Deloitte.

Commission on Taxation and Welfare - Consultation Response

17th January 2022

17 January 2022

VIA EMAIL: …………………………….

Dear Sirs/Mesdames:

We are pleased to submit comments on behalf of Deloitte in respect of the public consultation for the work of the Commission on Taxation and Welfare.

We appreciate this opportunity to share our views and trust that you will find our comments valuable to the discussion.

We look forward to continued collaboration with the Commission on this and other initiatives, and are available to discuss anything in this document, as needed. In the meantime, if you have any queries, please do not hesitate to contact us at 01-417-2200.

Yours sincerely,

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Chapter 1 - General Questions

1. **What elements of the taxation and welfare systems do you feel are working well? Please elaborate below: -**

- The corporate tax rate of 12.5% has been key to Ireland's development (including the clarity and certainty provided by the Government) and we welcome the fact that it is to be retained in a post OECD Pillar II environment.
- Transparency and consultation with stakeholders and the public generally is key in dealing with implementation of new laws and amending of existing law. Throughout the implementation of the BEPS measures, Ireland has sought feedback from stakeholders and issued roadmaps. This has facilitated a thorough and transparent process and led to implementation of law, which although may be subject to amendment for technical matters has a level of certainty of application.
- Revenue Online Service ("ROS"), MyAccount, MyWelfare, WelfarePartners, MyGovID are all important business and citizen services for taxation and welfare and in our experience are positively regarded. We would suggest that consideration is given to further automation and digitalisation which could lead to significant savings and free up resources to focus on other value - added activities.

2. What elements of the taxation and welfare systems do you feel are not working well?

Please elaborate below:

- Arguably prior Budgets have focused on tax measures to attract FDI, while tax measures associated with small businesses and entrepreneurs have received less attention. While Ireland has a significant number of reliefs etc. aimed at SME's many need to be refreshed and streamlined and should be revisited.
- Our marginal personal tax rate of 52% is one of the highest in the EU. It should also be noted that we have a low entry point for the higher marginal rate to apply. Ireland's high personal tax rate is a disincentive to businesses locating in Ireland, employees taking on additional work and foreign based talent (including Ireland's diaspora) relocating to Ireland. In light of the potential opportunities/risks arising out of OECD Pillar II/Brexit, it is vital that Ireland is well positioned to attract and retain companies. The marginal rate of tax should be reduced from its current level of 52% and the entry point to the higher rate of tax should be significantly increased. At the very least, a roadmap should be put in place to demonstrate to workers when this burden will be reduced. Assessing base broadening measures and entry points to the personal tax system in Ireland should also be considered in an equitable manner over time.
- We would suggest that a feedback and consultation approach similar to that used in respect of Ireland's implementation of EU directives should be extended to all material areas of taxation going forward. We understand that the intention is to continue to engage in consultation on various tax matters e.g. the R&D tax credit regime is due for review in 2022 as is a review of real estate taxation. We welcome consultation on such matters. That said, we outline our views on these measures, and indeed other measures, as part of this document.

3. Good quality public services, welfare provision and infrastructure are financed mainly from taxation and PRSI. What are the features that you think our taxation and welfare systems should have in order to meet these needs?

Please specify:

We would suggest the taxation system should have the following features: -

- Equity - Equity means taxing persons on their ability to pay. A tax system has a role in the redistribution of income. This is achieved by taxing those with higher levels of income at a higher rate than those with lower levels of income.
- A pro-business and pro-growth model designed to attract businesses and help them to grow. This would involve having a competitive tax system which is easy to understand and administer. For example, our

interest deductibility rules together with our double taxation rules are extremely complex and should be reconsidered (See Chapter 6).

- Competitive – We are a small open economy and we need to ensure that we are competitive vis a vis other countries. Again, in reviewing our interest deductibility rules, double taxation rules and personal tax rules, we should be cognisant of the taxation systems of other countries (See Chapter 3 and 6).
- Evidence based approach - Where available, facts and appropriate benchmarks are used to support the status quo or changes to the tax system.
- Simplicity & efficiency of application and administration– A straightforward, clear and rationale tax system where the tax rules are known and that liability is clear.
- Certainty & predictability – Clear commitments to aspects of the tax system with any changes highlighted in advance followed by engagement with stakeholders.
- Sustainable & broad based - The tax system should be designed with a view to eliminating as far as possible volatility of tax receipts.

4. In your view, what main reforms are necessary so that the Irish taxation and welfare systems can embrace the opportunities and meet the challenges that Ireland may face over the next 10-15 years?

Please outline your views:

Ireland has been a major beneficiary of globalisation and one of the principal drivers of that has been our corporate tax regime and the focus on providing taxpayers with clarity and certainty. While there are many reasons other than tax for Ireland's success, we cannot ignore the reality that the 15% minimum tax will to some degree level the playing field with other competitor countries. Accordingly, other areas of the tax system and economy must be adequately served to ensure that Ireland remains a competitive location in which to invest and grow businesses both from the perspective of inward investment and also domestic, indigenous growth.

Ireland should evaluate its role as a headquarter/holding company location for multinational entities (MNE) ensuring that it remains at least competitive with other countries. There are a number of areas in urgent need of reform, in particular: -

- *Interest deductibility rules*
    - Our interest deductibility rules are overly complex. We should reform our interest deductibility rules and introduce a new modern tax system for financing transactions (Discussed further in Chapter 6). In particular, we have brought about the Interest Limitation Rules ("ILR") as required by the EU's Anti-Tax Avoidance Directive ("ATAD") and have layered it over the interest deductibility rules that existed before our enactment of the ILR. It must be recalled that we had viewed our interest rules as "equally effective" to the ILR so in our view it would appear an appropriate time to review the complexity of our pre-existing interest deductibility rules.
    - We should also consider a notional deduction for equity in line with the EU's Debt Equity Bias Reduction Allowance (DEBRA proposal, which to some extent has already been implemented by six EU member states (Belgium, Cyprus, Italy, Malta, Poland, and Portugal). (Discussed further in Chapter 6)
- *Double taxation relief* (Discussed further in Chapter 6)
    - Our current credit/deduction double taxation system contained, inter alia, in TCA97 Sch24 is complex. It has been significantly added to over the years due to decisions of the Court of Justice of the European Union and indeed to deal with certain perceived avoidance issues. Such a regime compares unfavourably to the territorial exemption regimes for dividends and branch income of other EU countries. Moving to a territorial regime would reduce complexity without any significant tax loss (if any) to the exchequer (Coffey Report – June 2017). We are in the process of responding to the Department's specific public consultation on this matter.
    - In respect of other foreign income such as interest, royalties and leasing income, we should replace the existing double taxation relief system with a less complex system. (Discussed further in Chapter 6)

- *R&D* - We should improve our R&D offering. In particular, the list of qualifying scientific fields should recognise emerging technologies such as artificial intelligence, data analytics and carbon neutrality. (Discussed further in Chapter 6)

The 15% minimum tax agreed by the OECD Inclusive Framework may not result in existing MNE's leaving Ireland, but this is a key issue to be monitored going forward. However, a question that does arise is whether Ireland will be an MNE hub for the next new technology and future international investment flows. In addition to our continued efforts in the MNE sector, in order to ensure Ireland's tax base is sustainable, we should build a first class productive and innovative SME sector that is profitable and produces high value jobs. Ireland has in the past introduced new measures and amended existing measures aimed at the SME sector, but such measures have had limited take up, an example of which is the KEEP share option scheme. A strategic review of the taxation system pertaining to SME's should be carried out in order to create a competitive SME tax system.

In particular, our current SME tax system needs to be reformed to not only facilitate start–ups but also to incentivise entrepreneurs to remain and scale up their businesses. The taxation of entrepreneurs in a broad context should be addressed both in the context of personal taxation, taxation of funding/financing returns, as well as capital events. We need to ensure that our SME's have access to capital and talent and that such SME's receive the necessary support to drive research, development and innovation. While taxation is not the only factor in this, taxation can play a part.

Ireland also needs to look at how it taxes labour. In particular, Ireland has high marginal rates and such high marginal rates "kick-in" at relatively low levels of income compared to competitor countries. We need to retain and attract talent to Ireland not only to sustain our income tax base but also our corporate tax base. Notwithstanding Covid19, people are increasingly mobile. One of the factors which will determine where such employees locate is personal tax rates. Further, we need to reduce the marginal rate of income tax and look at base broadening measures over time. It should also be noted that personal tax rates will become a greater differentiator for the location for investment in a post BEPS world.

Ireland should be open to using the tax system to grow the economy, encourage investment in key areas and address societal and environmental requirements. In the current environment, we need a tax system that is competitive in comparison with other countries, and which can attract and retain talent. We also need a tax system that is resilient. In that regard, tax can play an important role in developing the SME sector and ensuring the SME sector can access capital and labour.

Chapter 2 - Fiscal Sustainability

1. What reforms to the taxation and welfare systems should be considered to ensure the system is sustainable and resilient and that there are sufficient resources available to meet the costs of public services in the medium and longer term?

Please specify taxation reforms you consider important:

According to a Department of Finance report in August 2021, in 2020 corporation tax accounted for 20% (€11.8Bn) of the Government's tax take. Of that foreign multinationals accounted for 82 per cent of corporation tax receipts. The top 10 largest MNE's accounted for just over half the corporate tax revenue generated. As can be seen most of the revenues from corporate tax are collected from a small number of companies.

In respect of 2021, corporation tax receipts were €15.3 billion, 22% of tax take in 2021 and up by €3.5Bn (DOF January 2021 press release).

A similar pattern is evident in respect of income tax. In 2020, income tax accounted for c.40% of the overall tax take. Despite Covid19, and a dramatic fall in employment in 2020, income tax receipts remained resilient. This was due to the fact that most of Ireland's income tax is collected from a small number of tax payers with many low earners completely outside the income tax net. According to the OECD, Ireland has one of the most progressive income tax systems in the developed world. While the progressivity of income tax may be a positive from an equity perspective, it does result in a narrowing of the income tax base. For example, in 2018, the latest year for which data such date is

available, around four-fifths of all income tax revenue was paid by the top 25 per cent of income earners; additionally, the top 1 per cent of earners paid over one-fifth of income tax.

The over reliance on certain tax receipts and Ireland's narrow tax base is a risk to meeting the State's commitments. This is particular concern at the moment as the Department of Finance has estimated that international tax reforms could reduce Ireland's corporation tax base by up to €2 billion. A reduction in inward investment could also impact the amount of income taxes collected. Broadening the tax base and developing the Irish SME sector will be essential to ensure Ireland remains resilient against economic shocks.

2. Rate each issue below in terms of strategic importance to the taxation and welfare system over the next 10-15 years (1 being least important and 5 being most important):

Rate each issue below in terms of strategic importance to the taxation and welfare system over the next 10-15 years (1 being least important and 5 being most important):

	1	2	3	4	5
Achieving good public health outcomes for our people					
Addressing the climate crisis					
Adequate social transfers and benefits					
Growing employment					
Sustainability of public finances					
Sustained economic growth					

3. Given approaching demographic pressures and future uncertainties, future funding of public services is a critical issue. In order to meet these challenges, what is the appropriate balance between the taxation of a) earned income, b) consumption e.g. VAT and c) wealth e.g. capital acquisitions tax?

Please outline your views:

In our view, key to ensuring sustainable funding for public services is economic growth. Increased taxes on profits and labour will damage economic growth and have a detrimental impact on the amount of taxes collected. Further to that, we need to retain the 12.5% corporate tax rate (and 15% rate where relevant) and improve our tax offering for MNE's and SME's. In addition, personal tax rates need to be reduced and the entry point to the higher marginal rate needs to be increased. In our view the taxation of wealth (e.g. Capital Gains Tax) and consumption are already at high rates compared with OECD countries and therefore, the balance should be maintained and that may mean reducing rates in order to maintain or increase yield.

Chapter 3 - Promoting Employment

1. What reforms to the taxation and welfare system should be considered to ensure that taxation and welfare work in tandem to support economic activity and promote employment while also supporting those most vulnerable in an equitable way?

