TSG 10/05

TAX STRATEGY GROUP

Capital and Savings Taxation Issues

1. Introduction and context

1.1 Scope of this paper

This paper covers a range of Capital Taxes, including Capital Gains Tax (CGT), Capital Acquisitions Tax (CAT), certain Stamp Duties (those covering financial cards and financial instruments), taxes on savings (DIRT) and the Domicile Levy. It sets out the current position for each of the main areas and examines issues that have been raised, or are likely to arise, in the context of the Budget/Finance Bill 2011, including recommendations made by the Commission on Taxation.

Stamp Duty on property is covered in a separate paper on the Taxation of Property to be considered by the TSG at a later stage.

1.2 Programme for Government

An Agreed Programme for Government 2007 – 2012 and the *Renewed Programme for Government* set out guiding principles for economic and fiscal policy for the lifetime of the Government, including a key commitment, detailed in Appendix I, which has underpinned policy development in relation to Capital Taxation.

This commitment to secure "A Fair Tax System" by keeping low income earners out of the standard rate band and average earners out of the higher band has informed the development of base-broadening measures in recent Budgets to shift the burden of tax from labour and consumption to wealth and sources of wealth.

1.3 Commission on Taxation

The Commission on Taxation recommended a number of options in regard to capital and savings taxes which are detailed in Appendix II. The most significant are:

- <u>Capital Gains Tax (CGT)</u>
- – Gains attributable to inflation should be excluded (i.e. reintroduce indexation)
- – Rollover relief should apply to the gains on disposal of farm land pursuant to a compulsory purchase order where the proceeds are re-invested in farm land
- – Continue the exemption on the disposal of a principal private residence.
- – Discontinue the exemptions (in both CGT and Stamp Duty) on the disposal of site to a child.
- – Relief for disposal of a business or a farm on retirement should continue.
- – The tax treatment of venture fund managers should be modified such that in the case of an individual who is a venture capital fund manager:
    - – Where the investment return on a carried interest represents income, it should be taxed at the appropriate marginal rate, and
    - – Where the investment return on a carried interest is a capital gain, it should be subject to capital gains tax at the normal rate (25%).
- – The remittance basis of taxation for income tax and capital gains tax should be discontinued.

- Capital Acquisitions Tax (CAT)
  - For business relief for CAT, a reduction of no more than 75% of the value of the business should be allowed before tax is calculated. The reduction should be subject to an overall monetary limit of €3 million.
  - For agricultural relief for CAT, a reduction of no more than 75% of the value of the business should be allowed before tax is calculated. The reduction should be subject to an overall monetary limit of €3 million. A condition of the relief should be that a farm asset is owned and operated as a farm for a period of six years after the transfer.
  - The annual exemptions for interest and dividends on special term accounts and special term share accounts should be continued.

- Stamp Duty on financial transactions
  - Stamp duty on ATM, credit and debit cards should be phased out in the interest of promoting the move towards a cash-free society

- Stamp Duty on shares
  - Stamp duty on all share transactions should be reduced to zero.

2. Capital Gains Tax

2.1 Introduction

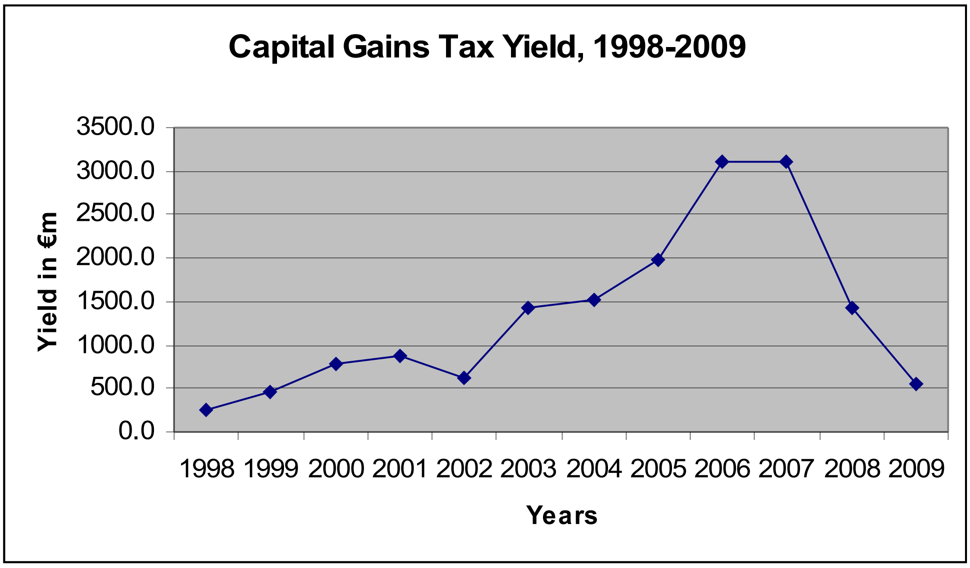
Capital Gains Tax (CGT) was introduced in the Capital Gains Tax Act 1975 in respect of disposals made during the tax year 1974/75. The tax is charged on the value of the capital gain of an asset when that asset is disposed. All classes of assets are covered by CGT, but the majority of the yield relates to property.

2.2 Evolution of CGT

- 1975 – CGT at a rate of 26% was introduced
- 1978 - 1990 – indexation relief introduced and rates periodically reformed.
- 1991 – CGT brought within self-assessment system.
- 1992 – multiple rate system (based on how long the asset was held) changed to a single rate of 40%.
- 1998 – single 20% rate introduced.
- 2003 – abolition of indexation relief, change in the CGT payment date to current year, and the abolition of roll-over relief.
- 2008 – Budget 2009 rate increase from 20% to 22%
- 2009 – Supplementary Budget 2009 rate increase from 22% to 25%

2.3 CGT Yield

The amount of (CGT) received for each year since 1998 is shown below.



