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Income Tax, Social Welfare & PRSI

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- Reform of the PRSI contribution system
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Income tax system

The Report strongly recommends a move towards a single system which collects tax on income. Overall the Report seems to favour a flat income tax structure, with few allowances and tax credits as evidenced by the number of tax credits and exemptions recommended to be discontinued. Such a system is usually easier to administer and generally gives rise to fewer tax induced distortions and unclaimed tax credits than other systems.

The Report recognises the merits of a three rate income tax structure, provided

taxes on labour are kept low and marginal rates remain competitive. The report envisages the third rate being used to adjust the tax rates upward as well as downward, as required.

While most employers are likely to welcome a simplified system, which combines the four current systems (PAYE, PRSI, health levy and income levy) and cuts down on payroll administration costs, they will obviously have concerns that such a move is likely to give rise to an increase in the standard rate of income tax, particularly if the main personal tax credits remain at the current levels.

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Reform of the PRSI contribution system

The Commission are proposing significant changes to the PRSI contribution system. Their proposals include:

- Removal of the salary cap (currently €75,037) on employee PRSI contributions.
- Moving to a single rate of PRSI for both employee and self-employed personal contributions.
- Extending PRSI and the health levy to share based remuneration such as unapproved stock options and share awards, which could result in an incremental cost of up to 9% for employees, and 10.75% for employers.
- Extending PRSI, health levy and the income levy to appropriation under an approved profit sharing scheme (APSS) and gains arising under approved Save As You Earn (SAYE) option schemes.
- Removal of the exemption from PRSI on investment income for employees, which again could result in an incremental cost of up to 8%.

- The abolition of the National Training Fund Levy.
- Allowing relief for trading losses in calculating PRSI liability (subject to a minimum contribution being payable).

The general thrust of these proposals will add significant additional PRSI costs to both individual taxpayers and employers. The Commission, however also recommends that the menu of proposals be seen as a package and any increase in PRSI be matched by a reduction in taxes on labour.

Given the financial costs associated with these proposed reforms, individual taxpayers should consider the following:

- Ensure that any income earned prior to these proposals becoming effective (potentially 1 January 2010) is paid in advance of that date.
- Review how these changes will affect any unexercised stock options, and consider if there is any financial merit in exercising in advance of any changes.

Employers should also:

- Consider how these proposed changes will effect the cost of operating share based remuneration schemes; and
- Review their internal systems in order to ensure that they will be capable of extracting the relevant information required to calculate any future PRSI liability.

If the proposed changes were to apply to all unexercised share options and unvested share awards from the effective date, employers could find that they have significant additional employer PRSI costs which they have not accrued for to date. As such, these changes could have significant implications on their current year profit and loss account.

Tax relief for re-training and up-skilling

While the Report recommends discontinuing or restricting a number of tax credits and reliefs it specifically recommends introducing a measure of tax relief for unemployed persons. Currently an employer may meet costs of up to €5,000, where an employee

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who has been made redundant re-trains or up-skills, without triggering a tax charge. The Commission recommends that individuals who are unemployed should be entitled to off-set any re-training costs they incur against income, subject to an annual limit, for the previous six years. This relief is likely to be similar to the seed capital scheme available to unemployed individuals who start up their own companies.

Residence rules

There has been much speculation in relation to Ireland's tax residence rules over the past year or so. Under current rules an individual is regarded as tax resident in Ireland if present in the State for 183 days or more in that year, or 280 days or more in that year and the preceding year combined. Since 1 January 2009 an individual is regarded as present in the State for a day if present at any time during that day (previously it was presence at midnight). Therefore it is possible to spend up to 139 days per annum in

Ireland without triggering tax residence, provided the aggregate limit of 280 days over two years is not breached.

In seeking to ensure consistency with other jurisdictions and taking account of the OECD model tax treaty, the report recommends that the current rules for determining tax residence of Irish citizens is supplemented by a permanent home and centre of vital interest test. This is likely to have a significant impact on certain individuals who could fall to be regarded as resident under the new rules, or who may have to make significant changes to their links to Ireland to continue to be regarded as non-resident.