Please outline what reforms should be considered:

Ireland's high personal tax rate is a disincentive to businesses locating in Ireland and employees taking on additional work. It is also a disincentive to foreign based talent (including Ireland's diaspora) relocating to Ireland. In light of the potential opportunities/risks arising out of OECD Pillar II/Brexit, we need to ensure that the personal tax system isn't a barrier to attracting and retaining talent in Ireland. This will be critical in terms of driving economic activity, future

investment and reinvestment, and supporting SMEs and entrepreneurs to grow and scale their businesses in and from Ireland. Our marginal rate of 52% is one of the highest in the EU and puts us at a competitive disadvantage compared to other countries competing for inward investment. It should also be noted that we have a low entry point for the higher marginal rate to apply. The marginal rate of tax should be reduced from its current level of 52% and the entry point to the higher rate of tax should be significantly increased. At the very least, a roadmap should be put in place to demonstrate to workers when this burden will be reduced. Assessing base broadening measures and entry points to the personal tax system in Ireland should also be considered in an equitable way over time.

Another area that could be reformed is the Special Assignee Relief Programme ("SARP"). SARP is an initiative aimed at encouraging skilled personnel to relocate to Ireland by granting an exemption from income tax for 30% of earnings between a €75,000 and €1m. However, as discussed further below, in order to be competitive, the Irish SARP needs to be modified.

Also, as discussed below, our remote working incentives and foreign earnings deduction ("FED") needs also to be improved.

There should be a focus on welfare to measures which act as a disincentive to people taking up employment. Despite various supports put in place, there are still situations where individuals are either less well off (or only very marginally better off) working, than they would be on a social welfare. Particular difficulties arise in relation to the interaction of some social welfare payments/benefits with employment. These include the Housing Assistance Payment ("HAP"), the medical card and the interaction of jobseekers payments and the number of days worked. As such, some people state that they are not in a position to increase hours on the minimum wage because of the knock - on impacts on their social welfare. Steps should be taken to eliminate these issues to ensure that people taking up employment are suitably better off.

SARP

There has been an evolution of the tax landscape over the last number of years with the OECD work on the Base Erosion and Profit Shifting (BEPS) project. A key feature of the project was an alignment of the taxation of profits to the location where activities are undertaken i.e. where substance is located. A critical element of substance for companies, in terms of activities, is the location of key executives. The attractiveness of a location from a personal taxation perspective is a factor in determining where a corporate group locates.

A tax policy that is competitive and effective in attracting top mobile talent to Ireland is vital to Ireland's position in retaining and attracting Foreign Direct Investment (FDI). Multinational clients repeatedly tell us that Ireland's 52% tax rate (income tax, USC and PRSI) is the biggest barrier that they face when trying to get senior employees to relocate to Ireland. Ireland has the eleventh highest personal tax rate of 38 OECD countries, being seventh highest in Europe. Additionally, the marginal rate applies at a much lower income level here than in most other OECD. These high tax rates make it difficult for companies to attract skilled workers to Ireland. For example, in California, which would have one of the highest state taxes in the US, an individual would need to earn $551,473 to reach the marginal tax rate of 49.3%. In Ireland, a 48.5% rate applies on earnings over €35,300 and the 52% rate applies on earnings over €70,044.

The INSEAD Global Talent Competitiveness Index (GTCI) Report for 2013 stated, "*The war for talent between organisations has been much researched and written about, but today, we see countries, not just companies engaged in this competition.*" This competition has continued through to today and become even more focused in the context of Covid and global skills shortages as regards companies seeking European bases and people within those locations. The 2019 GTCI Report ranks countries in terms of their competitiveness in attracting talent. The table below compares some of Ireland's competitor locations.

Country/city	European Ranking	Global Ranking
Switzerland	1	1
Singapore	N/A	2
Netherlands	6	8
UK	7	9
Luxembourg	8	10
Ireland	11	16
Hong Kong	N/A	27
Dublin	18	35

The report states, "*Attracting talent, in the context of national competitiveness, should be viewed in terms of luring foreign valuable resources, both productive businesses (through foreign direct investment and the like) and creative people (through high-skilled migration)."* It is clear from the rankings in the report that Ireland needs to enhance its ability to attract these highly skilled workers.

SARP is an important measure in this context and a necessity to ensure that we can work towards enhancing our ability to attract highly skilled mobile workers. Some of the restrictions within the existing relief should, in our view, be removed to provide a simpler more effective regime. We believe that an enhanced Irish regime should contain the following features: -

- The relief should be available in respect of USC and, where relevant PRSI, rather than being limited to income tax. Extending SARP to USC and PRSI would allow for a lower effective tax rate for the employee making the relief more competitive with regimes in other jurisdictions. This could reduce costs for employers by allowing a lower gross pay due to the lower effective tax rate payable. If SARP applied for employer PRSI purposes, this would further reduce costs for employers allowing for greater investment in the business.
- The base level income required should be aligned to the requirements for a Critical Skills Permit to seek to assist companies in attracting talent in the areas with the greatest skills shortages. SARP provides an exemption from income tax for 30% of employment income above a base salary level of €75,000. For those who commenced employment in Ireland in 2019 the relief is 30% of employment income between €75,000 and €1,000,000. This €1 million ceiling on income applies to all claimants for claims from 1 January 2020. In our view, the lower limit of €75,000 should be reduced and realigned to the limits applicable for Critical Skills Permits, which in some cases are lower than €75,000. The relief could therefore be twofold: -
  -attracting talent with specific skills required for the economy, and
  -attracting key decision makers.
  This two-prong approach would help to drive growth within the economy by filling skills shortages and growing companies situated in Ireland.
- The €1 million earnings cap that was introduced in Finance Act 2018 should be removed. Its introduction appears to have been motivated by the increased number of applicants and by the perceived cost. SARP will be important in retaining MNE's in Ireland and attracting MNE's to Ireland (with the resulting corporate tax effect).
- Similar to other jurisdictions, the relief should be available to new hires as well as existing employees assigned or transferred to Ireland. In the current climate, companies are finding it difficult to source suitably skilled employees and they cannot compete with other countries with lower tax rates or expatriate reliefs. In the 2014 review of SARP the observation regarding extending SARP to new hires, was that this could cause job displacement in the Irish labour market. In our view, this could be addressed by limiting access to the relief by new hires to specific areas in line with the requirements for a Critical Skills Permit. The relief could be available to new hires who, if they were required to hold a permit, would satisfy the conditions for a Critical Skills Permit. This would ensure that it was only available for those working in areas where a critical shortage in Ireland has been identified.
- The relief should be available to employees of all employers, i.e. not just employees of companies in Treaty or Tax Information Exchange Agreement ("TIEA") States.
- Non-residents should be able to claim the relief against the portion of earnings that is taxable in Ireland. This is the position in the Netherlands under the Dutch 30% regime.
- The requirement for approval in advance of claiming on a tax return should be removed to simplify the claim process.
- The 5-year period that a claimant needs to be non-resident should be reduced to 3 years

- The relief should be available for 10 years rather than 5 years to set Ireland apart in terms of competitiveness from a personal tax perspective. Existing claimants should be able to qualify for the relief for the extended period.
- The improvement in the SARP should also be combined with a roadmap to reduce high earner effective personal tax rates.
- In addition, the current relief is due to expire on the 31 December 2022. The inclusion of a sunset date for the relief is a negative in the context of companies seeking to attract people to Ireland or relocate business operations to Ireland on an ongoing basis. It is critically important that a decision on the extension of SARP beyond 2022 be made at the earliest opportunity. In our view, the relief should make it a fixed part of the tax code, i.e. remove the sunset provision entirely.

The above changes would greatly enhance our position as a key location for inward investment and as a location for highly skilled workers. Enhancing SARP would make it more attractive for these companies to locate and retain operations in Ireland.

There are a number of countries which have reliefs or incentives similar to SARP or tax regimes that compete with SARP. While we feel that Ireland's regime should be best in class in its own right and not necessarily shaped by what other countries do, the following should be kept in mind: -

Country	Comments on regime
France	Pay for coming to France and for duties outside France relieved from tax
	Up to 50% of income can be exempt
	Available for 5 years
	Applies to new hires
	Not French resident in the previous 5 years
Hong Kong	Only duties in Hong Kong taxed
	Maximum 15% tax rate
	No time limit
	Applies to new hires
	No residence conditions
Italy	Up to 70% deduction, i.e. 30% taxed
	Can be increased to 90% deduction, i.e. 10% taxed where the individual relocates to certain southern regions
	Usually lasts 5 years but can be 10 years where the individual relocates to certain southern regions
	Not Italian resident in the previous 2 years
	Applies to new hires
Luxembourg	Expat BIKs and allowances exempt
	Available for 5 years
	Not resident in or within a 150km radius of Luxembourg in the previous 5 years
	Applies to new hires
Netherlands	30% of earnings exempt
	Available for 5 years
	Not resident in or within a 150km radius of the Netherlands for at least 16 months of the prior 24 months
	No residence conditions, i.e. available to non - residents who are taxed on the earnings referable to Dutch duties
Singapore	Only duties in Singapore taxed
	Maximum 22% tax rate
	No time limit
	Applies to new hires
	No residence conditions

Foreign Earnings Deduction ("FED")

FED plays an important role in encouraging and incentivising Irish businesses to export to emerging markets. However, there are ways the relief could be enhanced to improve its appeal. We believe that FED should be enhanced as follows.

- Apply to all countries

Global Ireland 2025 sets out an ambitious strategy to double the scope and impact of Ireland's global footprint. It is clear from the report that this involves a range of measures focused across the globe and not just in emerging markets. Leo Varadkar stated, *"The EU has always offered the promise of a better future, but it is a future that will not be handed to us. We must work to create it*." It is clear that our aim is to continue to be an active and engaged member state of the EU. In the context of Brexit, we are focusing on new markets both in the EU and beyond and it is key that companies do not solely focus on emerging markets. The report states "...*diversifying beyond the UK market is an important aspect of the national effort to mitigate the negative impacts of Brexit. Further reinforcing our presence in Europe will support this drive, enabling us to better capture and exploit new market opportunities*."

When initially introduced in 2012 the Minister stated, "*I am ... introducing a Foreign Earnings Deduction to further support our export drive by aiding companies seeking to expand into emerging markets.*" The relief was extended to additional countries in 2013 and further locations were added in 2015 and 2017. It is clear from Global Ireland 2025 that there is a global focus not limited to specific regions or countries. The FED should be extended to all countries to align with this policy, so as to assist Irish companies looking to expand their exports.

This is particularly important in the context of businesses seeking alternative markets to the UK given Brexit.

- Extend the annual maximum relief to €100,000

The relief is currently capped at €35,000 equating to a maximum tax saving of €14,000 as the relief is only allowed for income tax. This is quite limited in the context of the extent of travel that an individual may have in a tax year. Employers incur significant costs in relation to travel and subsistence for employees that they need to send overseas and, in many cases, may need to offer an incentive for employees to undertake the development work due to the personal commitment required. Increasing the cap to €100,000 would allow companies to reduce their costs as the FED would be the incentive for employees. Companies could redirect any savings to increased investment in the drive for overseas exports resulting in increased growth and exchequer returns.

The above would make the relief sufficiently attractive to encourage greater travel to develop foreign markets while reducing cost for companies

- Again, the sunset provision should be removed, with this relief to be a permanent feature of Ireland's tax code.
- The relief should be extended to USC and PRSI.
- The alternative is for a territorial approach to be taken akin to that in Hong Kong and Singapore where tax/USC/PRSI would only be applied to earnings referable to duties exercised in Ireland.

Remote Working Tax Relief

Finance Act 2021 provides for income tax relief for remote working allowing employees who work from home to claim 30% of the cost of broadband, electricity and heating, apportioned based on the number of days worked from home during the year. The relief is reduced by any amount reimbursed to the worker by their employer. Also, where the relevant expenses are shared by two or more people, the total costs are apportioned between the individuals based on the amount of the expense paid by each person.

The increase to this relief is welcome, but in practice the tax relief due to most individuals will be minimal. For example, someone who works at home 50% of the time with circa €5,000 a year in expenses, will only benefit by around €175.

There are many benefits of working from home including environmental benefits, reduced stresses on infrastructure and improved quality of life. Remote working may also go some way in rejuvenating rural communities. Further to an

existing relief, we would recommend a €1,000 tax credit which may be reduced pro-rata depending in the number of days an individual spends in the office.

Share based rewards

There are also opportunities to approve the system pertaining to share based awards. We have included comments in Chapter 6 in respect of same.

2. Does Ireland's taxation and welfare system strike the right balance between maintaining the incentive to increase earnings and alleviating some of the risks of low income (poverty and deprivation)?

Yes No

Please explain your view:

See response to Chapter 3, Question 1.