The CGT yield in 2009 was €544.7m, down from €1,430m in 2008 – a fall of €885.3m (62%). The yield for the six months to 30 June 2010 was €107m and is projected at €340 million for 2010, almost €200m (38%) less than the 2009 outturn. The main payment date for CGT is in December.

The recent drop in the CGT yield can be attributed to declining asset values and a reduction in the number of property and share transactions. Given the likely continuation of this trend, or at best, a maintenance of current values and low transaction figures, there is little chance of an improvement in the CGT yield in the short to medium term as the tax is currently structured.

2.4 CGT Exemptions and Reliefs

The main exemptions and reliefs from CGT are as follows:

- Annual exemption
  An annual CGT exemption of €1,270 for to all assets disposed of in a calendar year by an individual.

- Principal Private Residence Relief
  An individual's principal private residence is exempt from CGT. Where the individual resides in the property for part of the duration of ownership, the relief is apportioned accordingly.

- Retirement Relief
  Business or farming assets are relieved from CGT where the person disposing of the assets is aged 55 or over and had owned and used the asset for the ten years prior to disposal. The relief applies to assets valued up to €750,000. Where the disposal is made to a child or favourite niece/nephew, there is no monetary limit to the relief.

- Remittance basis
  Individuals who are resident or ordinarily resident, but not domiciled in Ireland (that is, for whom Ireland is not their permanent home), are liable to tax on foreign capital gains only to the extent that the proceeds are remitted or brought into Ireland.

The most significant reliefs are the Principal Private Residence Relief and the Retirement Relief. The Commission estimated that the Principal Private Residence Relief cost €2.44bn based on 47,340 people benefitting in 2006. While costs are currently not available for Retirement Relief, they are likely to be significant.

2.5 **Capital Gains Tax issues - Budget/Finance Act 2010**

Given the limited taxation elements to Budget 2010 which focussed on expenditure, there were no CGT measures. However, Finance Act 2010 contained a number of CGT provisions, three of which were provisions to counter anti-avoidance schemes/ practices. The most important measures included: (i) Contrived Capital Losses – an anti-avoidance provision countering the creation of an artificial loss for CGT purposes; and (ii) Compulsory Purchase Orders – change of liable date to when the CPO compensation proceeds are received. It can be anticipated that Budget/Finance Bill 2011 are likely to continue to tackle avoidance schemes.

The NAMA Act introduced a "windfall tax" on profits or gains from the disposal of development land. A rate of 80% applies to the portion of any gain made on the disposal of land which is attributable to a decision by the local authority after 30 October 2009 to rezone the land.

The rationale for the tax is that this portion of the gain is attributable to the decision by the local authority rather than to anything done by the landowner. The balance of the gain is taxable at the normal CGT rate, if the land is disposal is treated as a capital gain, or at the appropriate Income Tax /Corporation Tax rates, if the disposal is part of a trade of dealing in or developing land. Finance Act 2010 extended the windfall rate to the portion of gains attributable to a "material contravention" decision by a local authority after 4 February 2010 and confirmed that disposals of land not exceeding an acre in size and €250,000 in value would not be subject to the windfall rate (unless the disposal was part of a larger transaction or series of transactions).

2.6 **Possible Capital Gains Tax issues - Budget/Finance Act 2011**

In the context of Budget/Finance Act 2011, a number of CGT issues can be identified for consideration:

(i) increase CGT yield by increasing the rate

- Rate increase from the existing 25% level
- Increase CGT rate for higher rate income tax payers
- Re-introduce multiple rates
- Relate rates to the value of the assets disposed

(ii) broaden the base for CGT by abolishing or restricting existing reliefs/exemptions

- Abolish/amend the annual CGT exemption of €1,270
- Abolish/amend the Principal Private Residence Relief
- Abolish/amend the Retirement relief

(iii) restructuring the CGT regime to support enterprise and investment.

- Re-introduce indexation (inflation) relief
- Re-introduce "roll-over relief" for farm CPOs

(i) Options for increasing CGT

A number of options can be identified for increasing the yield from CGT by increasing rates. In recent years, there have been a number of such changes:

- Budget 2008: increase in the rate from 20% to 22%
- Supplementary Budget 2009: increase in the rate from 22% to 25%

The rate increase in Budget 2008 was the first rate change since Budget 1998 when the rate was decreased from 40% to 20%. Any consideration of changing the CGT rates has to be considered within the overall context of taxation policy for Budget 2011 and, in particular, the balance between taxes on employment/employment creation (i.e. Income and Corporation Taxes) and taxes on capital/wealth such as CGT. The potential impact behavioural of a rate change on the owners of assets subject to CGT on disposal is also a factor.

In addition, the linkage between the various capital and savings taxes which are all currently at 25% and the 25% 'gap' between the 20% standard Income Tax rate and the 25% rate for capital/savings taxes have to be recognised. As a result, any change to the CGT rate should also be reflected in increases to the CAT and DIRT rates; further, there is an argument that the 25% 'gap' should be maintained between these rates and the standard Income Tax rate.