Arising from the suggested changes to the residence rules, the Report recommends that the rule that allows an individual, who has made a gift of property to Ireland, to be regarded as neither resident nor ordinarily resident in Ireland despite being present in Ireland for significant periods of time to be discontinued.

Remittance basis & attracting key skills to Ireland

The remittance basis of taxation currently provides favourable tax treatment to individuals resident in Ireland who are not domiciled in Ireland or are Irish citizens not ordinarily resident in Ireland, in respect of income and capital gains arising outside Ireland.

While Irish tax (PAYE) applies to the earnings from a foreign employment exercised in Ireland, under the remittance basis non-Irish income and gains have not heretofore been liable to Irish tax; and this has been a significant benefit in attracting senior executives, and specialists with key skills, to Ireland.

The Report proposes the withdrawal of the remittance basis of assessment. It acknowledges that this is a significant change in the tax system, and recommends that there should be a lead time of three to five years before any changes takes effect.

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The removal of the remittance basis would bring both income from foreign employment duties carried on abroad, and non-employment income and capital gains of such non-domiciled individuals working in Ireland within the Irish tax net. This would make Ireland significantly less attractive as an investment location as senior international executives and other key skilled individuals would be less inclined to work here.

The Commission acknowledges the need for incentives to attract individuals with key skills to Ireland, and proposes that a rather restricted existing scheme be discontinued and replaced with a targeted skills based scheme, under which a tax deduction of 25% of the individual's total income (subject to a maximum deduction of €62,500) would be available.

As a standalone measure, this is likely to be inadequate in attracting such key talent to Ireland in the absence of the remittance basis, and is unlikely to be a substitute for the retention of same.

Refundable tax credits

A number of countries, including the US and Canada, operate a system which refunds tax credits where the individual does not have sufficient income liable to tax to use all his/her tax credits.

Currently in Ireland only mortgage interest relief and medical insurance relief, where relief is provided at source, are available where the individual is not liable to Irish tax.

The Commission did not recommend a move to refundable credits at this stage, and suggests that such a move should only be considered as a policy option if there is not an appropriate level of uptake of direct expenditure supports e.g. Family Income Supplement over a 5 year period.

Cap on tax-free ex-gratia termination payments

Following on from their proposal to cap the maximum tax-free lump sum which an individual can claim from a pension fund, the Commission have also recommended that a cap of €200,000

should apply to the maximum tax-free ex-gratia termination payment an individual can receive.

Taxation of social welfare

The report recognises that all income should be taxed equally and on this basis social welfare payments should be subject to tax. In addition the fact that some social welfare payments are not taxable is seen as a disincentive to work. However the report recommends that specific exemption from income tax should be available for Family Income Supplement, Domiciliary Care Allowance and the Respite Care Grant, while the taxation status of maternity benefit, adoptive benefit and health and safety benefit should remain unchanged.

Health levy

The Report contains some interesting comments and recommendations regarding the health levy. The Commission have recognised that the health levy, which applies at rates of between 4% and 5%, now equates to a tax and have recommended that it

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be merged into the tax system when economic conditions improve.

Should this proposal be enacted, it would greatly simplify the current PRSI system as it would eliminate the need for sub classes, meaning the system would be streamlined and much easier to understand. It would however mean that the current exemption from the health levy for specific groups of individuals (persons age 70 or over, low paid employees, medical card holds etc) would be lost.

Approved Share Option Schemes (ASOS)

The Commission have recommended the removal of the current income tax exemption on option gains realised on share options granted under an ASOS.

Save As You Earn (SAYE) share option schemes

The Commission have recommended that the current SAYE provisions be amended in order to allow Employee Stock Purchase Plans (ESPP) to benefit from the income tax exemption available under the SAYE provisions.

Employee tax credit

Whilst recognising the significant cost implications of their proposal, the Commission have recommended the reconstitution of the current employee tax credit as an earned income tax credit, which should be made available to propriety directors and self-employed individuals on a phased basis.

Tax relief for charitable donations

The Commission are proposing that all tax relief on charitable donations will be made directly to charities and be restricted to the standard rate of tax. They have also proposed that the minimum donation which qualifies should be reduced from €250 to €100, and a cap of €500,000 be introduced for both individuals and corporates, from which the charity can benefit.