3. Are income supports equitable in terms of how they treat people of working age?

Yes No

How is this balanced with the requirement to meet differing needs?

We have no comments in this regard.

4. What changes to the social insurance system should be considered to ensure sustainability into the medium to longer term? (Please note the recommendations of the Pensions Commission and NESC Report 151 on the future of the Irish social welfare system)

We have no comments in this regard.

Chapter 4 - Climate

1. As Ireland moves to a low carbon economy, what should be the role of the taxation and welfare system in:

a) taking advantage of opportunities?

Ireland's geographical position is conducive to the production of renewable electricity from sources such as onshore wind, offshore wind, solar and wave / tidal. This not only gives Ireland an opportunity to be self-sufficient in energy terms but also creates opportunity for export. Having surplus energy, also creates other opportunities such as the production of renewable fuels such as green hydrogen.

It has been estimated by the IMF, that Ireland will need to invest €20 billion annually (or 5% of GDP) for the next ten years in climate-related infrastructures and mitigation measures to achieve its targeted emissions reduction. Creating surplus green energy which can be exported or used to produce other renewable fuels could be significant in offsetting the cost of that investment.

Further to that, it is important that the investment in green infrastructure and technology is stimulated and also that the associated tax rules are certain and clear. We have identified a number of tax measures which would support the renewable energy sector.

- Relief for investment in renewable energy generation

S.486B TCA 97 provided corporate tax relief for equity investment in companies involved in renewable energy generation. This relief was introduced in Finance Act 1998 but was withdrawn in 2014. Key features of the relief were as follows: -

- The relief was given in the form of a deduction from a company's profits for its direct investment in new ordinary shares in a qualifying renewable energy company.

- To have qualified for this relief, the energy project must have been in the solar, wind, hydro or biomass technology categories, and must have been approved by the Minister for Communications, Energy and Natural Resources.
- The relief was capped at the lesser of 50% of all capital expenditure (excluding lands), net of grants or €9,525,000 for a single project.
- Aggregate annual investment by a company or group was capped at €12,700,000.
- The corporate investor needed to hold the shares for 5 years in order to avoid a clawback of the relief.

As mentioned, this relief was withdrawn in 2014. We would recommend that consideration should be given to the re–introducing this relief. This relief would encourage corporate shareholders to invest in renewable energy projects. It should be noted that the relief became less attractive to investors when the corporate tax rate became 12.5% in 2003. Consideration could be given to allowing the relief to be used to shelter income or gains taxed at the higher rates of 25% and 33%.

- <u>Extension of the participation exemption to early - stage renewable energy projects</u>

In many cases, in order to progress a renewable energy project, it will be necessary for the original promoters to sell all or part of the project at an early stage (to facilitate the introduction of capital and development expertise). In particular, this could involve the promoter selling the shares in the project company. In certain instances, the sale of shares by an Irish holding company would not be subject to Capital Gains Tax, due to the availability of an exemption known as the participation exemption in TCA97 s626B. However, the sale of shares in a project company hosting an early-stage renewable project may not be in a position to claim the participation exemption as in the Revenue's view the company may not be considered trading (broadly, that the project company should be trading is one of the conditions required for the participation exemption to apply). Revenue practice is to view trading as commencing when the project company commences producing electricity.

Thus, a gain received by a holding company on the disposal of shares in a subsidiary company hosting an early-stage development project may be subject to tax at the rate of 33%. We would suggest that the participation exemption should be extended to the sale of companies that host early-stage development projects (in line with, for example, the UK broader approach). Such an exemption would increase the level of funds available to promoters to develop further new projects.

- <u>Pre-trading expenses</u>

In broad terms, an expense is only allowable if such expense is wholly and exclusively laid out or expended for the purposes of the trade. In the Revenue's view, a renewable energy trade will only commence once the company starts producing electricity. As such, any expenses incurred prior to the commencement of trading would not be deductible under first principles. There is however, a provision that allows deductions for pre–trading expenditure. This provision allows a deduction for certain expenditure incurred in the 3 years prior to the commencement of trade.

Renewable energy projects by their nature take several years from the point of initial investment, until the point the project starts to generate electricity and therefore commences trading. In many cases, this pre-trading period is in excess of 3 years. The costs in this pre–trading period can be significant. As a result, a taxpayer may lose out on tax relief for expenditure incurred outside the 3-year window. We would recommend that the rules are updated to ensure that all vouched pre–trading expenditure is deductible or at the very least expenditure in a 7-year window are deductible (in line with the 7 - year lookback period in the UK).

- <u>Grid connection costs</u>

Normally, in calculating taxable income, a deduction is only allowed for expenditure of a revenue nature (e.g. cost of sales type expenditure). A deduction is not available under general principles for capital expenditure e.g. broadly expenditure that endures for a number of years (e.g. buildings, plant and machinery, wind turbines, solar panels). However, capital allowances are available for capital expenditure. Under the capital allowances regime, broadly, a deduction is allowed for capital expenditure on plant and machinery on a straight-line basis over 8 years. One of the conditions of the capital allowances regime is that the taxpayer owns the asset.

While grid connections costs (costs incurred by the renewable energy company in establishing a connection between the electricity producing assets (i.e. wind turbines, solar cells) and the national transmission grid.) are considered capital expenditure, Revenue have in the past taken the position that no capital allowances were available for such expenditure. As a result, a taxpayer receives no relief for such costs, which in most cases are significant.

A recent Tax Appeals Commissioner (94TACD2021) case concluded that relief should be available for grid connection costs. We would ask that the position be clarified so that a developer gets relief for such expenditure. Such clarification would have a significant impact on the overall cost of a renewable energy project. It should be noted that the capital allowances regime in the UK provide relief for grid connection costs.

- VAT

Section 56 of the Value-Added Tax Consolidation Act 2010 provides for a supplier to zero rate the supply of qualifying goods and services to certain authorised persons. It also provides that those authorised persons can apply the zero rate of tax to the acquisition of goods and services received from other Member states, where obliged to account for VAT on the receipt of those supplies, and on the importation of goods from outside the European Union. Broadly, the persons who qualify (i.e. the authorised person mentioned above) are those primarily engaged in exporting more than 90% of their goods. (typically MNE's) In general, there should be no loss to the exchequer associated with this scheme as any VAT suffered would generally be recovered. However, where the scheme applies to the taxpayer, it avoids the cash flow impact of suffering VAT (i.e. when the invoice is paid) and subsequently reclaiming VAT. (i.e. any refund could take a number of months after the payment of VAT to the supplier).

A similar cash flow impact arises for a renewable energy project. As the outlay in expenditure can be significant and with refunds only due a number of months later, the this can create a significant cash flow burden.

We would recommend that a scheme similar to S.56 is introduced for renewable energy projects which provides for a zero rating of inputs until the project is operational (i.e. generating revenues). This would ease the cash flow burden on renewable energy developers. Alternatively, allowing renewable energy companies, the option of making monthly rather than bi–monthly VAT returns may help to alleviate some of the cash flow burden. (It is currently possible to file monthly VAT returns if the taxpayer is in a constant repayment position, however confirmation that this can apply to companies up to the point of operating their renewable energy business would be beneficial to the sector).

- Relevant Contracts Tax ("RCT")

Broadly, with certain exceptions, a developer of renewable energy infrastructure in receipt of services from contractors must deduct from payments to the contractors a withholding tax ("WHT") known as RCT. There are currently three RCT rates (35%, 20% and 0%) which may apply based on the contractor's RCT status. Following deduction of RCT, the contractors will then receive the net payment and should be in a position to recover the RCT deducted directly from the Irish taxation authorities or offset such RCT against other tax liabilities. One of the purposes of the RCT regime is to increase tax compliance in the contractor industry.

There is an exemption from the RCT provisions for persons carrying out building or development work where the payments being made relate to work on land or buildings which will be used or occupied by the person or their employees and the person is not otherwise considered a Principal Contractor. ("the own use exemption").

In practice, new companies will be subject to 35% WHT for up to 3 years. Once the company has established that it is tax compliant the WHT rate may reduce to 20% or 0%. However, in the early years a 35% WHT will create a significant cash flow cost for contractors. Also, it is not uncommon for contracts to include a gross up clause for withholding taxes thus increasing the business cost to the developer.

Consideration should be given to ways that would extend the 0% rate of WHT to companies backed by promoters with appropriate tax compliance records. Alternatively, consideration should be given to extending the "own use" exemption" to renewable energy development companies.

- <u>Decommissioning / rehabilitation costs</u>

S.681 TCA 1997 provides for a deduction for rehabilitation / decommissioning costs for mines. We would recommend that a similar type of relief be made available for renewable projects such that tax relief is available for decommissioning / rehabilitation costs.

- <u>Research and Development</u>

As Ireland expands its onshore wind, offshore wind (both fixed and floating), solar and biofuel industries, there is likely to be significant investment in research, development and innovation. With the proper incentives, Ireland could become an innovation hub' for renewable energy. We need to review our R&D regime to ensure that it is first in class. (See Chapter 6)

- <u>Solar Investment Vehicle</u>

It is estimated that Ireland will need to invest €20 billion annually (or 5% of GDP) for the next ten years in climate-related infrastructures and mitigation measures to achieve its targeted emissions reduction. Where will this level of capital investment come from? Is it expected that such investment will fall to the government or the private sector? If the private sector is to play a role in this targeted emissions reduction then we believe it is important that adequate incentives, not just through RESS type auctions, are used to facilitate the deployment of private capital.

According to EirGrid figures, renewable energy comprised almost solely of wind assets, accounted for c. 36.3% of Ireland's electricity generation in 2020. However, only 1% of the generation in the same year was made up of solar energy. As such there is a major potential for solar energy to aid in achieving Ireland's targets in the short-term. Solar farms have usually received a very positive reception from both the public and local authorities due to the low visual and acoustic impact of the infrastructure.

The under-investment in solar is due in part to the high costs of developing and operating solar projects in Ireland (including ongoing taxation) and, in particular, exceptionally high and uncertain grid connection costs, making the price of electricity required by such projects to generate a return on investment uncompetitive in the market. Pricing for CPPAs around Europe are below wholesale prices which can be achieved with low grid costs and low operational expenditure. In Ireland however given regulation costs that accompany infrastructure (such as electricity planning standards), business rates and grid connection fees it is difficult to achieve such low CPPA pricing to stimulate that sub-economy. Note a CPPA is a long-term contract where the end user business (rather than a licensed electricity supplier) agrees to purchase electricity directly from a renewable generator at an agreed price for a fixed term.

At a macro level, the inability of solar energy providers to ensure a competitive return on investment as a result of the relatively high costs of solar assets in Ireland (due to the various factors outlined above) will ultimately limit the amount of solar energy developments which can take place in Ireland (outside those subsidised through the RESS process) and will therefore, in turn, impact on Ireland's ability to meet its renewable energy targets. As such, a solar energy fund tax regime could be introduced to encourage investment in solar energy and to reduce the cost barriers to entry.

This specific tax incentive regime would aid in reducing the costs of producing the electricity and therefore make solar projects more viable to compete with wholesale electricity prices. This in turn should result in increased investment. Other key aspects of a solar investment vehicle include: -

(1) Exempt vehicles, such as exempt plcs, allow access to a wider investor group with potentially reduced demand for high returns. Although there are other exempt investment vehicles we believe that such vehicles do not support access to a wider investor pool as such investors are limited in terms of minimum investment and qualifying criteria and it will be important that both for the solar energy operator and society in general (as a means of environmental investment) investment is accessible widely.

(2) Current tax law does little in the way of incentivising investment in solar energy. While the Carbon Tax will likely impact and dissuade investors to invest in industries with high carbon emissions, it does little to incentivise them to look at solar energy investments. By providing an exempt regime to solar energy projects, be that for vehicles investing in or developing solar energy projects or mortgage type vehicles that finance such projects (both of which

are already evident in the US), the Government will be providing the incentive for investors to move their capital into the industry whilst allowing the vehicles themselves to service the investment in as tax-efficient manner as possible.

