Ernst & Young Tax Services

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TAX ALERT

ERNST & YOUNG
Quality In Everything We Do

Personal Taxes

In 2006 all earners will benefit from increased tax bands and credits…

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Budget 2006

The Minister for Finance, Mr Brian Cowen, TD, presented a complex combination of measures that will affect the net income of almost everyone in the State. However, the measures did little to improve Ireland's competitive position in the global economy.

Personal Taxes

As a result of the tax measures announced by the Minister, those on the minimum wage will now be outside the tax net and lower earners will move from the 42 % to the 20% rate. However, in a counter move the 2006 employee PRSI threshold is increased from €44,180 to €46,600.

With effect from 1 January 2006 the remittance basis of taxation will be discontinued in respect of employment income, in so far as the employment is exercised in the State. This basis of income tax currently applies to Irish resident individuals that are neither ordinarily resident nor domiciled in Ireland and it provides that such individuals are liable to Irish income tax only on the portion of their income arising outside the State or the United Kingdom that is remitted to Ireland. This will certainly be a disincentive in attracting certain high skilled individuals to Ireland.

The Minister did not take this opportunity to announce any innovative new pension funding schemes as indicated in the press in the run up to the Budget, instead he chose to introduce somewhat penal measures for investors:

Contacts

If you require further information, please call your regular contact in Ernst & Young or contact any of the following:

Dublin
PJ Henehan *(Tax Partner)*
E-mail: pj.henehan@ie.ey.com
Tel: +353 1 475 0555
Fax: +353 1 475 0599

Kevin McLoughlin *(Tax Partner)*
E-mail: kevin.mcloughlin@ie.ey.com
Tel: +353 1 475 0555
Fax: +353 1 475 0599

Cork
Frank O'Neill *(Tax Partner)*
E-mail: frank.oneill@ie.ey.com
Tel: +353 21 427 7116
Fax: +353 21 427 2465

Galway
Jerry O'Leary *(Consultant)*
E-mail: jerry.oleary@ie.ey.com
Tel: +353 91 530600
Fax: +353 91 565242

Limerick
John Heffernan *(Tax Partner)*
E-mail: john.heffernan@ie.ey.com
Tel: +353 61 319988
Fax: +353 61 319865

Waterford
Paul Fleming *(Tax Director)*
E-mail: paul.fleming@ie.ey.com
Tel: +353 51 872094
Fax: +353 51 872392

New York (Irish Tax Desk)
Declan Gavin *(Principal)*
E-mail: declan.gavin@ey.com
Tel: +1 212 773 8744
Fax: +1 212 773 6672

Disclaimer

- The maximum allowable pension fund on retirement for tax purposes will be €5million or the value of the fund at 7 December 2005 (if higher). Where a fund exceeds either limit, the excess will be liable to a once-off income tax charge at the 42% rate when it is drawn down.
- The maximum tax free lump sum has been capped at €1.25m for all pension investors with effect from 7 December 2005. Any balance of lump sum payable will be taxed at the marginal rate.
- For those who have post-retirement funds, which are referred to as Approved Retirement Funds (ARFs) with effect from 2007, the fund will be deemed to have distributed 1% of the fund's value, rising to 2% in 2008 and 3% from 2009 onwards and will be taxable. Any actual distributions paid in the year will be deducted from, in calculating the deemed distribution.
- The €254,000 earnings cap which was introduced in 1999, has finally been index-linked but only with effect from 2007.

Prior to the Budget, the Minister declared that 'there is no magic wand' that will sort out childcare. However, he unveiled a number of measures that will go some way towards tackling the much publicised childcare crisis, including a childminding relief, whereby an individual may mind up to 3 children in their own home and avail of tax free income up to €10,000 (if earnings are in excess of this amount the total amount will be taxable).