Apart from a straight-forward rate increase aimed to secure a higher CGT yield, there are a number of other possible options for increasing CGT yield:

- Increase CGT rate for higher rate income tax payers
  The new UK Government has increased the CGT rate for higher rate income tax payers from 18% to 28%. A similar measure could be introduced here. It is estimated that c. 70% of individuals declaring capital gains are higher rate income tax payers, so a similar measure would increase the CGT yield from this cohort.

- Re-introduce multiple rates
  Up to 1992, the CGT rate reduced for assets which were held for a longer period. A similar system is currently in place in the USA – assets held for a short period are taxable at income tax rates, whereas assets held for longer periods are taxed at a reduced rate. This system would encourage longer term investment. Consideration could be given to re-introducing a multiple rate system on this basis.

- Rates related to value of the assets disposed
  Consideration could be given to introducing a higher rate or higher rates of CGT on disposals over a certain amount.

(ii) Abolition/amendment of reliefs/exemptions

Although the abolition/amendment of the current CGT reliefs/exemptions would undoubtedly give rise to an increased yield, there would be difficulties in putting these options in place especially in regard to the Principal Private Residence Relief and Retirement Relief.

(iii) Restructuring the CGT regime to support enterprise and investment

There are two possible ways of restructuring the CGT regime as a means of supporting enterprise and investment: re-introduction of indexation (inflation) relief and re-introduction of "roll-over relief" for farm CPOs. Both were considered in depth by the Commission on Taxation, which supported their reintroduction, and they are covered in pre-Budget submissions from various interest groups.

- Re-introduce indexation (inflation) relief
  The Commission on Taxation recommended the re-introduction of indexation relief – this seeks to limit CGT to 'real' gains in asset values by excluding the impact of inflation as measured by the Consumer Price Index (CPI). Indexation (excluding gains attributable to inflation) was brought in a number of years after the introduction of CGT in 1975 to take account of high levels of inflation when CGT rates were relatively high. With a marked decline in inflation, and in light of the reduced standard rate of CGT, the relief was abolished in 2003 but still can be claimed for allowable expenditure incurred up to 31 December 2002.

  Any consideration of the case for the re-introduction of indexation would have to consider the current low rates of inflation and the fact that other jurisdictions do not exclude inflation from capital gains. In addition, the cost associated with introducing indexation relief would adversely affect the CGT yield.

- Re-introduce "roll-over relief" for farm CPOs
  "Roll-over relief" (under which the CGT payable on the proceeds of a gain was deferred if the proceeds were reinvested with the result that the tax liability is not realised until the assets are eventually sold) was abolished in 2003 for all disposals, including disposals as a result of a compulsory purchase order.

  The Commission on Taxation has recommended that it be re-instated for the purchase of farmland using an award made under a Compulsory Purchase Order (CPO). The rationale appears to be that it would enable farmers to consolidate their holdings and re-invest the proceeds from a CPO into productive economic activities rather than simply investing in a financial institution.

  However, if conceded, this change may lead to added pressure for the general re-introduction of roll-over relief for the business and agricultural sectors in the context of transfers of assets. This was not recommended by the Commission and would be extremely expensive. It was also the case that gains which were deferred under roll-over relief were often never taxed.

3. Capital Acquisitions Tax (CAT)

3.1 **Introduction**

The Capital Acquisitions Tax (CAT) code includes gift tax, inheritance tax and discretionary trust tax. It was first introduced in 1976 when it replaced estate duty taxation.

The tax is charged on the amount gifted to, or inherited by, the donee (the person receiving the gift/inheritance). There is a tax-free threshold (referred to as a 'group threshold'), depending on the relationship between the disponer (the person making the gift/leaving the inheritance) and the donee. Previous gifts/inheritances since 1991 from other disponers in the relevant group are counted when calculating the taxable amount over the threshold. The balance of the gift/inheritance above the threshold is taxable, currently at a single rate of 25%. On an annual basis, the tax-free thresholds are adjusted in line with movements in the Consumer Price Index (CPI). The group thresholds are set out below.

CAT Group tax-free thresholds 2009 and 2010

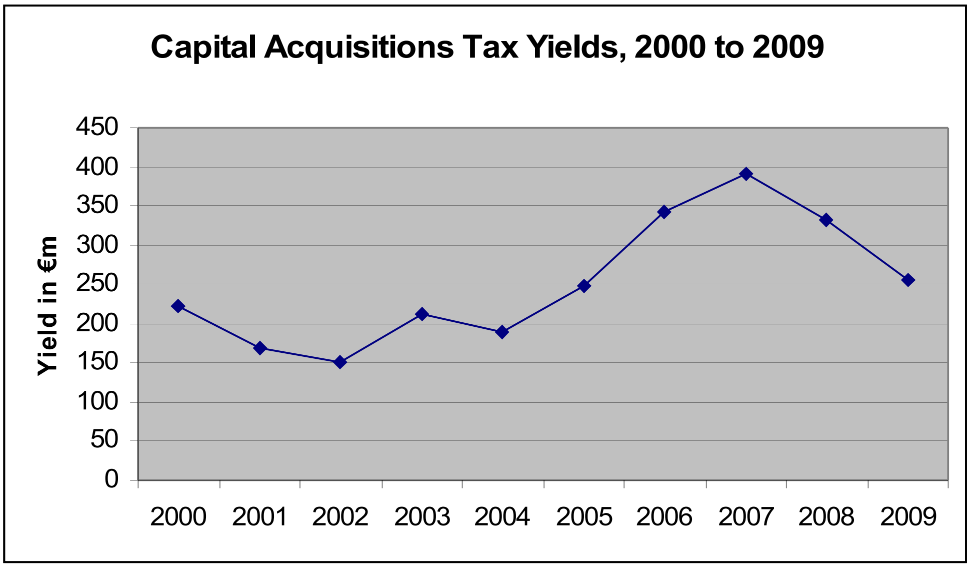
Group	Relationship of donee to disponer	1 January to 7 April 2009	8 April to 31 December 2009	2010
A	Son/Daughter	€542,544	€434,000	€414,799
B	Parent*/Brother/Sister/ Niece/Nephew/Grandchild	€54,254	€43,400	€41,481
C	Relationship other than Group A or B	€27,127	€21,700	€20,740

* In certain circumstances, a parent taking an inheritance from a child can qualify for Group A threshold.