Child benefit

Currently child benefit is exempt from tax which means that the payment is worth more to individuals liable to tax at the higher rate than those liable at the standard rate or indeed outside the tax net. In order to address this anomaly the Commission suggest

that child benefit should be taxable; however the Report also recommends that this should be benchmarked against alternatives such as means testing.

The report concludes that if a decision is made to tax child benefit then a child tax credit should be introduced to ensure those liable to tax at the standard rate or those currently outside the tax net are not adversely impacted.

Artists' exemption

The report recommends that the artists' exemption should be discontinued and that income averaging should be introduced as the method of taxing creative work. This is to take account of the time an artist might spend in creating an original work.

It is interesting to note that the Report recommends that sportperson's relief be retained, albeit subject to review and amendment. This is based on the economic activity generated by sporting events, and the relatively modest costs involved.

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Tax credit/relief	Recommendation to discontinue	Recommendation to continue	Recommendation to amend/restrict
Single persons tax credit		○	
Married persons tax credit		○	
Single parents tax credit			○
Dependent relative tax credit	○		
Blind persons tax credit	○		
Age tax credit		○	
Age tax low income exemptions		○	
Incapacitated persons – employment of a carer allowance			○
Employee tax credit			○
Relief of union subscriptions	○		
Film investment scheme		○	
Business expansion scheme		○	
BIK exemption of certain employer provided personal security			○
BIK exemption on travel Passes		○	
Exemption on scholarships		○	
Income tax artists exemption	○		
Income tax sports persons exemption			○
Seafarers tax credit	○		
Tax exemption on certain allowances to members of the Oireachtas	○		
Income tax exemption on payments under Scéim na Bhfaghlaimeóirí Gaeilge	○		
Tax exemption for credit unions		○	
Annual exemption for credit union dividends on special term accounts		○	
Income tax relief on certain deeds of covenant		○	
Income tax exemption on certain war pensions		○	
Income tax relief for certain long term unemployed and double corporation tax deduction in respect of the payroll costs associated with employing such individuals		○	
Relief for certain third level fees		○	
Tax exemption of statutory redundancy payments		○	
Relief on certain ex-gratia termination payments			○

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Relief for certain retraining costs on redundancy		○	
Tax exemption on job seekers benefit paid to systematic short term workers	○		
Income tax relief for compensation payments for loss of future earnings		○	
PRSI and health levy exemption on option gains	○		
PRSI, health levy and income levy relief on approved SAYE & APSS schemes	○		
Income tax relief under the ESOT provisions		○	
Income tax relief under the approved share option provisions	○		
Income tax relief for the purchase of new shares in their employer company by an employee	○		
Relief for certain training courses		○	
Home carers tax credit		○	
Income tax exemption on certain social welfare benefits including child benefit	○		
Income tax exemption on foster care payments		○	
BIK exemption on employer provided childcare	○		
Income tax relief under the rent a room scheme	○		
Income tax relief on local authority service charges	○		
Income tax relief on rent paid for private rented accommodation	○		
Mortgage interest relief			○
Medical expenses relief for nursing home expenses	○		
Relief for PHI contributions		○	
Relief for private medical insurance			○
Relief for long-term care policies	○		
Incapacitated child tax credit	○		
Payment of tax by donations of certain heritage items			○
CGT exemption for certain works of art on public display			○
Income tax relief for expenditure on certain heritage properties and gardens	○		
BIK exemption on employer provided art objects displayed in a heritage building or garden	○		
Income tax relief on certain charitable donations			○
Income tax relief on certain donations to sports bodies			○
Tax exemption on lotteries		○	

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The Global Tax Monitor recognises PricewaterhouseCoopers as one of the leading firms in Ireland for tax advice by reputation.

These results are based on the year-ending Q2 2009 figures, with a sample size of 100 primary buyers of tax advice in Ireland.

Launched in 2000, the Global Tax Monitor (GTM) is a multi-client independent survey conducted by research agency TNS, that examines the competitive position of the top firms in the tax advisory market - globally, regionally, nationally and on an industry basis. It provides a comprehensive measure of firm reputation, client service and brand health, gained currently from just over 3,000 telephone interviews annually with key decision makers (CFOs and Tax Directors) in 31 key markets.

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