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# Finance Act 2011



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# Introduction

The Finance Act was passed by the Dáil and the Seanad in record time. Reflecting on the times we live in, this was necessary to give some stability to our tax system and provide potential investors with some degree of certainty as to Ireland's commitment to fiscal stability. The Act, for the most part, simply brings into legislative effect the measures announced in the recent Budget.



The main positive point to mention from a business perspective is the retention of the 12.5 % corporate tax rate. It is welcome news for all companies doing business in Ireland and should help to give Foreign Direct Investment a degree of certainty.

Another welcome measure is the introduction of the Employment and Investment Incentive (EII) scheme, subject to approval from the European Commission. In the meantime the BES Scheme and the CSC Scheme will continue to operate. Together with the extension of tax exemption for start up companies who commence business in 2011, these measures should have a positive impact on companies in the SME sector to

bring their ideas to market and also give stimulus to Foreign Direct Investment in this area.

The income tax base has been widened and a number of reliefs have been abolished. Households will feel the impact of these measures but it is argued that it was necessary under the current circumstances, to reduce our fiscal deficit and to get on to the road of recovery.

The proposed restrictions to section 23 type and other property tax reliefs will now not come into effect immediately, but an economic impact study will be undertaken first. This is welcomed as the restrictions could have led to a loss of trust in our

taxation system, as well as indirect economic effects.

Overall, the Finance Act contains a number of important measures which companies and individuals should consider carefully.

We hope you find our summary useful and you should note that some of the issues contained in the Act were already discussed in further detail in our Budget 2011 summary which is available on our website. We would be very happy to answer any of your queries or discuss any of the topics raised in further detail.

We look forward to hearing from you.

**The ByrneWallace Tax Team**

# Tax on Business

## Employment and investment incentives

As previously announced in the National Recovery Plan 2011-2014, and mentioned in the recent Budget, the Act introduced legislation providing for the Employment and Investment Incentive (EII) (the replacement for the outgoing Business Expansion Scheme (BES)) which is intended to stimulate employment and growth in the indigenous small and medium enterprise (SME) sector. While the EII is now provided for legislatively, it is subject to a Ministerial Commencement Order due to the necessity to seek approval from the European Commission. Until such approval is received, the old BES legislation will still apply.

Despite the lengthy nature of the provisions of the Act in connection with the EII, many of the features and provisions of the old BES legislation have been retained. In effect, the EII is "BES plus". There are, however, some key changes:

- the restriction in relation to "qualifying trades" has been dropped. The EII should be available to a much more significant cross-section of SMEs across all industry sectors and types. In order to qualify, the requirement is simply that a company is carrying on a taxable trade, although of the course there are exclusions to this for specific activities including, amongst others, land dealing companies, financial services companies, certain companies in the hospitality sector and closely held professional services companies.
- companies that have not yet commenced the restriction in relation to "qualifying trades" has been dropped. The EII should be available to a much more significant cross-section of SMEs across all industry sectors and types. In order to qualify, the requirement is simply that a company is carrying on a taxable

trade, although of the course there are exclusions to this for specific activities including, amongst others, land dealing companies, financial services companies, certain companies in the hospitality sector and closely held professional services companies.

- companies that have not yet commenced trading but who are engaged in certain qualifying research and development activities can qualify for the EII but relief will only become available once the company commences to trade or has spent at least 30% of the proceeds raised on research and development activities.
- the holding period in which individuals must continue to hold the shares in the qualifying company has been reduced from 5 down to 3 years.
- the rate at which relief is given is initially reduced to 30% (formerly 41% under BES), however this can be increased after a period of 3 years by an additional 11% where certain employment or research and development targets are met.
- the lifetime limit on funding that a company may raise through the EII has been increased to €10m (was €2m under BES).
- the maximum that a company may raise in any given year has been increased to €2.5m (was €1.5m under BES).
- the certification process for approval under the EII has been streamlined as compared to BES.

## Interest deductions

The Act has introduced provisions which tighten up the legislation surrounding the ability of companies to claim a tax deduction for interest payments. The changes focus on two areas: intra-group borrowings and interest as a charge.

On intra-group borrowings, with certain limited exceptions, a tax deduction will no longer be available on interest incurred on such borrowings where they used to finance the purchase of assets from another group company. These changes are very wide in scope and could potentially affect corporate groups with centralised purchasing functions as well as certain financial services companies such as group treasury management.

The Act also introduces new anti-avoidance measures in relation to the deductibility of interest available to companies on loans applied in lending to or acquiring shares in other companies (Section 247 TCA 1997 – "interest as a charge"). As the provision only applies to loans made on or after 21 January 2011, existing loan arrangements should not be impacted.