Finance Act 2009 saw, for the first time, a reduction of approximately 20% in the tax-free threshold amounts for all groups reflecting a general fall in asset values. This measure was coupled with an increase in the rate to 25% (from 22%, which was raised in Finance (No. 2) Act 2008 from 20%).

The CAT yield for January to June 2009 has fallen by over 30% compared to the yield for the same period in 2008. As the CAT yield arises mainly from inheritances / gifts, any reduction in the yield can be mainly attributable to decreasing asset values, particularly the decline in property values. In 2010, the tax free thresholds fell by approximately 4.4%, in line with the decline in the CPI. There were no changes to the rates and thresholds in Budget 2010. Given the current forecast of 1% for CPI at end-year, it is likely that the thresholds will increase by this small amount.

The CAT yield for each year since 2000, the first full year since the introduction of the single CAT rate and revision of tax-free thresholds, is as follows:



The CAT yield was €255.6 m in 2009 (down €84.4m or 25% from the yield of €340m for 2008) and €130.5 m for the first six months of 2010. The projected CAT yield for 2010 is €240 m, this is some 6% lower than the 2009 outturn.

Receipts from CAT are generally not characterised by dramatic fluctuations given that its nature and application, in the main, to inheritances which gives rise to a steady yield impacted only by changes in asset values which has marked the tax since 2008. Given the likely continuation of this trend, or at best, maintenance of the current asset values, there is little chance of an improvement in the CAT yield in the short to medium term as the tax is currently structured.

3.2 **Evolution of CAT**

- 1980 – Agricultural relief introduced.
- 1994 - CAT payable at 20% on first IR£10,000 above tax-free threshold, 30% on next IR£30,000 and 40% on the balance.
- 1994 – Business property relief introduced.
- 1995 – Agricultural and business property relief set at 50% of the taxable value of the relevant assets (previously the rates varied depending on the value of the assets received and the nature of the asset)
- 1996 - Agricultural relief and business property relief increased to 75% of the taxable value of the relevant assets
- 1997 – Agricultural relief and business property relief increased to 90% of the taxable value of the relevant assets.
- 1999 - CAT tax-free thresholds increased to Group A - IR£300,000 (€380,921); Group B - IR£30,000 (€38,092); and Group C IR£15,000 (€19,046). [NB – the thresholds are linked to the Consumer Price Index and therefore have increased accordingly.]
  Introduction of single CAT rate of 20% on all amounts above tax-free threshold.
- 2008 – Finance (No. 2) Act 2008 increased the rate to 22% on all amounts above the relevant tax-free threshold.
- 2009 - Supplementary Budget 2009 increased the rate to 25% on all amounts above the relevant tax-free thresholds.
  CAT tax-free thresholds reduced by 20%: Group A - €434,000; Group B - €43,400 and Group C - €21,700.
- 2010 – Modernisation of CAT system, including introduction of a single payment date (31 October), removing of secondary liability and mandatory electronic filing where claiming major reliefs.

3.3 **CAT Reliefs/Exemptions**

The main CAT reliefs and exemptions are as follows:

- <u>Small Gifts Exemption</u>
  The CAT code contains an exemption on the first €3,000 of taxable gifts (not inheritances) received in a tax year. This is in addition to the group thresholds which relates to gifts and inheritances received from 1991 to date.

- <u>Dwelling House Exemption</u>
  In addition to the group thresholds, Finance Act 2000 introduced an exemption from CAT for certain dwelling houses. The purpose of the exemption is to benefit individuals who have been living in a house prior to receiving it as a gift or inheritance. The main condition is that the beneficiary has to occupy the dwelling house as his or her only or main residence for three years prior to the gift/inheritance and continue to reside in it for six years

after the gift/inheritance. It is a full exemption without a ceiling or a requirement that the beneficiary has to be related to the disponer.

- <u>CAT Agricultural/Business Relief</u>
  Qualifying farmers and business owners can avail of CAT agricultural/business relief which reduces liability to CAT by 90%. In order to qualify for these reliefs, 80% of the individual's/farmer's assets, after having received the gift/inheritance, must consist of qualifying agricultural/business assets.

3.4 **Possible Capital Acquisition Tax issues - Budget/Finance Act 2011**

In the context of Budget/Finance Act 2011, a number of CAT issues can be identified for consideration:

(i) increase CAT yield by increasing the rate

- Rate increase from the existing 25% level
- Re-introduce 'slicing'

(ii) broaden the base for CAT by abolishing or restricting existing reliefs/exemptions

- Reduce the three tax-free thresholds (Groups)
- Reduce agricultural and business property relief

(i) Options for increasing the CGT rate

In recent years, there have been a number of to the CAT rate which mirror developments for CGT, namely:

- Budget 2008: increase in the rate from 20% to 22%
- Supplementary Budget 2009: increase in the rate from 22% to 25%

The rate increase in Budget 2008 was the first rate change since Budget 1999 when a single 20% rate was introduced on all amounts above the three tax-free thresholds –previously there were different rates for different amounts. As with CGT, any consideration of changing the CAT rates has to be considered within the overall context of taxation policy for Budget 2011 and, in particular, the balance between taxes on employment/employment creation (i.e. Income and Corporation Taxes) and taxes on capital/wealth. The potential impact of a rate change on the owners of assets subject to CAT on disposal is also a factor.