Tax Reliefs and Incentives

Unsurprisingly, the Minister terminated most of the property based tax incentives, albeit with transitional measures. Transitional measures include the availability of full relief for qualifying expenditure up to the end of December 2006, 75% relief in the period January 2007 to December 2007 and 50% relief in the period January 2008 to July 2008. No relief will apply for expenditure after July 2008. 31 July 2008 will also be the termination date for the exemption from tax in relation to stallion and greyhound stud fees. However, the Minister did indicate that new taxation arrangements would be introduced for the stallion and greyhound stud industries which would be subject to discussions with the EU Commission. It would also appear that the Minister still believes in the power of focused tax breaks as tax relief for investment in childcare facilities, private hospitals and private nursing homes are to be continued.

The Minister announced the introduction of a new mechanism to deal with allowances associated with certain tax reliefs, which will be effective from 1 January 2007. This will restrict the amount of specified reliefs which a taxpayer can use to reduce their tax bill in any one year to 50% of the taxpayers income. The new mechanism will work as follows:

Income Tax Year 2007	**€**
Taxable income (i.e., income after reliefs)	200,000
Specified reliefs in 2007	600,000
Recomputed gross income	800,000
Deductible reliefs restricted to the greater of 50% of €800,000 or €250,000	400,000
Original taxable income	**200,000**
Add restriction of deductible reliefs (€600,000 less €400,000)	200,000
Revised taxable income	**400,000**

The amount of relief allowed in 2007 will be €400,000. The €200,000 balance will be carried forward for deduction in 2008 (subject to the same mechanism).

The Minister announced the immediate abolition of interest relief available to individuals on new loans taken out to acquire an interest in a property rental income company. However, relief will continue to be available on existing loans and on new loans in relation to trading companies.

Minister Cowen has introduced measures to circumvent a particular capital gains tax avoidance scheme whereby assets which ordinarily would be subject to capital gains tax were transferred to a spouse, separated or former spouse who was not tax resident in the State, free of capital gains tax. That spouse would then dispose of the asset in the year in which he/she acquired it while being non tax resident in Ireland thereby avoiding a charge to Capital Gains Tax.

This anti-avoidance measure which will take effect from 7 December 2005 effectively makes the initial transfer between the individual and their spouse, separated or former spouse liable to capital gains tax.

The details of a new tax relief for the donation of heritage property to the proposed Heritage Trust will be unveiled in the 2006 Finance Bill. It is understood that up to 100% of the total market value of the donated properties will be available for setoff against the tax liabilities of the donor.

Business Taxes

The Minister announced, with immediate effect, an anti-avoidance provision to deny interest deductions where the principal purpose of a transaction is to create ‘artificially generated’ debt. One example might be a situation where a foreign parent with a profitable Irish subsidiary incorporates a new subsidiary; then the new subsidiary borrows money to purchase the first Irish subsidiary. For transactions effected before 7 December 2005 the interest cost of the new subsidiary can be set off against the taxable profits of the existing subsidiary.

The anti-avoidance measure will deny this interest relief for transactions effected on or after Budget Day, although the precise scope of the measure has not yet been announced. The Minister has stated the legislation will be carefully targeted so as to minimise its impact on the 'legitimate commercial' use of the interest relief provision or any other area of Ireland's tax code introduced to facilitate bona-fide transactions between companies.

The abolition of the 0.5% rate of capital duty on the issue of shares puts Ireland on a level footing with other EU countries.

In a welcome move the Minister announced that the 2006 Finance Bill will contain measures that will reform the rules relating to the taxation of leasing companies. Currently, such companies are restricted in the use they can make of losses generated by excess capital allowances claimed on certain long life leased assets. The Finance Bill 2006 will allow the breaking of the ring fenced loss provisions in certain circumstances.

The threshold for leases and capital allowances for new and second cars used in the course of business is increased from €22,000 to €23,000.

Stamp duty relief on the transfer of land to certain young trained farmers was due to expire on 31 December 2005. This has been extended for a further three years to 31 December 2008. The EU Single Farm Payment Entitlement will qualify as an asset for the purposes of capital gains tax retirement relief. It will also be recognised as a qualifying agricultural asset for the purposes of the capital acquisitions tax agricultural relief qualification test.

