Budget 2015 – what does it mean for Ireland and its private business sector?

The political backdrop to this year's Budget was perhaps the most interesting of recent years. Improving growth outlooks, and widely reported improvements in GDP, meant that the adjustment required in Budget 2015 was not as severe as previous year projections had anticipated. Not only this, but Minister Noonan was also in the unfamiliar position of having a small surplus to "play with" - and lots of stakeholders were putting forward their cases.

From an international perspective, Ireland has been under increasing pressure to address the infamous 'Double Irish' structure, for which Ireland has received a lot of unfair criticism in recent times. Minister Noonan was tasked with finding a balance between phasing out the 'Double Irish' and maintaining Ireland's attractiveness to large multinationals. The outcome was broadly positive. Personal tax, corporate tax in both the Foreign Direct Investment and Irish private business sectors, and the property/construction sector all received some modest but welcome measures, which seek to facilitate future growth and increase spending.

The domestic economy

As well as a clear focus on FDI and our international reputation, a number of measures have been introduced that are aimed at stimulating activity in the domestic economy.

The private business sector in Ireland is moving into "post-austerity" mode and there is a renewed focus on growth and expansion, with a big emphasis on export markets. In our SME CEO Pulse Survey (released in September, see link: http://download.pwc.com/ie/pubs/2014-sme-pulse-survey.pdf) CEOs of Irish private businesses outlined their views that the economy is turning the corner, and that confidence is "somewhat" restored. Most companies are going for growth (revenues, profits and employment) over the next twelve months. However, a number of "blockers" to future growth were also identified. For instance, funding remains a core challenge, and there are concerns around availability/retention of talent, and an increasing labour cost base. The ability to attract, retain and reward talent is critical for growth.

What was needed?

Based on the results of the survey, and the views expressed by a representative group of Irish businesses who attended a recent event hosted by PwC's Private Business Services group, a "wish-list" of the private business community in Ireland was prepared and submitted to the Minister for Finance. It focused on what the sector believed should be done in Budget 2015 to help facilitate private business as it emerges from the economic doldrums.

The key issues identified as needing to be addressed were:

- the employment tax burden,
- management of overall labour costs through income tax cuts,
- financing from a "State bank" or from loan capital investments from individual investors,
- exporting incentives to promote the exploration of new markets,
- the retention of the 9% VAT rate in the tourism sector, and
- an improved CGT relief for entrepreneurs.

See our submission at the following link: http://download.pwc.com/ie/pubs/2014-pwc-ireland-pbs-pre-budget-wishes-01-10-2014-1.pdf .

So, what actually happened?

Budget 2015, and the subsequently initiated Finance Bill 2014[1] that will, when enacted, legislate for its provisions, outlined a number of initiatives that addressed some of the primary concerns of Irish private businesses.

Some welcome changes to personal tax rates and thresholds should help to address the issue of **labour costs,** whereby lower and middle income employees stand to benefit from a reduction in the top rate of income tax to 40% (a reduction of 1%). Furthermore, while the standard rate of tax remains at 20%, the threshold at which middle income earners will start paying the higher rate of tax has increased to €33,800 (up €1,000) for single people and €42,800 (up €1,000) for married couples with one earner. Changes to USC rates and thresholds were also designed to benefit lower to middle income employees. While these changes will lead to some increases in take home pay, they do not, unfortunately, address the issue of reducing labour costs for employers.

In Budget 2015, the Minister acknowledged the importance of helping private businesses to **raise finance** by announcing increases in the annual and overall limits for the Employment and Investment Incentive Scheme (EIIS) to €5m and €15m respectively. He also announced that the Strategic Banking Corporation of Ireland will increase the availability of loans with longer terms and more flexible conditions, and the Seed Capital Scheme has been reintroduced and rebranded as Start Up Relief for Entrepreneurs ("SURE")

As part of a package of **export initiatives**, Minister Noonan announced a three year extension to the Foreign Earnings Deduction (FED) to 2017 and extended the relief to additional countries, including Mexico, Chile and certain countries in the Middle East and Asia. The conditions were also revised to make it less onerous for employees to qualify for the relief.

Some changes were announced to the **CGT relief for entrepreneurs**, which had not been enacted pending EU approval. By way of background, this relief is intended to be an incentive for "serial entrepreneurs" who have disposed of trading assets and reinvested in assets used in another trade in the period from 1 January 2014 to 31 December 2018. Where they later dispose of the second assets, the CGT payable on that disposal will be reduced by the lower of:

- The CGT paid on a previous disposal of assets, and
- 50% of the CGT due on the disposal of the new investment.

Some of the changes introduced by Budget 2015 are merely technical adjustments to avoid the requirement to obtain EU State Aid approval. However, there are also some amendments aimed at widening the application of the relief. For example, the minimum shareholding required to qualify for

[1] This article goes to print by reference to Minister's Budget 15 speech and Finance Bill 2014 "as initiated". Amendments may be made, and/or additional measures introduced, as the draft legislation passes through the Houses of the Oireachtas.

the relief has now been reduced to 15% for corporate investments, where a controlling investment was previously required to qualify for the relief.