In addition, the linkage between the various capital and savings taxes which are all currently at 25% and the 25% 'gap' between the 20% standard Income Tax rate and the 25% capital/savings rate have to be recognised. As a result, any change to the CAT rate should also ideally be reflected in the CGT and DIRT rates; further, there is an argument that the 25% 'gap' should be maintained especially if the standard Income Tax rate.

Apart from a straight-forward rate increase aimed to secure a higher CGT yield, there are a number of other possible options for increasing CGT yield:

- Reintroduce 'slicing'
  Up to 1999 CAT was payable in "slices", with rates increasing depending on the amount inherited above the tax free thresholds. Consideration could be

given to re-introducing slicing on higher inheritances (for example, 25% on the first €100,000 gifted/inherited over the threshold and a higher rate on greater amounts).

(ii) Options for broadening the CAT base

- Reduce agricultural and business property relief
The Commission on Taxation has recommended reducing these two reliefs from 90% to 75% of the taxable value of the relevant assets; this would increase the yield from CAT. This could be a useful measure in terms of base-broadening and ensuring equity for different classes of taxpayers. However, when combined with the Commission's recommended cap of €3m, it could have a negative impact on the development and growth of family businesses. The Commission has also recommended that the two reliefs be amalgamated by aligning the conditions for availing of the reliefs.

  Alternatively, consideration could be given to providing that an individual could only claim either the CAT tax free threshold or agricultural/business relief in respect of a gift or inheritance, rather than being able to claim both, as is the case at present. This would mean that at least some CAT would be payable on most inheritances/gifts of such agricultural and business property.

- Reduce tax-free thresholds
The CPI is projected to rise by 1% in 2010. This would lead to a minor rise in the current tax-free thresholds. The asset which is most likely to pass by inheritance, property, is likely to fall in value by greater than the CPI increase. Consideration could, therefore, be given to further reducing the tax-free thresholds (for example, Group A to €350,000; Group B to €35,000; and Group C to €17,500).

4. Stamp Duty

4.1 Introduction

Stamp Duty is generally a tax on documents or transactions, which has been in existence since the late-Seventeenth Century. There are a variety of Stamp Duties; some are fixed (e.g., Stamp Duty on credit and debit cards, which is a fixed amount irrespective of how much the card is used), while others are proportional (e.g., Stamp Duty at 1% on the value of shares sold).

The main (non-property) Stamp Duties are:

- Financial Cards (including ATM, credit and debit cards) and cheques
- Insurance Levies
  - Non-Life
  - Life
  - Health Insurance
- Shares

4.2 Stamp Duty on financial cards (Credit, ATM and Debit cards) and cheques

4.2.1 Introduction

The Stamp Duty on cheques, bills of exchange and promissory notes is long-established. When electronic means of money transfer (credit cards, ATM cards and debit cards) were introduced, Stamp Duty was gradually extended to those products to ensure that receipts from paper transactions were not eroded. The current Stamp Duty for each cheque and paper transaction is 50c, increased from 30c in Budget 2009.

The Stamp Duty on credit cards is charged on accounts open at any stage during the year and is payable on 1st April of each year in arrears, or on the date the account is closed. The Stamp Duty on ATM and debit cards is charged on relevant accounts at 31st December each year.

Current stamp duty charges are as follows:

Description	Stamp Duty	Payable
ATM cards	€2.50	31 December each year
Debit cards	€2.50	
Combined ATM/Debit cards	€5	
Credit cards/ Charge cards	€30	1 April in arrears
Cheques	50c	Per cheque

4.2.2. **Yield from financial cards and bills of exchange**

The following table details the yield from stamp duty on financial cards and bills of exchange over recent years:

Year	Yield (€m)
2002	48
2003	100
2004	112
2005	118
2006	121
2007	133
2008	176
2009	116

4.2.3 **Stamp Duty on financial cards and cheques – issues for consideration**

The Stamp Duty yield from financial cards and cheques rose every year between 2002 and 2008, but declined considerably in 2009 – this can be attributed to a decline in the use of financial cards and cheques. The yield to 30 June 2010 was €20 million and it is projected at €115m in the full year.

The Stamp Duty rate for bills of exchange and cheques increased from 30c to 50c from 15 October 2008, while the rate applicable to ATM, debit and combined cards was halved. This measure was introduced to encourage the movement away from these forms of payment towards electronic means of payment.

Consideration may be given to reducing/eliminating Stamp Duty on ATM/debit/combined cards, in line with the Commission on Taxation's recommendations. If considered, this could be balanced by increasing the charge on cheques and Bills of Exchange. However, the increased charge is unlikely to compensate for the reduced Stamp Duty yield from cards, etc.

Consideration could also be given to reducing Stamp Duty on credit cards, in order to facilitate electronic commerce, although this could lead to criticism that the State was encouraging individuals to get into debt via credit cards. No other European country has a Stamp Duty on credit cards, although there is such a duty in Malaysia.

Recently, there have been some initial discussions at EU and IMF/G20 levels on the merits of introducing a Financial Transactions Tax (FAT) which could cover financial transactions undertaken by individuals and businesses. While this is at a very early stage and it will have to be considered at EU Working Group level, there may be implications at some stage for Ireland's Stamp Duty on financial cards and instruments regime.

