



Tax Matters – Pre-Budget

Welcome to the
September 2010
edition of Tax Matters.

Introduction

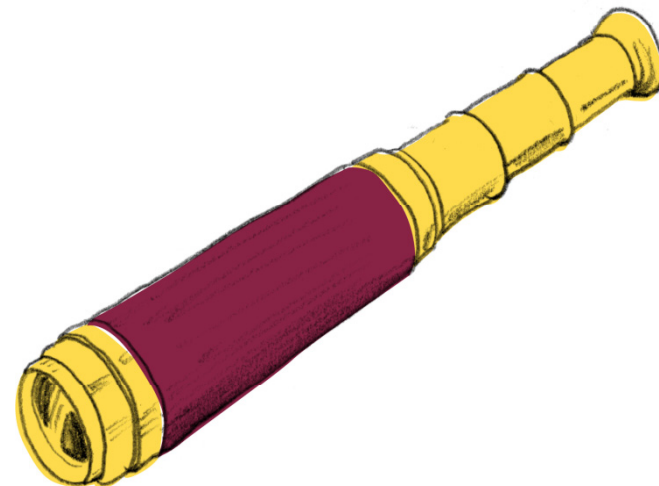
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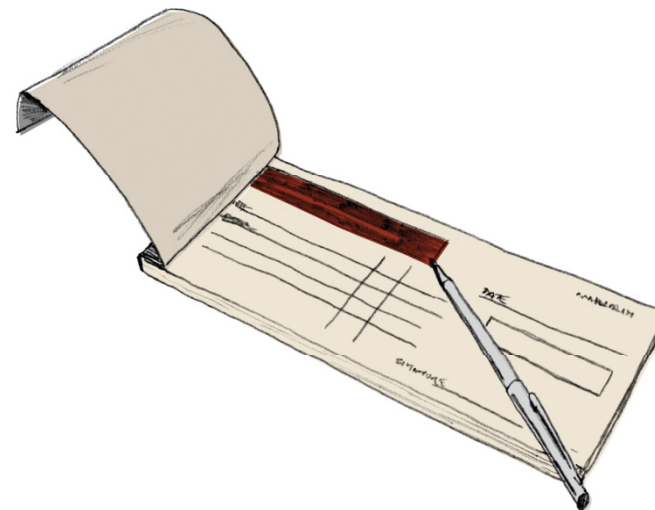
Introduction

The Minister for Finance, Brian Lenihan has announced that the date for Budget 2011 has been set for Tuesday 7 December 2010. Recent suggestions are that the Government may deliver more than the promised €3 billion savings in the Budget.

If Mr Lenihan sticks to the €3 billion figure, the December 7 Budget could be made up of €1 billion in capital spending reductions, €1 billion in current spending (probably social welfare related) and €1 billion in revenue raising measures. Revenue raising measures could include a broadening of the tax base, an

increase in the higher rate of tax, the introduction of water charges, higher excise duties, higher carbon taxes and possibly even the introduction of a property tax.

Tough austerity measures in this Budget could do more harm than good to the economy unless the Minister also announces a stimulus package for consumers. It seems likely that certain tax changes which have already been signalled will be included in this Budget and some of these are featured in this edition of Tax Matters.



Possible restriction of certain tax reliefs

The Commission on Taxation report which issued in September 2009, made a number of recommendations in relation to capital taxes and reliefs, including the following:

- Business Asset Relief (BAR) to be reduced from 90% to 75% and subject to a maximum relief claim of €3 million. Currently the relief is 90% of the value of the assets with no cap on the value; and
- retirement relief on disposals to children to be capped at an asset value of €3 million. Where the values of the assets exceed €3 million, the excess would be subject to Capital Gains Tax (CGT). Currently there is no cap on the value which can be transferred tax free.

In addition the Taoiseach, Brian Cowen, recently reiterated the Government's intention to focus on taxes on capital rather than income as a way of boosting employment prospects. It is quite possible that the CGT and CAT rate of 25% could be increased in the next budget and some of the Commissions proposals above implemented.

Any business owner who is considering passing the business to the next generation needs to be aware that the aforementioned changes are likely to be introduced. Accordingly **now** is the time to act on such plans as the cost of delaying the transfer of a business could be significantly higher post December. Current low asset values are another valid reason to proceed with such plans.

Many business owners are concerned at the prospect of handing over full control of adult children who, while employed in the business, may not yet have sufficient experience. It is usually possible to make arrangements to deal with these concerns.



Pension changes

The Government set out its intentions in relation to pensions with the publication of the Pensions Framework document on 3 March 2010. Among the ideas flagged at that time were the restrictions of tax relief on personal pension contributions, capping tax free lump sums at €200,000 on commutation of pensions and an increase in the state pension age.

These proposals combined with the introduction of the earnings cap for pension contributions with effect from 1 January 2009 means that it is imperative that all individuals conduct a review of their pension arrangements as soon as possible.

Much of the media speculation surrounding the restriction of the tax relief on pension contributions concerns the rate

at which tax relief will be granted to an individual in respect of future personal contributions. Currently taxpayers obtain a tax deduction for the contribution made at their marginal rate of tax e.g. 41% or 20%. It seems likely that post Budget 2011 tax relief will be confined to a specified rate higher than the present standard rate of tax (20%) but lower than the current top rate (41%). A rate of 33% has been speculated on. Those individuals currently paying tax at the top rate will therefore see a net increase in the cost of funding for their retirement.