(3) As a result of current tax rules Ireland will suffer financial and economic losses due to the opportunity cost of failing to maximise renewable energy development opportunities and by failing to meet its 2030 renewable energy targets. Each nation within the European Union must enact policy which enables the transition to a low carbon economy including targets for lowering emissions. If such targets are not met, then such nations will incur fines and penalties. Ireland paid €63m in statistical transfers in 2020 despite the downturn in the economy and faces compliance costs of up to €1.8Bn cumulative between 2020 -2030 if actions are not implemented to curb greenhouse gases. Clearly, incurring such high fines and penalties when that capital can be deployed elsewhere in the economy, particularly in incentivising investment in renewables is impractical. Thus we are suggesting a redeployment of these costs in establishing a solar investment vehicle

(4) Sustainability: The wide scale implementation of solar energy projects will have a positive wider impact on rural Ireland. In addition to helping Ireland fulfil its solar energy ambitions, including those relating to CO2 emissions, the solar energy industry has the potential to make an important contribution to Ireland's growth agenda and the diversification of industry in rural Ireland. The accelerated deployment of solar energy will generate jobs, particularly in the construction and installation sectors but also more broadly in professional services across consultancy, finance and asset management. A larger domestic market will enhance Ireland's offering as a location for firms in the solar energy supply chain, which could bring further jobs and investment in high-tech, exporting industries. Creating an industry for the development, operation and management of renewable energy projects particularly solar farms could make Ireland a leading competitor for such services. Also, an increase in activities and renewable energy projects in rural areas will increase the rates received by the local authority and will allow the community to prosper more generally through the update of local infrastructure and facilities.

(5) Whilst recognising the need to create the required market signal for renewables investment, we are conscious that an open ended tax exempt vehicle may not be the preferred policy going forward, particularly when the renewables sector has reached the required scale to meet targets and indeed reduce our reliance on carbon driven electricity generation. Therefore, we would suggest that certain criteria are included to give a manner of certainty on the potential benefits economically and in time provide a natural source of tax revenues to supplement, or replace, what might be a diminishing carbon tax yield as and when Ireland reduces its reliance on fossil fuels. Additionally, a change in current tax law is likely to have a net positive effect on tax revenues. We are of the view that the tax revenues from the solar energy industry will not increase significantly in the future due to the lack of investment. Thus, there should be little potential opportunity cost of implementing an exempt regime for the solar energy industry. In fact, where we see the potential for increased revenues is from the increase in construction services provided in Ireland in the construction of the solar energy assets as in most instances this will be undertaken by third party contractors but more significantly we see the increased rental payments under lease arrangements as providing a positive effect on tax revenues. Further, as with the provisions for other exempt plc's, distributions are mandated for the plc exemption to apply. Therefore, a level of annual taxation will still occur, albeit at the shareholder level.

Proposed Legislation

In order to achieve the objective of incentivising investment in solar energy projects, we would recommend enactment of new legislation. This would create an exempt renewable energy vehicle for the sole purpose of generating income from the financing, development or operation of solar energy assets in the State. We would propose qualifying conditions as follows could apply:

During the accounting period in which the company or group elects to be an exempt renewable energy vehicle it must –

1. be resident in the State and not in another territory;

2. be incorporated under the Companies Acts;

3. have its shares listed on the main market of a recognised stock exchange in a Member State

4. not be a close company within the meaning of Chapter 1 of Part 13 TCA 1997;

5. it must derive at least [70%] of its aggregate income from sources outside the RESS regime – e.g. through merchant trading or corporate PPAs;

6. it must maintain an appropriate profit to financing costs ratio which reflects the market from time-to-time;

7. it must ensure that the aggregate of the specified debt does not exceed 50% of the aggregate market value of the business assets of the renewable energy vehicle and

8. it must have a diversified share ownership and distribute at least 85% of its solar energy income annually on or before the specified date of return date for the accounting period in relation to the renewable energy vehicles.

Solar energy business could be defined as follows, along with ancillary definitions:

"solar energy business" means a business which is carried on by the renewable energy vehicles or the sole purpose of generating income from the financing, development or operation of solar energy assets in the State,

"solar energy assets" means land and accompanying infrastructure, including onsite energy storage, relating to Solar energy.

"solar energy income" means all profits (including chargeable gains) of the solar energy business, as].

The exemption may be drafted as follows:

"Notwithstanding anything in the Acts, but subject to the provisions of this Part, a company which is a renewable energy vehicle shall not be chargeable to tax in respect of solar energy income"

b) mitigating the risks?

c) in meeting Ireland's emissions targets?

Questions (b) and (c) are addressed as follows: -

In July 2021, the Climate Action and Low Carbon Development (Amendment) Act 2021 ("the Act") was signed into law amending the Climate Action and Low Carbon Development Act 2015 (the principal act). The 2021 Act requires the Government to "pursue and achieve the transition to a climate resilient and climate-neutral economy by the end of 2050". In particular, the Act amends the principal act and provides a framework to reduce green-house gases ("GHGs") including an objective of climate neutrality by 2050 and an interim target of a 51% reduction in GHG emissions by 2030, relative to a baseline of 2018. This is an extremely ambitious target and Ireland will face many challenges if it is to meet its environmental commitments. One of the key levers available to the Government is tax policy which can be used to influence behavioural change throughout business and society. In particular, these policy matters could include: -

- Tax exemptions for both companies and individuals in respect of certain types of capital gains and income/benefits. (See Chapter 4 (a) above)
- Tax relief for investors investing in particular types of investments - For example, the Employment Investment Incentive Scheme ("EIIS") allows investors to deduct the cost of their investment from income, therefore reducing their income tax liability.
- Accelerated capital allowances. In general, a taxpayer claims a deduction in respect of expenditure on plant and machinery over a period of 8 years. An accelerated capital allowance allows the taxpayer to take a deduction for all of the expenditure in the year such expenditure is laid out.
- Super deductions. For example, a corporate taxpayer that incurs capital expenditure on energy efficient plant and machinery assets worth say €10m would be able to get a tax deduction of €13m. This would amount to a tax saving of €375k for the taxpayer ((€13m - €10m) @ 12.5%).
- Relaxation of restrictions on particular types of deductions. For example, Finance Act 2021 introduced a restriction in respect of interest deductible. Broadly, only interest less than 30% of EBITDA would be deductible. However, interest on borrowings to finance renewable energy infrastructure was excluded from these interest restriction rules
- Reductions or increases in: -
    - VAT rates

  - Excise Duty including VRT and Carbon Taxes and
  - Motor Tax
- Tax credits - For example, under the R&D credit regime, a taxpayer investing in R&D can obtain a deduction against turnover in arriving at taxable profits. Such profits are then taxed at 12.5%. But the taxpayer also provides a credit equal to 25% of the expenditure. This credit is deducted from the aforementioned tax liability.

In this regard, we have set out below some suggestions.

Incentivise green spending

We would recommend that spending on green low consumption technology and buildings with recognised accreditation should be incentivised by way of super deductions or accelerated capital allowances. For example: -

- 'Super deduction' of up to 150% of capital expenditure incurred (depending on the type of expenditure) or/and
- Accelerated capital allowances.

Such reliefs could apply for the purposes of: -

- Developing new buildings/factories that receive a recognised accreditation for overall energy performance
- Retrofitting existing commercial buildings
- Expenditure on plant and machinery that receive a recognised accreditation for overall energy performance
- Expenditure on IT equipment for remote working
- Expenditure on commercial hybrid and electrical vehicles ("EV's") to encourage companies to electrify their fleet
- Expenditure on charging stations for electric vehicles

Transport

- Encourage wider adoption of electric/hybrid vehicles via: -

  - Tax incentives for hybrid/electric vehicles such as super deductions and accelerated capital allowances
  - Lower rates of VRT on electric/hybrid vehicles
  - Lower rates of motor tax on hybrid/electrical vehicles

  Currently, there are limits on the amount of capital allowances a business may claim on a company car i.e. regardless of the cost of the car, the capital allowances that may be claimed over the lifetime of the car is €24k. The limit on capital allowances for EVs could be increased to make the acquisition of such vehicles more attractive.

- Consider the VAT rate of electric and hybrid vehicles in order to bring the cost of such vehicles to a more competitive level.
- Extend the benefit-in-kind exemption for electric vehicles when the current scheme expires.

2. Are there existing taxation and welfare measures that are counter-productive to Ireland's climate change commitments?

Yes No

If yes, please specify:

To what extent are these justified in the Irish context and are any reforms necessary?

See discussions above in earlier questions, in particular Chapter 4 (a).

3. What changes should be made to the taxation system to ensure longer term fiscal sustainability given the expected impact of the continued decarbonisation of the Irish economy, in particular the impact of reducing tax revenues from energy, carbon and motor taxes?

Please detail the changes:

See earlier responses to Chapter 4 questions.

Chapter 5 - Housing

1. Taking into account previous taxation related interventions in the housing market, what role do you think the taxation and welfare systems have to play in contributing to the long-term supply of housing?

Please outline your views:

We would recommend the following could be considered.

- Currently, where a developer acquires a site, then 7.5% stamp duty is payable on that site. However, subject to certain conditions, where residential property is developed on the site, then a refund of 5.5% is due. This relief is due to come to an end for developments commenced post 31 December 2022. This relief should be extended beyond 31 December 2022.
- Covid19 has accelerated the trend towards online shopping and home working. While the exact outcome is unclear, this may result in a decreased demand for retail and office space. Currently, where a developer buys commercial property and re–purposes that property for residential purposes, then the above 5.5% refund may be available. Again, this relief should continue to be available post 31 December 2022.
- Currently, housing supply is falling significantly short of demand. There are multiple reasons for this shortage including capacity constraints (e.g. labour shortages), delays in planning and viability (based on current prices obtainable in the market, certain developments are not economically viable). In respect of affordability and viability, one of the factors driving this, is the amount of taxes and other levies associated with developing new houses. The VAT rate of 13.5% is an absolute cost for homes buyers and property investors (any cost incurred by an investor will likely be passed to tenants). In that regard, there are opportunities to reduce VAT and other levies such as development levies that could improve affordability and viability (albeit, as discussed below, the mechanics of same will need consideration).
- The CGT rate of 33% is high by international comparison and consideration should be given to reducing the same.
- The 20 – 25% rate associated with special vehicles such as IREF’s and REIT’s should be maintained. These vehicles are predominately used by foreign institutional investors. It is important to attract such capital to the Irish market as it adds to the stability and professionalism of the Irish property market.
- We would recommend that a review of the land taxes (local property taxes, Zoned Land Taxes) should be carried out. In particular, consideration should be given to whether the cost of new infrastructure should be passed to the purchaser of a new home (via development levies) or whether such infrastructure costs should be charged via Local Property Tax on the entire community (as in many cases it is the entire community that benefits from the new infrastructure). Such a change could have a positive impact on the viability and affordability of housing.
- The reintroduction of Mortgage Interest Relief should be considered – See below.
- The Help to Buy Scheme should be made available in respect of new and second-hand property. The Help to Buy Scheme should be available to a second-time buyers in very limited circumstances on a case-by-case basis (e.g. acquisition of a property following a divorce, by a spouse who did not remain in the family home).
- Providing tax reliefs to sellers (CGT exemption or a reduced rate) and buyers (Stamp Duty exemption or a reduced rate) for derelict/over-the-shop properties to be renovated and occupied as a principal private residence (“PPR”).
- Property Investors

- The Case V rules dealing with the expenses which are deductible are very prescriptive often resulting in costs that are incurred in the course of the rental business not being deducted, The rules should be amended so that expenses incurred wholly and exclusively for the purposes of the rental business are deductible.
- As discussed further in Chapter 6, capital allowances should be available on the cost of buildings used by businesses subject to such buildings achieving certain environmental accreditation.

Creating certainty for developers and investors is critical. While we have outlined above some suggested changes, it should be noted that in general these changes amount to relatively minor changes. In our view, fundamental changes to the taxation of Irish property is currently unnecessary and may lead to developer/investor uncertainty and ultimately drive entrepreneurs and capital away.

- International Investors

Foreign Private equity firms, insurance companies, pension funds and other institutional investors ("large foreign investors") have invested significant amounts in the Irish residential market in the last number of years. Many of these large foreign investors entered the Irish market in the early 2010's acquiring significant amounts of distressed debt following the financial crash. However, this was not the extent of the investment made by large foreign investors. Subsequently, significant amounts of capital were deployed by large foreign investors to finish uncompleted developments (including residential developments) and to commence new developments (including residential developments). In recent years a particular focus of large foreign investors has been social and affordable housing.