In light of recent 'tiger' bank robberies, there was some discussion of imposing an ATM charge. Although it was unclear whether this would be charged (and kept) by financial institutions or levied as part of the existing Stamp Duty regime, there would again be implications for the existing Stamp Duty on financial cards and instruments.

4.3 Insurance Levies

4.3.1 Non-Life Insurance Levy

A 2% stamp duty on certain non-life insurance products (for example, house and motor insurance) was introduced in 1982 and it is charged on most non-life insurance premiums. The exceptions are re-insurance, voluntary health insurance, marine, aviation and transit insurance and export credit insurance. Finance Act 2009 increased the rate to 3% for premiums received by an insurer on or after 1 June 2009.

The non-life levy yielded €86.4 million in 2009 and €54.63 million up to 30 June 2010.

4.3.2. Life Assurance Levy

Finance Act 2009 introduced a new levy on life assurance policies at a rate of 1% levy on premiums received by an insurer on or after 1 August 2009. An earlier life assurance levy was in place from 1982 to 1993. After some intensive lobbying from the insurance industry, it was amended in Finance Act 2010 so that it did not apply to life assurance premium income attributable to pension products – new business in the pension sector had declined sharply as a reflection of the general economic situation and some 'switching' of investments to avoid the levy.

It now applies to life assurance protection products (e.g. mortgage protection) and investment products. There are ongoing requests from the industry for additional changes to the levy which will further restrict its nature, thus reducing the yield from this source – this pressure relates to continued business difficulties for this sector and an argument that they are losing business to competitors in the banking sector because customers are not investing in products which would be subject to the levy, but instead putting their money in other investment products.

Consideration could be given to imposing the levy on products which would be in direct competition with life insurance-based investment (such as unit trusts and tracker bonds, which are also subject to similar exit taxes to life insurance products).

Alternatively, consideration could be given to removing the levy from life insurance investment products and imposing it solely on protection products at a rate of 3% - this is the same rate as the non-life insurance levy, which is imposed on products such as motor or home insurance which are analogous to life assurance protection products. This could protect the current yield and prevent any arguments that the life assurance industry was being discriminated against. However, mortgage protection policies would be one product affected (albeit that the actual increase in premium payments would be small) and such an increase could lead to criticism at a time when some people are having difficulties paying their mortgages.

The life levy yielded €8.7 million in 2009 (the levy is paid quarterly and only one payment date arose in 2009) and €30.1 million to June 2010.

4.3.3 Health insurance levy

A levy on health insurance premiums was introduced in the Health Insurance (Miscellaneous Provisions) Act 2009. This levy was designed on a Exchequer-neutral basis because it was introduced to facilitate community rating on health insurance following the judgment in *BUPA Ireland Ltd and another* v *Health Insurance Authority and others* [2008] IESC 42 which struck down the Government's community rating scheme.

The levy is accompanied by a tax relief at source for health insurance policy holders aged 50 and over – this is paid by Revenue to the health insurance companies. The levy was set at €160 for adults and €53 for children covered by the policy in 2009, and at €185 per adult and €55 per child in 2010. The scheme, and a related EU State Aid approval, is predicated on the Department of Health developing a more sustainable policy response to the BUPA judgement which will replace the current temporary scheme.

This health insurance levy yielded €196.9 million in 2009 (in respect of seven months of renewals) and is projected to yield c. €300 million in 2010. It is payable on 30 September in 2010 so there was no yield from this source in the six months to 30 June 2010.

The legislation provides that the levy and TRS are reviewed on an annual basis so that any changes (usually upwards to reflect claims history and costs) can be announced and made in December well in advance of the vast majority of renewals by customers.

The continued cancellation of policies by customers in the context of financial difficulties and, in many cases, unemployment will ensure that the levy will continue to rise in the coming years because higher claim costs will have to be borne by an increasing small number of customers.

4.4 Stamp Duty on share transfers

4 .4.1 Introduction

Under rules laid down by the Department of Enterprise, Trade and Innovation, the only approved operator that can transfer legal title in Irish quoted companies is 'CREST' and all dematerialised shares must be transferred in CREST. Share transfers outside of CREST require a share transfer certificate and this must be stamped by Revenue. Share transfers incur a 1% stamp duty charge and there are exemptions for intermediaries.

4.4.2. **Yield from Stamp Duty on Share Transfers**

The following table details the yield from stamp duty on share transfers over recent years:

Year	Yield (€m)
2002	303
2003	256
2004	261
2005	324
2006	406
2007	609
2008	419
2009	209

The yield in the six months to 30 June 2010 was €88.8 million.

The recent significant declines in the yield from Stamp Duty on shares can be attributed to declining asset values and a reduction in the number of transactions; factors also noted for the decreased yield for CGT and, to a lesser extent, CAT. Given the likely continuation of this trend, or at best, maintenance of the current asset values and low transaction figures, there is little chance of an improvement in the yield from Stamp Duty on shares in the short to medium term.

4.4.3. **Stamp Duty on Share transfers – issue for consideration**

Consideration might be given to reducing/eliminating Stamp Duty on share sales, as recommended by the Commission on Taxation. This change would also be in line with EU intentions on this issue which aim to eliminate all Government charges on shares as a means of encouraging the free flow of capital and investments between Member States. However, the cost would be considerable at over €200m, based on 2009 yields.