Pension contributions made in the current year may be the last opportunity for many people to obtain tax relief at the top income tax rate.

It is worth recalling that premiums paid before 31 October next may be carried back for tax relief purposes to, 2009, subject to the individual's income and age related limits. Tax relief at 41% is available in respect of contributions claimed in that way. Similarly, qualifying payments made before Budget day this year in respect of 2010 will still be available for tax relief at 41%.

In general terms all individuals with pension funds have a right to commute a portion of their pension fund at normal retirement date and take a tax free lump sum. The quantum of that sum varies depending on the type of pension scheme. Typically the lump sum is 25% of the accumulated fund or 1.5 times final salary.



Should the proposed cap of €200,000 be imposed, individuals with pension funds in excess of €800,000 or with salaries of €133,500 p.a. would see their entitlement to the expected tax free lump sum curtailed. Anyone with a concern over their lump sum pension entitlements should contact their Grant Thornton advisor to explore the options available to them.

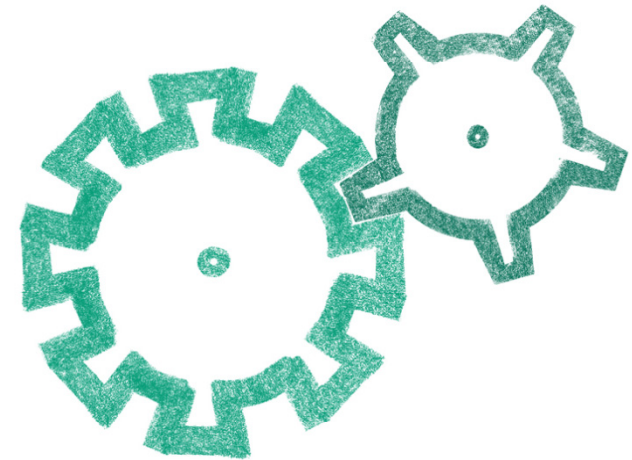
Universal social insurance

The current system of Pay Related Social Insurance (PRSI) has long been regarded as cumbersome and difficult to administer. In last December's budget speech a new Universal Social Contribution (USC) was mooted as a replacement for PRSI which would also combine the health levy and the income levy. It is anticipated that the system will be effective from 1 January 2011 and the details should be provided in December's Budget.

Among the expected changes are the abolition of the employee contribution ceiling (currently €75,036), a harmonisation of the contribution rate paid by employees and the self-employed and possibly an extension of the charge to other

sources of income, including rental income, investments and share options (unearned income). Presently those paying self-employed PRSI make contributions on their unearned income through the self-assessment system. This is in contrast to employees in receipt of unearned income for whom the PAYE system does not provide a mechanism for assessing PRSI on such income. The scope of the new system is likely to be extended to include those with earnings below €352 per week, and may also modify the employer contributions required in such instances.

One of the difficulties under the current system is the classification of PRSI for company directors.



Many directors, in particular those with a shareholding in the company, may be paying PRSI at the incorrect contribution class. In anticipation of the introduction of the new system we would suggest that employers review their current payroll records, including employment contracts, to determine that the correct class of PRSI is presently being operated on all salary payments. This should ensure an orderly transition to the new system.

Current tax issues

Foreign property

The Revenue are currently looking at disposals of foreign property both in relation to any possible capital gains tax arising on sale and also in relation to whether the owner had declared the funds used for the original acquisition as well as any rental income arising during ownership. Revenue are working with property agents in locations such as France, Spain and Portugal in connection with this project and of course Revenue can access details with foreign taxation authorities.

Spanish property disposals

The Spanish Revenue have set next month as the deadline for reclaiming Spanish capital gains tax overpaid on disposals of Spanish property made prior to 31 December 2006.

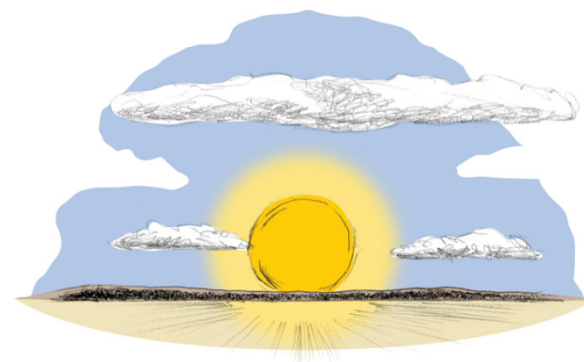
These overpayments arose due to the Spanish rules where non residents were taxed at a higher rate than locals.

Where the disposal took place before 2007 foreign owners paid at a rate of 35% while Spanish residents only paid 15%. In 2009 the European Court of Justice ruled that this was illegal and as a result it should now be possible to recover Spanish tax overpaid together with interest at the rate of 6% p.a.

Remittance basis of taxation and UK income/gains

The 2008 Finance Act introduced a change whereby UK income arising after 1 January 2008 qualifies for the remittance basis of taxation.

Following a recent appeal case, Revenue will now allow this basis (subject to a four year time limit) where refunds would apply if such a basis was available for years prior to 2008. Claims will be examined on a case by case basis.



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