Prior to making any investment, large foreign investors will model the likely return over the investment period. This model will be used in making an investment decision. One of the factors in estimating that return is the amount of tax cost associated with the investment. Such tax cost can be a significant part of the cost of the investment. While there is always some level of volatility with forecasts, and in particular with tax, it is important that investors have a high degree of certainty when it comes to tax. In recent years, in a property context, investors have not been able to rely on the certainty that has historically been a feature of the Irish tax system. There is a view of many investors, whether right or not, that the Irish tax system pertaining to property is constantly changing. The following are some of the more significant changes that have been made to the property tax system since Finance Act 2016:

- The Irish Real Estate Fund (IREF) regime. Broadly, an IREF is an Irish real estate rich QIAIF or ICAV.
  - Finance Act 2016 introduced a 20% exit tax on IREF's.
  - Further changes were made to the IREF regime in Finance Act 2017 and 2019.

- The Real Estate Investment Trust (REIT) regime. A REIT is typically an ordinary Irish incorporated company that has a special tax status
  - The REIT regime was introduced in Finance Act 2013. Typical of REIT regimes in other developed countries, the REIT itself was exempt from tax. Instead, a 20% tax was collected on exit on that part of the profits relating to rental profits.
  - Finance Act 2019 increased the exit tax to 25% in certain circumstances, and extended the exit tax to dividends sourced from capital gains.
  - Finance Act 2019 also removed the stamp duty exemption for certain schemes of arrangements. Prior to this change, broadly, no stamp duty would arise on the transfer of a listed company. Following this change, stamp duty of 1% would apply.

- In May 2021, the Minister for Finance announced, by way of a financial resolution, the introduction of a 10% stamp duty rate in certain circumstances. In particular, where a person acquires a house on or after 20 May 2021, and the total number of houses acquired by that person or a connected person in the 12 months immediately preceding that date including the current acquisition is greater than or equal to 10 residential units, then the acquisition of that unit is liable to stamp duty at a rate of 10%. Normally, in respect of residential property, stamp duty of 1% would be payable on the first €1m and 2% thereafter
- Finance Act 2021 brought a non–resident company that holds Irish real estate into the corporation tax charge and thereby increased the rate of tax applicable on rental profits from the income tax rate of 20% to

25% and subjected such companies to the interest limitation rules which they would not have been subject to previously.

While a 20% – 25% tax on exit from the REIT/IREF regime is not unreasonable, it should be noted that many investors, who invested in the regime before the Finance Act 2016/2019 changes, invested on the basis of a different set of assumptions i.e. they would have modelled their expected returns using the tax system that existed at the date of their investment. Nonetheless, the Finance Act 2016/2019 changes applied equally to new and existing investors and there were no grandfathering provisions.

The Finance Act 2019 REIT changes and the introduction of the 10% stamp duty charge applied to particular transactions where the contracts where already signed. Amending law in an effective retrospective manner is seen as somewhat arbitrary by investors. Over many years, Ireland has developed a reputation as an open economy that welcomes foreign investment. Such changes can impact Ireland's reputation as a place to do business.

Also, in 2019 the Department of Finance flagged that a review of the taxation of property would commence in 2020. As a result of Covid19, that review has been delayed and is now likely to commence in 2022. While a review of the system is welcome, we would highlight the fact that the very expectation of changes coming out of such review has increased investor uncertainty. We would urge that this review proceeds in 2022.

The critical challenge in addressing the housing crisis is supply and viability. The focus should be on increasing supply, reducing costs/prices and removing many of the bottleneck developers face associated with matters such as capacity constraints, zoning and planning. We need large investors to provide the capital necessary to deal with these challenges. Key to ensuring continued investment by large foreign investors is providing a level of certainty in respect of tax. Further to that, we would urge:

- Where changes are made, the investor, the transaction or results accrued under the earlier legislation (whichever is relevant) is grandfathered.
- Prior consultation is had with the industry.

2. Should the taxation system have a role in supporting or promoting any specific form of housing tenure (e.g. home ownership, rental), or should it remain neutral?

Yes, taxation should have a role No, taxation should be neutral

Please elaborate further:

Whether government should promote home ownership over rental or vice versa is a wider discussion. However, in our view, prima facie both types of tenures are necessary.

Whatever the policy objectives of government, tax can play a role in stimulating investment, in the allocation of investment capital and changing behaviour. The main challenge in the current market is supply and viability and tax policy can only go so far in solving this.

The critical point is that care is needed to ensure that any changes to tax policy achieve an objective and is evidence driven.

3. What in your view is the role that taxation should play in housing affordability?

Please outline your views:

The cost of any new build includes a significant tax cost that may be passed to the end buyer including: -

- VAT at 13.5%
- Stamp Duty of 1% payable by the end buyer
- The developers/other contractors income tax and corporate tax are ultimately passed to the end buyer .i.e. such tax is another cost of the project

- Payroll taxes associated with the employees of the developer/contractors are ultimately passed to the end buyer
- Stamp Duty at c. 2% paid by the developer on acquisition of the site.

In addition to above the State will receive development levies. And a new Zoned Land Tax of 3% of market value may apply.

One suggestion is that instead of an upfront reduction of development levies together with upfront reduction in VAT and stamp duty rates for home buyers, consideration could be given to the re – introduction of mortgage interest relief.

4. Following the introduction and recent amendments to the Local Property Tax (LPT) and the commitment in Housing for All to introduce a new taxation measure to activate vacant land for residential purposes, do you consider there is a role for a Site Value Tax in Ireland?

What is a Site Value Tax?

A site value tax is an annual property tax based on the value of land, without regard to the value of any development or buildings on that land.

Yes, Site Value Tax has a role No, Site Value Tax does not have a role

Please elaborate further:

There is already a number of existing land value taxes including a Vacant Site levy (to be replaced with a Zoned Land Tax), Derelict Sites levy, Local Property Tax and Commercial rates. Adding another land-based tax to the mix would not be desirable. In addition, the Commission on Taxation Report 2009 concluded that while there was an economic rationale for a Site Value Tax, it was not recommended at the time and in any event there were significant practical matters which would need to be addressed before such tax could be introduced .e.g. a nationwide register and a methodology for valuing land. These practical barriers continue to exist and therefore, we would not recommend a Site Value Tax.

A Site Value Tax (SVT) is a tax on the value of a site or land. Underpinning this approach is a principle that land is valued according to its optimum potential use ('highest possible use') as defined by the planning process rather than on the current use which is disregarded. Thus, the idea of the tax is to reward owners who have developed land to its optimal potential while encouraging other owners to do so. In our view, if the purposes of the SVT is to encourage behaviours (and not a revenue raising tax), then such tax is unnecessary. The market will decide the optimal potential use and in most cases, the owners will sell or develop at the right price.

Chapter 6 - Supporting Economic Activity

1. How can Ireland maintain a clear, competitive, sustainable, and stable taxation policy with regard to its attractiveness to Foreign Direct Investment (FDI) in light of the rapidly changing global environment?

Please outline your views:

On 7 October 2021, the Minister for Finance, Paschal Donohoe issued a statement that Ireland would enter the OECD International Tax Agreement on Pillars I and II. Prior to signing up, Ireland successfully sought reassurances from EU officials that retention of the 12.5% rate for companies below the Pillar II threshold (€750 million global turnover) would be possible. Therefore, the agreement will allow for the retention of the 12.5% rate of tax for businesses with annual turnovers less than €750million. The Minister recognised the potential cost of the agreement as being very difficult to predict but noted an estimated cost of up to €2 billion annually. Nonetheless, the capping of the Pillar II rate at 15% can be considered a positive from Ireland's perspective. Further to above, we would make the following comments: -

- Ireland should continue to reiterate its commitment to the 12.5% rate and where relevant the 15% rate under Pillar Two. Ireland should continue to lead the way as a champion of fair tax competition.
- In addition, Ireland should consider ways to make its tax code more competitive. Some suggestions are set out below in more detail but in summary: -
    - Reform Ireland's interest deductibility rules, including introducing a Notional Interest Deduction on equity.
    - Consider appropriate measures for a territorial regime in respect of dividend and branch income.
    - Reform and streamline the double taxation relief regime in respect of other income such as royalties and interest
    - Continue to expand Ireland's treaty network
    - Improve our R&D offering
- Certainty for investors is critical. Recently, there has been significant amendments made to the Irish tax regime, with the introduction of many new rules including: -
    - Anti–hybrid rules
    - Interest Limitation Rules
    - Controlled foreign Company (CFC) rules
    - Exit tax rules
    - Substantial amendments to the Transfer Pricing rules
    - DAC6 mandatory reporting rules, Country by country reporting.

  In addition, Ireland will implement the Pillar I and Pillar II rules from 2023. While Ireland must continue to update its tax law to reflect international developments and remain competitive with other countries, we would recommend that following these changes, the government allows business a period where they can take stock and adjust. We would recommend that reforms to the interest rules and the double taxation rules are made in 2022 followed by a clear statement that there will be no significant unilateral changes to the Irish tax system in the short to medium term.

- Also, Ireland has made strong moves to be seen globally as engaging in "best practice". While this is essential to maintain our international reputation, Ireland is a small open economy which relies on FDI. Ireland does not operate in isolation and must be conscious of the positions being adopted by competitor nations. With respect to Ireland's remaining BEPS commitments, it is necessary that a desire to engage in "best practice" does not lead to Ireland agreeing to non-mandatory or more onerous provisions which are contrary to its competitive offering and position going forward

Interest deductibility rules

In comparison with our competitors, Ireland's interest deductibility rules are complex and cumbersome and are in need of urgent reform. By way of background, in Ireland, broadly interest is deductible under three separate provisions: -

i. Interest is deducted against trading income if such interest is wholly or exclusively laid out or expended for the purposes of the trade.
ii. Interest is deducted against rental income if such interest is on a loan to purchase, improve or repair a premises. (S.97 TCA 1997)
iii. Interest is also deductible under S.247 TCA 1997 on loans used: -
    - to acquire shares in other companies or
    - to on – lend to other companies for use in their business.

Further to above, we would make the following comments: -

- The wholly and exclusively for the trade provision is a principle-based approach and is well understood in practice.
- The TCA97 s97 provision is in general fit for purpose albeit it has certain shortcomings. For example, interest on a loan used to refinance a loan used to purchase, improve or repair a premises would not be technically deductible. In addition, certain financing costs such as swaps and arrangement fee would not be

deductible from a strict technical perspective as neither amounts are "interest". Some of these shortcomings have been addressed by Revenue practice, but such practices should be put on a legislative footing. In particular, a change of the rules to the effect that all financing costs, including interest should be deductible if incurred in the course of a rental business would be welcome.

- As mentioned, S.247 TCA 1997 provides relief for interest on loans used to acquire shares or to on- lend to other companies. The following should be noted: -

- The S.247 rules are condition heavy i.e. interest is only deductible if certain conditions are satisfied including if the monies are used for certain very defined purposes, if the interest is paid, if a certain percentage of shares are held in the company acquired, if the companies have common directors, if the monies are used within a specific period of time and if no capital has been recovered etc.
- The rules are complex. For example, certain provisions such as the need for common directors would seem to serve little purpose.
- As mentioned, any monies borrowed must be used for a highly prescriptive purpose. In some cases, even if the borrowings are clearly for business purposes, they may not fall within the very descriptive rules resulting in no tax deduction for genuine business interest.
- Under the Recovery of capital rules (S.249 TCA 1997), certain routine bona fide transactions such as repaying intra–group debt or internal restructurings can result in denial of interest relief.

In addition there are a wide range of other rules pertaining to financing which operate in tandem. These include: -

- Anti-Hybrid rules
- Controlled Foreign Company rules
- Transfer Pricing rules
- Distribution rules applicable to equity type debt instruments
- Anti-avoidance rules denying a deduction for interest on connected party loans to acquire connected party assets
- Other anti–avoidance rules such as S.840A TCA 1997 which broadly deny deductions in interest on connected party loans used to acquire connected party assets.

In addition, in Finance Act 2021, Ireland introduced the ATAD Interest Limitation Rules (c.50 pages of legislation). The introduction of such rules provided an opportunity for Ireland to review its existing interest deduction regime. Instead, the Interest Limitation Rules (which are in themselves, very complex) were layered on top of the complex and cumbersome rules already in place.
This places Ireland at a competitive disadvantage with other countries. In our view, S.247 TCA 1997 should be repealed and replaced with new modern interest deductibility rules that are principle based e.g. interest should be deductible if it is laid out or expended for the purposes of the business concerned. The Transfer Pricing rules, Interest Limitation and Controlled Foreign Company rules referred to above did not exist when S.247 was originally introduced. With these rules now in place, many of the reasons associated with the complexity of S.247 are no longer necessary.