5. Deposit Interest Retention Tax (DIRT)

5.1 **Introduction**

Deposit Interest Retention Tax (DIRT) is deducted by Irish financial institutions from deposit interest paid to the accounts of Irish residents. The basic rate is 25% where interest is paid or credited at least once annually (bank accounts) and 28% where it is paid less frequently (life assurance and funds products).

DIRT is a "final liability tax" – that is, it satisfies the individual's full liability to Income Tax in respect of deposit interest, although the individual may still be liable to PRSI and/or the health contribution. Deposit interest subject to DIRT is not subject to the Income Levy. Subject to certain statutory exceptions, financial institutions are required to deduct the tax from interest paid or credited in respect of the income on deposit.

Up to Budget 2009, the rate of DIRT was equal to the standard rate of Income Tax at 20%. In line with policy on capital and savings taxation to shift the burden from labour and consumption to wealth/capital and the sources of wealth, the DIRT rate was increased in line with increases for CGT and CAT, namely:

- Budget 2008: increase in the rate from 20% to 23%[1]
- Supplementary Budget 2009: increase in the rate from 23% to 25%[2]

5.2 **Evolution of DIRT**

- 1986 – DIRT introduced at 35% (pegged to the standard rate of income tax)
- 1994 - DIRT becomes a final liability tax (see above).
- 2007 - Finance Act 2007 introduced a new scheme to allow the operation of DIRT free savings accounts for two groups: (a) account holders aged over 65 years of age whose total income does not exceed the relevant exemption threshold. (€20,000 (for an individual) or €40,000 (for a married couple) in 2010; and (b) permanently incapacitated persons. These groups were already entitled to have DIRT refunded.
- 2009 - Rate of DIRT increased from 20% to 23% for all payments, including deemed payments made on or after 1 January 2009.
  Rate of tax increased from 23% to 25% for all payments, including deemed payments made on or after 8 April 2009.

5.3 **Net Yield from DIRT**

The following table sets out the net yield from DIRT collected from 2002 to 2009:

Year	**Net Yield (€m)**
2002	207
2003	153
2004	144
2005	167
2006	254
2007	472
2008	654
2009	614

The yield in the six months to 30 June 2010 was €122.8m - the main payment date for DIRT occurs in the second half of the year.

5.4 **DIRT issues for consideration**

The sharp increase in the DIRT yield in 2007 and 2008 can be attributed to an increase in deposit interest rates and rising savings levels in the economy as investors moved away from more-risky investments such as property and shares. Interest rates fell in 2009, but the yield held up reasonably well, although this may be attributable to the increased rate (all DIRT received in 2008 would have been at the 20% rate whereas DIRT received in 2009 would have been at the 23% or 25% rate). Given the current rates of saving in the economy, consideration could be given to an increase in the two DIRT rates – there may be some potential 'leakage' of savings to other jurisdictions, primarily the UK, but the savings market is largely inertia-driven and it would be expected that most people would not move their savings.

An increase of 1% in the two DIRT rates is estimated to yield an additional €25m in a full year.

Consideration could also be given to making DIRT no longer a final liability tax – that is, higher rate taxpayers would have an additional liability to income tax on deposit

[1] From 23% to 26% for life assurance and funds products.

[2] From 26% to 28% life assurance and funds products.

interest over and above any DIRT deducted. This would require individuals to declare the income, either through the PAYE system or in self-assessment, and this could lead to compliance issues. If such a change was made, in the interest of equity the DIRT rate might also have to be re-aligned with the standard rate of Income Tax. However, it is possible that no additional yield would result from such a move.

In addition, consideration could be given to restricting or abolishing the current age-related exemption from DIRT for a couple aged over 65 with an income under €40,000 do not pay DIRT and an individual with an income under €20,000.

There are also exemptions for incapacitated persons, but is suggested that these should not be considered for any restriction.

6. Domicile Levy

6.1 Finance Act 2010 introduced a Domicile Levy, which applies from 1 January 2010 to Irish-domiciled individuals who are also Irish citizens, who:

- have a world-wide income greater than €1 million
- own Irish property worth greater than €5 million; and
- pay €200,000 or less in Irish income tax

The amount of the levy is €200,000 payable annually. Any Irish Income Tax paid in that year is allowed as a credit against the Levy. Although the Levy applies regardless of an individual's residence status, in practice Irish resident individuals who meet the criteria above will have paid in excess of €200,000 in Irish Income Tax, so the Levy is likely to be paid by Irish citizens/domiciled persons who are not resident in Ireland for tax purposes.

The Domicile Levy provisions contain a measure whereby Revenue may give an "opinion" to an individual who is considering making a significant investment in the State as to whether he or she would be likely to be regarded as both domiciled in and a citizen of the State in a particular tax year. This "advance opinion" system is designed to act as an incentive for wealthy individuals to invest in Ireland.

Capital and Savings Taxation Policy

September, 2010

APPENDIX I

PROGRAMME FOR GOVERNMENT – UPDATE SEPTEMBER 2009

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A Fair Tax System

Subject to the controlling economic and fiscal framework, the Government will implement the following specific approach to tax:

- *Our first priority remains low and middle income earners – therefore our first task will be to use tax credits and bands to keep low income earners out of the standard rate band and average earners out of the higher band.*

Finance (No 2) Act 2008 and Finance Act 2009 increased both the Capital Gains Tax (CGT) rate and Capital Acquisitions Tax (CAT) rate from 20% to 22% (2008) and then to 25% (2009). CAT thresholds were also reduced in the Supplementary Budget. Taxation on savings income were also increased – DIRT increased in two stages from 20% to 25% and exit taxes on investment products were increased by a similar amount. These base-broadening measures help to shift the burden of tax from labour and consumption to wealth and sources of wealth.

