholding (Pay As You Earn – PAYE) on unapproved share plan benefits, and any income tax due is assessed on the employee's year-end return. If these recommendations are adopted, and employers are obligated to operate PRSI and health levy withholding, it is expected that the Irish Revenue will also require employers to operate income tax withholding on unapproved share benefits. This recommendation could be announced in the December 2, 2009 Federal Budget.

APPROVED PLANS

Current System

Contrary to unapproved plans, approved plans in Ireland comply with specific Revenue mandates regarding plan operation and, for certain plans, award holding periods. Regardless of the type of award granted, approved awards are exempt from income tax, PRSI (employee and employer), the health levy and the income levy. However, approved awards are subject to capital gains tax, where applicable.

Proposed Changes

The Commission has proposed two sets of recommendations with respect to approved share plans:

- Recommendations with respect to all approved share plans other than Save As You Earn (SAYE) and Approved Profit Sharing plans
 - The Commission has recommended that all tax exemptions/reliefs bestowed upon approved plans, other than SAYE and Approved Profit Sharing plans, be abolished. If adopted, this recommendation would effectively eliminate the distinction between approved plans, other than SAYE and Approved Profit Sharing plans, and unapproved plans.
 - All grants of approved awards, other than SAYE and Approved Profit Sharing plan awards, would therefore be subject to income tax, the income levy, PRSI (employee and employer), the health levy, and capital gains tax where applicable.

- Recommendations with respect to SAYE and Approved Profit Sharing plans
 - With respect to SAYE and Approved Profit Sharing plans, the Commission has recommended abolishing the exemption from the income levy, PRSI (employee and employer), and the health levy that these plans enjoy.
 - SAYE and Approved Profit Sharing plans will retain their exemption from income tax.

PRSI EARNINGS CEILING

Currently, employees pay PRSI at a rate of 4%, up to an earnings ceiling of €75,036 for the calendar year ending December 31, 2009. The Commission has recommended removing this earnings cap and, if implemented, the earnings cap is expected to be phased out gradually over a number of years. As such, if this recommendation and the recommendation to apply PRSI to share awards were implemented, a greater amount of share-based income from approved and unapproved awards would be subject to PRSI, until the cap is completely eliminated. This recommendation is also likely to be adopted in the forthcoming Federal Budget.

SAYE PLAN TREATMENT EXTENDED TO ESPP PLANS

As noted above, while the Commission has recommended the imposition of PRSI, the health levy and the income levy on SAYE plan awards, the Commission has also recommended that SAYE plans and Approved Profit Sharing plans retain their exemption from income tax. The Commission has also proposed an extension of the existing rules regarding Revenue approval of SAYE plans to ESPPs. If adopted, ESPPs would be eligible to receive the same tax treatment currently available to SAYE plans, and would thus be exempt from income tax.

CAPITAL GAINS TAX – INDEXATION RELIEF

When calculating capital gains tax in Ireland, employees are able to attribute a certain portion of the gain realized to inflation. The portion of the gain attributable to inflation will be exempt from capital gains tax, though this relief is presently only available for periods of ownership up to December 31, 2002. In calculating the amount of "indexation relief" available, employees multiply the costs incurred to acquire the underlying shares (i.e. their "basis") by a factor set by the government; the factor varies depending on the year the shares were acquired by the employee. Under current legislation, the full gain realized from January 1, 2003 is subject to capital gains tax.

The Commission has recommended that all gains attributable to inflation be excluded from the capital gains tax. If adopted, all employees who hold shares will be able to obtain some level of capital gains tax relief dependent upon when they acquired their awards and the applicable inflation rates announced by the government.

ACTION

- Employers should forecast their future PRSI obligations and consider accruing for this potential new liability.
- Companies granting equity awards should ensure that their internal systems are capable of operating social tax and, possibly, income tax withholding.
- Employers should review their award plan documents and employee communication materials to identify those sections which may require amendment should these recommendations be implemented.

People to Contact

For assistance in this matter or any other issue related to the operation of your global rewards plans, please contact your local Deloitte global rewards consulting services advisor or email us at: globalequity@deloitte.com and a global rewards consultant will contact you.

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