The provisions in relation to Section 247 are as follows:

- in order for interest on a loan to qualify for relief under Section 247, the borrowed money must be used wholly and exclusively for the purposes of a trade, the purposes of property rental or for acquiring trading or property rental companies.
- the company qualifying for interest relief must have a material interest in the company that ultimately uses the borrowed money and these companies must have a common director.
- relief will be restricted where the companies which use the borrowed monies are not within the charge to Irish corporation tax and are in receipt of interest on those monies.
- interest relating to monies used for the purpose of a trade will be relieved at the 12.5% rate of corporation tax on trading income.
- the recovery of capital rules are amended to permit companies to elect that they do not apply in the case of an exchange of shares.

# Financial Services



## Section 110

The Act introduces a number of changes to Ireland's structured finance regime which is centred on the tax designation provided to certain securitisation vehicles under Section 110 TCA 1997.

The most significant change has been to broaden the scope of the range of assets and nature of activities that a qualifying company may undertake for the purposes of Section 110. Qualifying assets for the purposes of Section 110 now includes

physical commodities (such as gold, silver etc.), plant and machinery (i.e. aircraft) and certain carbon offsets. This expansion recognises the shift in structured finance away from the more traditional areas of RMBS and CMBS towards areas such as the Green IFSC and is intended to reinforce Ireland's position as a world leader for structured finance.

The Act also introduces certain anti-avoidance measures which seek to limit the

ability to claim a tax deduction for certain profit dependent interest payments and total return swap payments where the recipients are resident in a non-tax treaty jurisdiction. The changes are complex but are targeted at manipulation of the Section 110 rules for certain tax avoidance purposes. It is likely that most capital market transactions will fall outside the scope of these provisions given that payments to investors holding quoted Eurobonds and wholesale debt instruments are exempted from the provisions.

## Property related measures

### Property tax incentive scheme restrictions

In the face of significant criticism and lobbying, the implementation of the proposed restrictions to Section 23-type reliefs and other property related capital allowances schemes announced in the Budget has been delayed. Given the potential impact to employment and the economy in general it is welcome that there is to be an assessment of what this impact will be in comparison to whatever saving could be achieved to restricting these allowances.

The provisions in relation to the restrictions have been included in the Act, however they are subject to a Ministerial Commencement

Order. This Order can only be issued after the publication of the impact assessment report and thus, in practical terms, the earliest that the restrictions could now apply is 1 January 2012.

### Reform of relevant contracts tax

Significant changes to the relevant contracts tax (RCT) system are contained in the Act. Similar to the provisions in relation to the property related tax reliefs, these changes are also subject to a Ministerial Commencement Order.

Though the new provisions do not appear to broaden the scope of the RCT system, they do substantially change the nature of its operation. The key changes are:

- the abolition of the old C2 certification system and the introduction of a three level system with a different withholding tax rate for each level: 0%, 20% and 35%.
- significant changes to the administrative elements of the system and in particular a push towards electronic reporting and returns.

Until the Ministerial Commencement Order, the old RCT rules will apply, however, once the Commencement Order is in place, the new system will apply to all relevant contracts still on going, including those signed pre the commencement date.



# Tax on Individuals

## Universal Social Charge

As previously signalled in the Budget, a new tax known as the Universal Social Charge (USC) has been introduced with effect from 1 January 2011. The USC effectively merges the pre-existing health and income levies into one streamlined charge and thus is not a new tax in the true sense. The Charge will have the following rates and thresholds:

- 0% < €4,004
- 2% €0 to €10,036
- 4% €10,037 to €16,016
- 7% > €16,016
- 10% > €100,000 (only for the self-employed)

This is broadly in line with that the Minister announced in the Budget, however there were a couple of key changes. A reduced rate of 4% will apply to income over €16,016 where the individual holds a medical card or is aged 70 or over at any time in the relevant tax year. In addition, for the self-employed there is a new higher rate of 10% for income over €100,000. This new higher rate does not however apply to the self-employed aged 70 or over, to which the 7% rate still applies for income over €100,000. These additional changes are not intended to be permanent and shall not apply for tax years 2015 onwards.

## Payment date for self-assessed income tax

The proposed changes (contained in the first draft of the Finance Bill) in relation to the payment date for self-assessed income tax and return deadline for income tax returns have been dropped. Therefore, the pay and file date for self-assessed taxpayers remains 31 October, with a small extension for those taxpayers paying and filing online using the Revenue On-line System (ROS).

## Bankers bonus tax

As previously promised by the Minister, the Act contained provisions for a new special punitive tax on bonuses paid to certain employees of financial institutions covered by the Government guarantee for the banking sector (i.e. Eligible Liabilities Guarantee Scheme).

Essentially the tax increases the USC to 45% on performance related bonuses of over €20,000 paid to relevant employees of the covered financial institutions. When combined with the marginal rate of income tax (currently 41%) and PRSI (up to 4%) this potentially increases the rate of tax on such bonuses to 90%.

## Key Contacts

ByrneWallace is one of Ireland's largest law firms and advises in relation to all aspects of taxation. For further information please contact one of the following:



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