APPENDIX II COMMISSION ON TAXATION RECOMMENDATIONS ON CAPITAL TAXES

Taxation of Capital

Recommendation 5.25
Gains attributable to inflation should be excluded from the charge to capital gains tax.

Recommendation 5.26
Capital gains tax rollover relief should apply to the gains on disposal of farm land pursuant to a compulsory purchase order where the proceeds are re-invested in farm land.

Stamp Duty - Cards

Recommendation 5.29
Stamp duty on ATM, credit and debit cards should be phased out in the interest of promoting the move towards a cash-free society.

Stamp Duty - Shares

Recommendation 7.8
Stamp duty on all share transactions should be reduced to zero.

Remittance treatment of Capital Taxes

Recommendation 5.32
The remittance basis of taxation for income tax and capital gains tax should be discontinued.

Capital Taxes and Housing

Recommendation 8.17
The capital gains tax exemption on the disposal of a principal private residence should be continued.

Recommendation 8.20
The capital gains tax and stamp duty exemptions on the disposal of site to a child should be discontinued.

Capital Taxes and Philanthropy

Recommendation 8.35
The capital gains tax exemption on works of art loaned for public display should be retained but the exemption should only apply to the gain accruing in the period for which the work of art has been so loaned.

Recommendation 8.38
The CAT exemption of heritage property and heritage property of companies should be retained.

Capital Taxes – Fishing Industry

Recommendation 8.64
The tax treatment of the decommissioning of fishing vessels should continue.

Capital Taxes – Venture Capital Investments

Recommendation 8.66
The tax treatment of venture fund managers should be modified such that in the case of an individual who is a venture capital fund manager:

- **Where the investment return on a carried interest represents income, it should be taxed at the appropriate marginal rate, and**
- **Where the investment return on a carried interest is a capital gain, it should be subject to capital gains tax at the normal rate (25%).**

Capital Taxes – Remittance basis of taxation

Recommendation 5.32
The remittance basis of taxation for income tax and capital gains tax should be discontinued.

Business and Agricultural CGT and CAT Relief

Recommendation 8.69
Capital gains tax relief for disposal of a business or a farm on retirement should continue.

Recommendation 8.70
For business relief for CAT, a reduction of no more than 75% of the value of the business should be allowed before tax is calculated. The reduction should be subject to an overall monetary limit of €3 million.

Recommendation 8.71
For agricultural relief for CAT, a reduction of no more than 75% of the value of the property should be allowed before tax is calculated. The reduction should be subject to an overall monetary limit of €3 million. A condition of the relief should be that a farm asset is owned and operated as a farm for a period of six years after the transfer.

Recommendation 8.72
Business relief and agricultural relief should be amalgamated into a single relief.

Taxation of savings and investments

Recommendation 8.103
Tax exemption for the income of credit unions should be continued.

Recommendation 8.104
The annual exemptions for interest and dividends on special term accounts and special term share accounts should be continued.

APPENDIX III FINANCE ACT 2010 – CAPITAL GAINS TAX MEASURES

Exemption for Disposal of Property by Local Authorities

Provision for the extension of existing Capital Gains Tax exemptions and favourable CGT treatment for some Local Authorities to all Local Authorities and certain other Bodies, namely: (i) jointly established by Local Authorities (e.g. Joint Library Committees or Burial Board); and Bodies established under the Local Government Services (Corporate Bodies) Act 1971 such as the Local Government Computer Services Board (LGCSB) and Local Government Management Services Board (LGMSB). This will eliminate circular transfers of funding for the payment of CGT leading to greater efficiencies and effectiveness in the transaction of activities by these Bodies.

As a related measure, the favourable CGT treatment for some Local Authorities to cover disposals of property is extended to a number of State Cultural Bodies such as the National Gallery, the National Museum, and the Friends of the National Collection of Ireland. The changes will encourage and facilitate transfers of property to these bodies.

Compulsory Purchase Orders

This amendment allows the proceeds of the sale of property arising from a Compulsory Purchase Order to be assessed to Capital Gains Tax where the person who made the disposal dies before receiving the consideration.

Change to Payment Dates

This measure amends Section 958(3)(c)(ii) Taxes Consolidation Act 1997, to align the payment dates for Capital Gains Tax (CGT) with the revised payment dates as set out in Finance (No 2) Act 2008.

Contrived Capital Losses

Section 43 of the Finance (No 2) Act 2008 introduced legislation to counter a specific avoidance scheme relating to the creation of an artificial loss for Capital Gains Tax (CGT) purposes. Further measures are now required to close off these types of schemes and protect Exchequer revenues.

Retirement Relief

This section amends section 598 Taxes Consolidation Act (TCA) 1997 which relates to retirement relief from Capital Gains Tax (CGT) to ensure that individuals do not receive full retirement relief on the disposals of assets of a family business where the aggregate of the assets being disposed of exceeds retirement relief threshold of €750,000.

Participators in Offshore Companies – Trading Exemption

Anti-avoidance provision to attribute a gain made by an offshore company to an Irish resident “participator” (e.g., a director) in that company. The provision does not apply where the offshore company is a trading company. This exemption is being extended to group companies and also to trading in intangible assets as well as tangible assets.

Compulsory Purchase Orders - Change to Payment Date

The date on which tax on CPO proceeds falls due for non-farmers is being changed to the date on which the compensation proceeds are received. The rate of tax which will apply to land acquired under a CPO will in most cases be the rate on the date when the authority with compulsory purchase powers enters the land.