In our view, adopting a principles-based approach to legislation whereby tax relief is permitted for finance costs measured on an accounts basis where the monies have been applied for business purposes and other commercial purposes of the taxpayer concerned would not extend tax relief inappropriately. This approach can then be effected subject only to the measurement limitations prescribed in ATAD which provide a bulwark against excessive interest burdens.

The purpose and intended effect of reform in this area would not be to increase the quantum or availability of relief but to bring simplicity and certainty for Revenue, taxpayers and advisers alike. Such clarity should reduce the necessity for Revenue opinions. The above changes would not only benefit MNE's, they should also benefit SME's.

In addition to above, outside a trading context, relief is given only to the extent that an express statutory provision permits relief: -

- An uncommercial distinction is made between interest and other forms of borrowing cost (e.g. discount or premium).
- The relative advantages of risk management tools such as financial derivatives (i.e. those relating to interest rate and foreign exchange hedging) are, outside treasury operations, reliant on statements of revenue practice rather than statute to determine whether and to what extent relief is available.

In this context, we advocate that consideration be given to a broad simplification reform of the Irish Corporation Tax Code provisions dealing with the tax treatment of all aspects of corporate finance.

Notional interest deduction on equity

On 18 May 2021, the European Commission adopted a new "Communication on Business Taxation for the 21st century". The Communication set out a number of proposals including a proposal for a Debt Equity Bias Reduction Allowance ("DEBRA"). While the exact mechanics are not final, the DEBRA will likely be a notional deduction calculated as a percentage of equity (DEBRA is also often referred to as a Notional Interest Deduction ("NID") or sometimes as an Allowance for Corporate Equity ("ACE"). The DEBRA is designed to align the tax treatment of the cost of equity with that of the cost of debt.

The proposal aims to address the pro-debt bias that exists in the tax rules of several EU member states where businesses can deduct interest attached to debt financing, but not the costs related to equity financing (such as dividends). This arguably encourages companies to accumulate debt. The proposal is intended to encourage companies to finance more investment through equity contributions. The Commission fears that over-indebtedness could threaten the stability of the EU's financial system and increase bankruptcy risk.

On 15 June 2021, the European Commission published an impact assessment on DEBRA. In the impact assessment, the EU Commission stated that the NID could be applied on (i) all corporate equity, (ii) new corporate equity, or (iii) corporate capital (equity plus debt). The introduction of an NID is already, to some extent, implemented by six EU member states (Belgium, Cyprus, Italy, Malta, Poland, and Portugal). Some of the features pertaining to these regimes are as follows: -

- The NID is deducted from the taxable income of the company
- The NID is calculated as the notional interest rate X equity
- The notional interest rate may be the rate on a government bond plus a risk premium
- The equity is broadly the share capital., share premium and reserves of a company adjusted for certain items.
- The NID is sometimes limited to a percentage of annual profits with any excess being carried forward for offset in subsequent years.
- In certain cases, the NID may be a tax credit rather than a tax deduction.

The Commission will make a legislative proposal in 2022 in respect of DEBRA. We would recommend that regardless of EU developments, Ireland proceeds to implement a DEBRA like regime. Introducing similar rules in Ireland would: -

- Encourage companies to seek equity rather than debt investment
- Decrease the cost of financing
- Reduce the risk associated with raising capital
- Allow companies to plan long term.
- Result in a general reduction of the effective corporate tax rate for companies,
- Act an incentive to retain earnings and to use these to finance new investments/growth

Territorial regime

We will be responding to the Department of Finance's recently published public consultation on the above but some of the matters at issue follow. It is generally accepted that relief for foreign taxation, and hence potential double taxation, is complex under Irish law. We would recommend the following:

- Ireland should consider an appropriate foreign branch profit exemption and a foreign source dividend exemption .i.e. a territorial regime.
- In addition a broad simplification of the existing tax credit rules in TCA 1997 Schedule 24 would be welcome such that the distinction between different categories of income is eliminated (i.e. interest, royalties, etc.). Relief should also be available in respect of any form of foreign tax suffered, irrespective of the type of the foreign tax.

Territorial regime - Dividends

The adoption of an appropriate exemption for foreign source dividends would be positive for Ireland and would replace what in practice is an effective exemption (due to extensive unilateral credit relief as well as bilateral measures) with an actual exemption. An effective exemption arises where the foreign tax suffered exceeds Irish tax on certain foreign dividends, which is the case in most circumstances. A simplified and competitive system for foreign source dividends would be particularly beneficial for Ireland's attractiveness as a holding company location.

European tax law requires tax neutrality in respect of the residence of the shareholder. In order to ensure the neutrality in respect of the source of the dividends, many European Member States switched from the (indirect) credit system to the exemption system. Ireland did not make this switch and ensuring our tax code is compliant with European law has led to the current difficulties with Schedule 24. A participation exemption would be a welcome simplification of our system and would reduce needless complexity.

The principal motivation behind any move towards such a 'territorial' system should be to enhance the competitiveness of Ireland's tax regime. We would recommend that taxpayers be allowed the option of an exemption given that it could reduce the level of interest deductibility (due to the Interest Limitation Rules introduced by Finance Act 2021); therefore, the regime should be optional. The proposed exemption system would be simplest if the exemption for foreign dividend and branch profits included as few exceptions as possible. Some of the enhancements to competitiveness arising from such a move are listed in the Coffey Review, and include:

(i) Improving the position of domestic firms vis-à-vis the taxation of outbound foreign direct investment;

(ii) Improving the attractiveness of the corporate tax code vis-à-vis the location of holding companies; and

(iii) Reducing what may be a non-trivial compliance burden on domestic outbound investor.

We would also add the following: -

(iv) Ensuring those provisions of Ireland's corporate tax code related to the treatment of foreign source earnings are compliant with EU law in a simplified manner; and

(v) Bringing Ireland's system in line with the majority of EU states

These measures are addressed in turn below.

(i) Improving the position of domestic firms vis-à-vis the taxation of outbound foreign direct investment;

TCA97 sch24 already in effect ensures a de facto participation exemption for foreign source dividends (see discussions relating to the Coffey report below) in most instances and foreign branch profits by its foreign credit mechanisms including credit pooling etc.

(ii) Enhance Ireland's competitiveness as a location for holding companies

Ireland is generally seen as an attractive holding company location. However, as mentioned throughout our response, in an increasingly competitive tax sphere Ireland needs to take steps to ensure it remains an attractive location. The Netherlands, Switzerland and the UK are typical competitors to Ireland as a location for ultimate and intermediate holding companies, and each of these jurisdictions offers a participation exemption for foreign-source dividends. Various international country guides routinely note that although Ireland does not offer a participation exemption for dividends it does offer credit relief, etc. such that little or no additional Irish tax should be payable. Such a statement is of course fact pattern specific. However, such detailed provisions make Ireland a prima facie less attractive holding company location, as international investors desire the simplicity, familiarity and clarity that a participation exemption affords.

(iii) Reduce compliance burdens for those companies already operating in Ireland

The Coffey report notes that "in practice Irish resident companies with foreign subsidiaries will not pay tax on the profits of such subsidiaries as companies will utilise the pooling of dividends and timing of dividends payments to 'mix' credits from high tax and low tax jurisdictions, retain earnings overseas for reinvestment rather than face a potential Irish tax liability". At present, there is a multitude of separate mechanisms of relief depending on the

source and nature of the dividend, with the result that the application of such rules is timely and costly for taxpayers. These complex rules arguably are of little consequence to the Exchequer, given they generate little or no additional revenue. In principle, an exemption system should also be simpler and administratively less burdensome for companies to comply with.

(iv) Ensure compliance with ECJ rulings

Although the ECJ has confirmed in principle in the first FII GLO case that a credit system for participation dividends conforms to treaty principles, substantial changes to Irish legislation have been required as a result of various court rulings (see for instance both FII Group Litigation Order rulings and Haribo amongst others). It is possible that future court challenges may arise as a result of our continued operation of a credit and deduction system which will require further changes to Irish tax law. In anticipation of any such potential challenges we believe that it is easier to achieve compatibility with an exemption system than it is with a credit system

(v) Simplification of Ireland's tax code

Previously one of the main arguments against a participation exemption for foreign source dividends has been the lack of CFC legislation. This is no longer the case as Ireland has introduced CFC legislation.

(vi) Bring Ireland in line with the majority of other EU Member States

The majority of EU Member States offer some form of participation exemption for foreign source dividends, and such dividends would ensure Ireland is on an even playing field with other Member States and is not an unnecessary outlier.

To maximise Ireland's competitiveness and ensure a clear and simple code, the participation exemption should apply for all foreign source dividends irrespective of whether they are derived from treaty or non-treaty locations. This broad application would help Ireland become more competitive as a holding company location relative to other nations such as the Netherlands, etc. It would be reasonable to apply a minimum ownership test similar to those which apply in existing legislation, see for instance the 5% holding requirement outlined in TCA 1997 s626B or s831.

<u>Branch exemption</u>

In broad terms, we recommend companies are provided with the option of an exemption from corporation tax for foreign branch profits, irrespective of the branch territory.

Opt-in mechanism

 Each Irish-resident company would be able to make an election for its foreign branches to be exempt from corporation tax. The profit or loss arising in each foreign branch would then be deducted from the Irish company's worldwide profit calculation to give a net amount that is subject to corporation tax.

 A branch exemption could prevent relief being given for branch losses and reduce the level of interest deductibility (due to the Interest Limitation Rules introduced by Finance Act 2021), and so the regime should be optional. A similar comment would apply to participation exemption for dividends. The election will cover only the company making the election, but would apply to all present and future branches of that company.

 Where a company does not opt-in to such measures, the existing provisions for branch taxation should remain in place as well as appropriate relief for double tax. Although these should be simplified in line with other revisions to TCA97 sch24.

We believe the exemption for branch profits should be extended to all branch income, irrespective of its nature. CFC rules could be used to combat any non-genuine arrangements.

<u>Overhaul of TCA97 sch24</u>

We propose a broad overhaul of TCA97 sch24 such that relief would be available for foreign tax suffered by whatever name. This reform should be carried out in conjunction with the introduction of a foreign branch profits exemption and a foreign source dividend exemption. The aim of such a broad overhaul should be to introduce a best-in-class regime for the relief from double tax. Relief should be available in respect of foreign tax suffered,

irrespective of the type of the foreign tax. The simplified regime would distinguish between income sources as follows:

 Income taxable as part of the company's trade (i.e. at the 12.5% rate)

 Income taxable as passive investment income (i.e. at the 25% rate)

We recommend that relieving provisions for tax suffered on income from non-EU / non-DTA sources should be no less favourable than those available for EU / DTA source income e.g. this could be made subject to the EU's published listing of non-cooperative jurisdictions as was the case with the Finance Act 2021 provisions regarding CFC rules.

We recommend that no distinction is made as to the class of income, e.g. interest, royalties etc. as is the case under the current system in determining foreign tax credits, pooling, etc.

The removal of differing treatment depending on income classification in our view is the simplest, most efficient manner in which to overhaul the current system. Differing treatment between the various classifications is a core part of the problem practitioners and clients face with the current system.

Pooling

There should be no restriction on the pooling and carry forward of excess credits, with one exception being a restriction on the pooling and carry forward for 12.5% v 25% source income. A form of value-based pooling could be applied in such instances.

Research and Development

Ireland competes for foreign direct investment (FDI) with multiple geographies. We also compete for R&D activities performed by established multinationals.

The continued narrowing of the allowable expenditure within claims creates significant difficulty for claimants. The removal for example, of rent as an allowable expense in many claims has signalled a reduction in the value of R&D tax credits for many claimants. This is happening at a time when the UK for example is moving to a higher rate of tax relief and clarifying inclusion of cloud hosting costs etc.

In the absence of such a change we would like to see a broadening of the direct R&D costs that qualify for the credit to include outsourced services which are not R&D when considered as stand-alone activities. This should encourage companies and in particular SME's, to invest in R&D and ensure that they get the benefit for the specific costs that are essential to the R&D process. The types of expenditure that we would like to see included would include testing and analysis of prototypes/materials/samples and where materials and equipment are modified or transformed by external suppliers so that the claimant company can use these items in their R&D.

As Ireland expands its onshore wind, offshore wind (both fixed and floating), solar and biofuel industries, there is likely to be significant investment in research, development and innovation. With the proper incentives, Ireland could become an innovation hub for renewable energy.