The Minister has announced that there will be no changes to the VAT rates. The VAT registration thresholds that were last adjusted in 1994 are to be increased. The threshold for the supply of services increases to €27,500 and the threshold for the supply of goods increases to €55,000. The new thresholds will have effect from 1 May 2006.

Facts About Tax 2006	2006 Euro	2005 Euro
Income Tax Rates		
Standard	20%	20%
Marginal	42%	42%
Standard Rate Bands		
Single	32,000	29,400
Married *	64,000	58,800
Married – one income	41,000	38,400
Single Parents	36,000	33,400
* both spouses income >	23,000	20,400
Personal Tax Credits		
Single	1,630	1,580
Married	3,260	3,160
Widowed (no dependent children)		
- year of bereavement	3,260	3,160
- subsequent years	2,130	1,980
PAYE	1,490	1,270
Home Carers Credit (Maximum)	770	770
- Spouses income limit	5,080	5,080
- Marginal relief / effective limit	6,620	6,620
- Optional cut-off point	3,500	3,500
Widowed person tax credit	500	400
Additional widowed allowance (with dependent children)		
- First year after bereavement	3,100	2,800
- Second year	2,600	2,300
- Third year	2,100	1,800
- Fourth year	1,600	1,300
- Fifth year	1,100	800
Single Parent (additional)	1,630	1,580
Age (65 or over in the tax year)		
- Single	250	205
- Married	500	410
Blind		
- Single widowed	1,500	1,000
- Both spouses	3,000	2,000
Trade Union Subscriptions (Maximum)	60	40
Service Charges (Maximum)	39	39
Rent		
- Single under 55	330	300
- Single 55 or over	660	600
- Married/widowed under 55	660	600
- Married/widowed 55 or over	1,320	1,200
Incapacitated Child (maximum)	1,500	1,000
Dependent Relative (maximum)	80	60
Exemption Limits		
Single under 65	5,210	5,210
Single over 65	17,000	16,500
Married under 65	10,420	10,420
Married over 65	34,000	33,000
Increase per dependent child		
For each of the first two children	575	575
For each subsequent child	830	830

Facts About Tax 2006	2006 Euro	2005 Euro
PRSI Rates		
Employer		
- standard	10.75%	10.75%
- lower rate	8.50%	8.50%
Weekly lower rate limit	356	356
Self-employed		
- PRSI	3%	3%
- Health levy	2%	2%
Minimum Contribution	253	253
Employee		
- PRSI	4%	4%
- Health levy	2%	2%
PRSI Exemptions		
Employee annual PRSI ceiling	46,600	44,180
Weekly PRSI allowance	127	127
Weekly PRSI exemption limit	300	287
Weekly Levy exemption limit	440	400
Benefits in Kind exemption limit	250	250
Capital Gains		
Standard rate	20%	20%
Foreign life assurance policies	40%	40%
Tax Clearance CG50 limit	500,000	500,000
Withholding tax rate	15%	15%
Capital Acquisitions Tax		
Standard rate	20%	20%
Corporation Tax Rates		
Standard rate on trading income	12.50%	12.50%
Higher rate on passive income	25%	25%
Manufacturing (effective rate)	10%	10%
Qualifying Shipping	12.50%	12.50%
Residential land (effective rate)	20%	20%
Non-residential land	25%	25%
VAT Rates and Limits		
Standard	21%	21%
Reduced rate	13.5%	13.5%
Farmers Flat rate	4.8%	4.8%
Distance selling limit	35,000	35,000
Registration limit – taxable goods	55,000	51,000
Registration limit – taxable services	27,500	25,500
Cash receipts basis limit	635,000	635,000
Companies Capital Duty		
Standard rate	0%	0.5%
Motor Cars Capital Allowances		
Car value threshold	23,000	22,000