We would recommend a new legislative mechanism to provide specific tax relief for qualifying expenditure under defined sustainability criteria. This should assist in driving Ireland's capability in the area of green and sustainable technology and serve to promote and emphasise the importance of investment in this area, in the same way that the digital gaming tax credit is focusing on the growing Irish base for this industry. It should assist Ireland in meeting its significant emissions targets and provide benefit to a new specialist business sector. This incentive could potentially reward companies for investing in product development in this space, for projects that do not meet the requirements for R&D tax credits and also to companies investing in the implementation for existing technology.

We refer to the FA2019 amendments to the R&D code which remain subject to Ministerial order and acknowledge the difficulties the Minister noted at the Committee stage debates of Finance Act 2021. That said, we would suggest that similar types of changes be brought about for the SME sector given the difficulties facing that area in terms of investment.

An immediate, easily implemented and significant value add for Irelands FDI competitiveness would be to increase the R&D tax credit to 30% for all claimants. This will reduce the cost of conducting high value activities, managed and conducted by a skilled workforce on the island of Ireland. This in turn improves competitiveness and secures our already established R&D performing multinationals. It also has the added benefit of closing the gap on Irelands R&D specific competitiveness when compared to other European and international geographies where more generous tax benefits exist for undertaking R&D activities.

Knowledge Development Box

We understand that the uptake for the scheme to date has been low. The latest data available shows few claimants availing of the benefit. Arguably, this can be attributed to the restrictive criteria of what constitutes qualifying Intellectual property (IP) for inclusion in the scheme, which has limited the range of IP assets that can benefit from the incentive. In addition, a major component of calculating the benefit relates to the identification of the profits which are derived from the qualifying IP asset. This requires significant analysis and a range of factors must be considered when calculating same.

Tax Treaty Network

Ireland should continue to expand its treaty network in particular with developing countries where there is significant opportunity for growth.

Capital Allowances

One of the shortcomings of the current capital allowances regime is that expenditure on many buildings do not qualify. To be clear capital allowances are available for certain building like factories, mills and hotels. However, most buildings such as offices, call centres and retail units do not qualify for capital allowances. We would recommend that tax depreciation be allowed for these buildings. A condition for this relief might be a requirement that the building obtains a certain energy rating.

Tax administration

- Ireland should ensure that the Irish Revenue has sufficient resources with the right level of competence.
- It is imperative that our system is seen as fair and balanced. Further to that, we would refer you to the following: -
    - An Appeal Commissioners can give directions to both Revenue and the taxpayer during the course of an appeal for example to provide a statement of case and/or an outline of arguments. Those directions will have deadlines. If such deadlines are not adhered to, the Appeal Commissioner can dismiss the appeal. This would be an appropriate consequence if a taxpayer does not comply with a direction. However, it is wholly inappropriate that a taxpayer's appeal could be dismissed if the Revenue Commissioners, who raised the assessment under appeal in the first instance, do not comply with such a direction. We would submit that in such an instance, the equitable outcome should be that the appeal be determined in favour of the taxpayer (S.949AV TCA 1997).
    - Section 960GA TCA 1997, which was introduced by Finance Act 2020, provides that where a taxpayer appeals an assessment issued by Revenue and discharges the disputed tax liability but subsequently wins the appeal, no interest shall be paid on the tax refunded. This treatment discriminates against a taxpayer who has paid the tax liability pending appeal. In contrast, if tax is found to have been underpaid, the taxpayer is charged interest at annualised rates of 8% or 10% per annum from the date the tax liability falls due. Given the time between the assessment and the decision of the tax Appeals Commission can be significant we would suggest that TCA97 s960GA be reconsidered.
    - Interest is due at a daily rate of 0.0219% on late payments or payments of corporation tax that are not made in full (c8% per annum). This is one the highest interest rates in Europe (e.g. Italy 0.01-4%, UK 2.6%, France 2.4%). Further an interest charge cannot be appealed to the Tax Appeals Commission.. Consideration should be given to a proportionate resolution of both difficulties.
    - Section 110 TCA 1997 provides for the taxation of securitisation vehicles. In order to avail of this regime, a company must, amongst other conditions, notify an 'authorised officer' in Revenue that it is or intends to be, a 'qualifying company'. Companies must submit a Form S.110 to Revenue within eight weeks of the date that they meet the conditions in the definition of "qualifying company" in TCA97

s110(1). If that deadline is missed, the company will not be regarded as a "qualifying company". We would suggest that it would be a more proportionate response to impose fixed fines or penalties in such cases.

Such measures directly impair Ireland's pro-business status-and as a result impair our global competitiveness. Such provisions should be amended to ensure balance.

General

- The continued dual rate corporation tax system should be reviewed .i.e. the 12.5% rate for trading and the 25% rate for passive income. The worldwide average statutory corporation tax rate, measured across 202 tax jurisdictions, is 22.96% with Europe having a regional average of 18.35%. Whilst Ireland's 25% rate may be considered competitive back in 2000, many governments have over time reduced rates to attract investment and ensure continued economic prosperity of their citizens. On that basis, a detailed review needs to be undertaken at this point to consider the merits of moving to the single rate of 12.5% (or 15% where respective provisions for the application of OECD's Pillar II apply) for all income taxable in Ireland.
- Like most developed countries, Ireland has a participation exemption which exempts gains on the disposal of certain trading companies/subgroups. This exemption, however, is limited to companies which are tax resident in the EU and Double Taxation Agreement ("DTA countries"). Consideration could be given to expanding this exemption to companies tax resident in non–EU/DTA countries. This would further improve Ireland's attractiveness as a headquarter region. Disapplication of that relief could be considered for e.g. countries on the EU Commission's blacklist. Such an approach has already been taken for CFC reliefs as part of Finance Act 2021.
- The participation exemption also does not extend to a migration of tax residency giving rise to exit tax. With an increase in migrations arising in M&A, while there may well be another policy rationale for not extending the exemption to deemed disposals, the extension of the exemption to such cases should be considered.
- Ireland currently has a wide range of interest, royalty and dividend withholding tax exemptions. These exemptions should be maintained – albeit, accepting that there will be some changes to update for EU blacklisted countries.
- Irish Companies paying dividends to a partnership must withhold tax even if the partners in that partnership themselves would be exempt if holding shares directly. While Revenue can give a concessional treatment, it would be preferable to have this provided for in legislation.
- Close company related legislation aggregates partnership interests to treat a company held by "partners" as "close". In private equity there can be a very large number of investors. While Revenue can grant a concessional clearance on structure-by-structure basis, it would be preferrable to have a legislative concession for widely held funds.

2. How can the taxation environment support indigenous enterprise, particularly small and medium sized enterprises (SMEs) to be productive, to innovate and be competitive internationally?

Please specify:

While the impact of Pillar II on our economy is currently unclear, it does highlight the structural risk of a reliance on MNE's. It is imperative that Ireland provides an attractive entrepreneurial landscape for upcoming entrepreneurs. There are numerous forces which will drive a successful entrepreneurial landscape in Ireland, such as a skilled workforce, financial and technological resources and infrastructure, etc. Critical to all of these forces is our tax system. It is imperative from an entrepreneurial perspective that our tax system incentivises innovation, encourages longevity and does not punish failure.

We suggest the following moves as part of our recommendations: -

- 20 per cent tax rate on certain dividends: A 20 per cent tax rate should be provided on dividends, subject to a €100,000 per annum limit once the business has been in existence for five years. This would: (a) encourage entrepreneurs to grow their business for five years; and (b) retain cash for re-investment in the company during this start-up period

- **Capital Gains Tax (CGT) Tapering Relief:** With a view to designing a tax system that encourages individuals to stay in business for longer, CGT tapering relief should be introduced for individuals. This relief would encourage entrepreneurs to 'stay the course' and scale their business internationally.
- **100 per cent rollover relief** to be provided for entrepreneurs that exit the business earlier, but who re-invest 75 per cent of the proceeds in shares in another trading company, the disposal of which would be within the CGT charge
- **Tax-Efficient Financing Arrangement:** We recommend that a loan finance arrangement be introduced whereby individuals can lend money to SMEs and, provided certain safeguards are in place, for example, market interest rates are applied, then, the individual will be taxed on the coupon received at the standard rate of income tax (i.e. 20 per cent) as opposed to the marginal rate of income tax (i.e. up to 55 per cent)

In addition, we outline below some additional amendments to existing legislation.

Entrepreneur Relief

CGT Entrepreneur relief provides that gains on disposals of "chargeable business assets" made by individuals are liable to a reduced CGT rate of 10%, up to an overall lifetime limit of €1m. The standard rate of CGT (currently 33%) applies to gains made in excess of the lifetime limit.

A "chargeable business asset" is defined as –

- A holding of not less than 5% of the ordinary shares in the qualifying business (or in a holding company of a qualifying group)
- The asset must be held by an individual who is director or employee of the qualifying company (or companies in a qualifying group) in a managerial or technical capacity;
- The individual must be required to spend not less than 50% of their working time in the service of the qualifying company; and
- The individual must have served in that capacity for a continuous period of 3 years in the 5 years immediately prior to the disposal.

To qualify for the reduced rate of 10% the shareholder must have owned the "chargeable business assets" for a minimum period of 3 years prior to disposal. A qualifying business is widely defined to include all activities apart from (i) holding assets as investments, (ii) holding development land or (iii) the development or letting of land.

We would make the following comments: -

- The lifetime limit of €1m is too low and should be reviewed.
- There is no incentive for an entrepreneur to remain in place and scale the business.

In our view the entrepreneur should also be able to choose to apply a form of tapering relief as discussed below.

CGT Rate

The current CGT rate of 33% is high by international standards, and consideration should be given to reducing same. However, alternatively, consideration could be given to reducing the CGT for entrepreneurs who stay with their respective businesses with a view to scaling up their business.

It is generally in the enterprise's interest that the entrepreneur remain actively involved with the enterprise for as long as possible. In the past, reliefs such as CGT tapering relief recognised this fact and incentivised the entrepreneur remaining with the business. We would argue that a similar relief should now be introduced.

Take the example of a successful entrepreneur who builds a business to a particular size such that he or she is offered, say €10 million for their investment. The owner knows that the business has the potential to reach a multiple of that if she/he remained, giving the necessary direction for, say, another five years. An additional incentive for remaining with the business may be a reduced rate of CGT where an investment is held for a particular point in time. Tapering relief is not without precedent in that the Capital Gains Tax (Amendment) Act 1978 had provisions for "tapering relief" before its repeal in 1982. The 1970s tapering tax relief operated in such a manner that the applicable CGT rate was reduced after every three years in which an individual had company ownership, with no CGT

being charged for ownership periods in excess of 21 years. On introducing CGT tapered relief, the then Minister for Finance provided as follows: -

> *"Section 4 [The relevant amending section] proposes a further fundamental change in the rate structure of capital gains tax. The new structure is based on the principle that the rate of tax should be related to the length of time for which an asset is held between acquisition and disposal. A basic aim of any capital gains tax should be, I believe, to discriminate between the speculator and the genuine entrepreneur or businessman or farmer. Equity clearly demands that investment and hard work should not be penalised while economic logic demands that a capital tax should not act as a disincentive to economic activity. A man who builds up a business over 15 or 20 years, putting time, effort and money into its improvement and expansion, should not be taxed on the same basis as somebody who simply buys and sells an asset within a short time, relying solely on market forces to increase the value of the asset in question."*

A new tapered tax relief could operate in such a manner that the applicable rate of CGT would be reduced on a pro rata basis depending on the length of ownership in the relevant assets by the individual concerned. The very reason for the introduction of this form of relief is commensurate with our need to stimulate growth in the Irish entrepreneurial landscape. A similar relief would reward commercial longevity, signal Ireland as an excellent place to operate as an entrepreneur and encourage direct domestic investment and future domestic employment. In our view, the design of such a tapering relief should encourage long-term ownership, which could be achieved by providing for the CGT rate to be reduced over time depending on the period of ownership/active involvement as follows:

Period of ownership	*CGT rate*
0-5 years	33%
5-10 years and a full-time working director for 5 years	16.5%
10+ years: working director for 10 years and a full-time working director for 5 years	8.25%

In addition, 100 per cent rollover relief should be allowed for persons who exit the business earlier but who then re-invest 75 per cent of the proceeds in another company which is itself subject to CGT on a future disposal of that investment.

Therefore, with this policy objective in mind of rewarding the 'genuine entrepreneur', we should look to the approach adopted in the 1970s and should introduce a 'fundamental change' in our capital gains tax rate structure for entrepreneurs that encourages a strong entrepreneurial spirit in our domestic economy that is aligned to economic success. If deemed necessary the relief could apply to certain industry sectors subject to State Aid rules etc.

Dividends taxable at the standard rate of income tax

With a policy objective of encouraging entrepreneurs to keep investments in the business and to reward successful entrepreneurs that have emerged from the start-up period, a 20 per cent tax rate on dividends could be provided to entrepreneurs subject to an annual dividend cap of €100,000 and subject to the company's having been trading for a period of five years. Currently, preferential rates of tax on dividends apply in the UK and the United States and we would recommend that Ireland update tax policy in this area, which will aid in attracting and retaining entrepreneurs.

Making the investment – Tax efficient financing arrangement

Many SMEs require access to financial support in various stages of their development in order to continue and grow their business. Without such support it may not be economically viable to operate. Debt funding from third-party financial institutions may be limited for SME's and thus alternative means of funding are paramount.

An alternative to debt funding from financial institutions would be to introduce a special loan finance arrangement whereby individuals can lend money to SMEs in the EU (and based on the EU definition of an SME) and provided certain safeguards are in place (for example, market interest rates are applied), then the individual will be taxed on

the coupon received at the standard rate of income tax (i.e. 20 per cent) as opposed to the marginal rate of income tax (i.e. up to 55 per cent).

This alternative funding option for SMEs is important as while the Employment and Investment Incentive is a welcome source of finance for SMEs, the reality is that, from an investor's perspective, the shares acquired under this scheme rank behind trade creditors on liquidation. This results in a significant concern regarding the security of the investment. The loan finance arrangement should alleviate these concerns. In addition, many potential investors have capital held in deposit accounts etc. which give a particular rate of return. This loan finance initiative should act as an incentive to 'relocate' those funds into 'active' investments with the potential for a higher market rate return taking account of the additional risk being borne by the investors.

Start Up Relief for Entrepreneurs (SURE)

The Start Up Relief for Entrepreneurs (SURE) aims to incentivise individuals currently or recently in employment to start and invest in their own business. SURE enables such individuals to claim income tax relief on investments in their business of up to €100,000. The relief is limited to the amount of income tax the individual has paid through PAYE over the previous 6 years. We would recommend that:

- SURE is extended to include new business founders who were previously self-employed and are starting up another business.
- SURE should be extended to companies engaged in professional services and financial activities. Given Fintech is a burgeoning industry, financial activities should not be excluded from this relief. Also, professional services are a key part of the economy and encouraging new start-ups will increase competition in the area.

Employment Investment Incentive (EII)

EII is a tax relief which aims to encourage individuals to provide equity to trading companies. An individual can claim tax relief (against income taxed at either the 20% or 40% rates) against their income tax liability in the year in which they subscribe for shares in the company. The maximum investment on which an individual can claim relief in a year is: -

- €250,000 where those shares are held for a minimum period of 4 years only or
- €500,000 subject to those shares being held for a minimum period of 7 years

Any gain on the subsequent disposal of the shares in subject to CGT of 33%. However, any loss on disposal is not an allowable loss. We would suggest the following: -

- Enhance the EII by allowing USC tax relief on qualifying EII investments: -
    - Even if just for a period post pandemic which would allow companies to bolster their balance sheets
    - Or where investments are say held for a certain period.
- Allow CGT loss relief if the investment fails.
- Add a higher annual investment limit for investments over say a 15 - year period.
- Relief is only available where the company is carrying on "relevant trading activities". Relevant trading activities exclude professional services and financial activities. As above, given Fintech is a burgeoning industry, financial activities should not be excluded from this relief. Also, professional services is a key part of the economy and encouraging new start-ups will increase competition in the area.
- Only investors that are Qualifying Investors can obtain relief. One of the conditions to be a Qualifying Investors is that the investor cannot be "connected" with the company. Essentially, an investor should be a third-party investor with no prior connection with the company (other than where that connection is by means of a previous EII investment). References to connected in this context include situations where the individual or a relative of the individual (being a spouse, civil partner, ancestor, lineal descendant or sibling) has an interest in the capital of the company. (TCA97 s500(2)) For micro firms these associates are likely to be one of the few sources for initial small-scale capital. We would recommend that this is amended to allow such associates to invest in micro companies. Indecon, in their 2018 review of the EII scheme, recommended that associates

should be permitted to invest up to an aggregate amount of €200,000 in the first 12 months of their establishment in micro enterprises employing less than 5 employees.
- Under the Renewable Electricity Support Scheme (RESS), renewable electricity projects bid for capacity and get a guaranteed price for their output. At least five RESS auctions are planned to be held between 2020 and 2025, supporting the government's objective of cutting emissions by 51% and reaching up to 80% renewable electricity by 2030. Many of these projects are driven by the local community or seek a level of community investment. The structure of such Community investments is generally through a corporate vehicle. A requirement of the RESS scheme is that such corporate vehicle is at least 51% owned by the Community. This requirement means that Community led projects may not be eligible for EIIS i.e. one of the conditions of the EIIS is that the company must be a qualifying company. For a company to be a qualifying company, the company must not be under the control of another company. We would recommend that the definition of qualifying company is amended so that a company may be a qualifying company if under the control of a community led corporate vehicle.
- In addition, the requirement of tourism enterprises to have applications reviewed by Failte Ireland should be removed. An Indecon review of the EII scheme carried out in 2018 considered the additional application requirements on tourism enterprises which Failte Ireland undertakes on behalf of the Revenue Commissioners. The review could see no reason why the information requested was needed and noted that it created an "unnecessary layer of bureaucracy".

Retaining talent

In the current market, many SME's are struggling to attract and retain employees. It is important that measures are introduced for SMEs to firstly, assist them with their remote working offering, and secondly to facilitate non-cash reward mechanisms to help attract and retain key staff. In particular, employee ownership has many benefits including:

- Employee-owned businesses tend to be more successful, productive, competitive, profitable and sustainable.
- Staff in employee-owned businesses tend to be more entrepreneurial and committed to the company. (2012 Nuttall Report)

Share Options

There is generally no tax due on the date that an option is granted. When an employee exercises an option, that individual must pay Income Tax, Universal Social Charge and PRSI on the difference between the market value of the shares on the date of exercise and the amount paid for the shares. Any subsequent sale of the share will be subject to CGT of 33% on the gain arising.

However, the taxation treatment of a long option is different. A long option is an option that can be exercised more than seven years from the date it is granted. In the case of a long option, the taxpayer should pay Income Tax on the grant date and the date of the exercise of the option if the option price is less than the market value of the shares at the grant date. The tax at grant date is due on the difference between the market value of the shares on the grant date and the amount the employee will pay when they exercise the option.

We would suggest that the distinction between short options and long options be removed, i.e. that the treatment of long options be the same as short options.

Key Employee Engagement Programme ("KEEP")

The KEEP (Key Employee Engagement Programme) is a share option scheme introduced specifically for certain qualifying SME companies. There is no tax charge on the date of grant or exercise of the share option. The tax charge arises only on disposal of the shares acquired on exercise of the KEEP option. The tax charge will be on any gain at the CGT rate of 33%.

The introduction of the Key Employee Engagement Programme ("KEEP") was heralded as a welcome move to incentivise Small & Medium-Sized Enterprises ("SMEs") to retain and reward staff in a tax efficient manner. KEEP was intended to bring Ireland into line with a number of other jurisdictions in order to assist SMEs in competing with publicly quoted companies who have the ability to use share-based remuneration to attract talent. However, KEEP in

its current design has unfortunately failed to provide SMEs with an easy-to-implement and cost-effective way to offer shares to employees. We would recommend that: -

- Professional services and companies involved in financial activities are allowed to avail of KEEP.
- CGT treatment should be allowed on the buy-back of shares to reflect the fact that the employer company represents the likely buyer of employee shares in the SME sector.

Innovation - R&D Credit

See earlier comments in respect of R&D.

VAT

- Extend the 9% VAT rate for the hospitality sector indefinitely. Ireland's hospitality sector is world-renowned and providing certainty around the 9% rate would underpin confidence and stimulate investment and growth.
- The 23% rate is one of the highest rates in Europe. The rate should be reduced to 21%. This should stimulate consumer spending potentially increasing the VAT take.
- The current VAT thresholds are: -
    - €37,500 for businesses that supply services only,
    - €75,000 for businesses that supply goods only and
    - €75,000 for businesses that supply both goods and services (provided they generate more than 90% of their turnover by supplying goods).

  Increasing these thresholds to €50,000 and €100,000 respectively would help small businesses.

- Increase the cash-receipts basis of accounting for VAT threshold (currently €2m)

Trading Losses

- Broadly, current year trading losses can only be set back 1 year against profits of the prior year. This is a useful relief as the trader can get an immediate tax refund. We would recommend that the ability to monetise corporation tax losses be extended by allowing for the carry back of such losses for a period of three years. (Consideration could be given to imposing a maximum amount on this relief)
- Currently, trading losses forward can only be set against profits of the same trade. We would suggest allowing trading losses forward to be set against other trades or passive income (whether of the respective company or the loss group of which the company is a member).

3. With regard to starting, scaling or growing a business in Ireland:

a) what features of the current taxation system work well?

b) what features do not work well and how can these be improved?

See suggestions made in response to previous questions in Chapter 6.

Chapter 7 - Tax Expenditures

1. How do you think the process of reviewing taxation measures and taxation expenditures is currently functioning?

Please outline your views:

How well defined do you think the benchmark taxation system is in Ireland?

We have no comments to make in this regard.

2. How do you think the process of taxation expenditure review could be improved?

Please specify:

We have no comments to make in this regard.

3. Please give examples of taxation expenditures that you believe run counter to public policy/are badly designed?

Please specify:

Please explain your rationale?

In our view, there are a number of reliefs that need to be reviewed and amended such as the Special Assignee Relief Programme ("SARP"), the Foreign Earnings Deduction ("FED"), Employment Investment Incentive (EII), Start Up Relief for Entrepreneurs (SURE), CGT Entrepreneur Relief and Key Employee Engagement Programme ("KEEP"). These reliefs have in general not met their policy objectives or there is limited uptake. We have commented further on each of these reliefs in Chapters 3 and 6.

4. Please provide examples of taxation expenditures that you believe work well, either in Ireland or internationally?

Please specify:

The R&D credit has been a successful tax expenditure. However, we would refer you to Chapter 6 and our comments in respect of same.

Chapter 8 - Public Health

1. How well do the taxation and welfare systems support good public health outcomes, addressing health challenges including but not limited to those caused by or related to tobacco and alcohol use, obesity, poverty and/or environmental issues?

Please outline your views:

We have no comments to make in this regard.

2. What changes would you like to see to better promote the goal of good public health?

Please specify:

We have no comments to make in this regard.

Chapter 9 – Administration

1. How can modernisation of the taxation and/or welfare administrations evolve to best meet customer needs in a satisfactory manner while respecting data rights and ensuring secure and reliable tax collection?

Please outline your views:

What do you see as the implications of modernisation for taxpayers either positive or negative?

The Department of Social Protection (DSP) saw a huge surge in Jobseeker's applications in March 2020 as the Covid-19 pandemic closed businesses across Ireland. Automation has proved to be highly successful in rolling out quick and stable solutions to deal with increased demands associated with the Covid-19 pandemic. The automation was further expanded to provide a solution to automate the issuing of PUP Arrears Statements. Automation has been successful in the automation of mundane and repetitive work thus freeing staff to focus on more critical and high value activity. Also, automation reduces errors and increases processing time and can break the direct line between service demand and cost. We would recommend that further consideration is given to what other taxation and welfare services can be automated.

Revenue Online Service (“ROS”), MyAccount, MyWelfare, WelfarePartners, MyGovID are all important business and citizen services for taxation and welfare. They provide real time, convenient and efficient access to government services. In particular, in our experience, Revenue Online Service (“ROS”) is positively regarded by taxpayers.

It will be key to ensure that all system continues to be user friendly and intuitive.

2. What improvements in service quality and delivery could be achieved by integrating (elements of) the taxation and welfare administrations?

Please specify

Are there any risks arising from such integration?

We have no comments to make in this regard

Chapter 10 - Submit Your Ideas

1. Taking into account the Terms of Reference, submit any other thoughts, ideas or feedback on taxation and welfare in Ireland:

Please outline your views:

See responses to previous questions.

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