Other welcome measures that have implications for private Irish businesses include:

- an extension to the three year start up relief for new companies for one additional year to the end of 2015

- an amendment to business property relief from Capital Acquisitions Tax, to deal with a specific circumstance where a business is controlled by a husband or wife (or civil partners) on a 50:50 basis. The legislation as originally drafted did not allow for relief to apply on the transfer of assets personally held (but used in the business) unless the disponer also controlled the shares (i.e. greater than 50%). This has now been changed so that the control requirement is satisfied where both partners taken together control the company.

- Improvements to Irelands "innovation tax policy" announced in the Budget provide both immediate cash benefits and some potential longer term opportunities for private Irish businesses. The R&D regime has constantly been enhanced since its introduction in 2004 and the announcements in Budget 2015 are once again very positive, with the abolition of the "base year" expenditure from R&D tax credit calculations. Furthermore, a consultation process has been initiated to consider the creation of a 'Knowledge Development Box' regime which would enable companies to exploit the output of their R&D activities and which, together with the abolition of the base year, will help position Ireland as a prime location for innovation activities

- Budget 2015 attempts to address the key objectives outlined in Construction 2020 strategy released in May of this year. The abolition of the "windfall gains tax" and the extension of the Home Renovation Incentive Scheme should assist in increasing construction activity in the country, which in turn should lead to an increase in jobs. Furthermore, the commitment to construct a minimum of 10,000 new social housing units by the end of 2018 is an important step in solving Ireland's social housing problems, and offers further scope for jobs and opportunities for companies in this sector.

It is also worth noting that the 7 year relief from CGT in respect of land and building purchases between 7 December 2011 and 31 December 2014 has not been extended. There remains a window of opportunity to make acquisitions on or before 31 December 2014, which may be worth considering.

What didn't happen?

Overall, Budget 2015 has been largely positive against the backdrop of the last 7 years. However, the Minister might have availed of additional opportunities to provide support to private Irish businesses at this critical stage in the economic life-cycle.

For example, while some initiatives aimed at improving private business finance were introduced (e.g. amendments to the EII scheme, and the creation of the Strategic Banking Corporation), it would have been helpful if the Minister had introduced a relief to promote loan capital investments in private businesses by individuals, such as including a USC exemption or a reduced rate of income tax on interest income earned. This is in the context of recently published Central Bank figures[2] that suggest that in excess of €91b is held by Irish banks in the form of Irish household deposits. A tax efficient opportunity to lend to "your local SME" is an initiative which could release private funds to private businesses.

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[2] Irish Central Bank – Deposits from Irish Private Sector – 31 July 2014

The reduction in the effective tax rate for medium and low income earners should boost consumer sentiment, helping to fuel domestic demand for products and services. However, despite this welcome move, calls from the private business community to reduce the employment tax burden, through either a reduction in the employer's PRSI burden or some form of employer tax rebate, have once again been ignored.

In relation to the CGT entrepreneur relief, despite some welcome changes, the relief still does not compare favourably with similar reliefs operated within the EU. It remains overly restrictive and is likely to benefit only serially successful entrepreneurs.

The property sector could also have further benefited from a reduction in the CGT rate, which remains comparably high by international standards. Furthermore, widespread calls for a reduction in the VAT rate on construction activity from 13.5% to 9% have been to no avail. Minister Noonan stated clearly in his Budget speech that the Government will not move back towards a tax regime that favours property developers. Accordingly, tax policy is likely to help stimulate demand for property, rather than reducing the cost of supply.

The international context

At macro and international levels, the changes announced in relation to the corporate residence rules demonstrate Ireland's commitment to ensuring that its taxation system is globally accepted as an open, transparent, rules based system which is fair and, most importantly, competitive. The decisive action taken in phasing out the 'Double-Irish' structure should boost Ireland's reputation internationally.

The proposed grandfathering period of six years will provide affected multinational groups with time and flexibility to restructure their global arrangements in a considered manner, particularly important given the current uncertainties on how the OECD project on Base Erosion and Profit Shifting (i.e. BEPS, the allocation to different countries of multinational companies' profits) will impact the tax laws of other countries in which they operate.

Multinationals currently operating here should welcome the new and improved incentives for indigenous and the Foreign Direct Investment sectors, including changes to the Special Assignee Relief Programme and the Foreign Earnings Deduction as well as the proposed "Knowledge Development Box" regime mentioned above. This latter will involve a consultation process in 2015 ahead of expected draft legislation in next year's Finance Bill and an effective date of 1 January 2016 (subject to EU approval). In this context, the complete abolition of the 2003 base year in the R&D credit is very significant as it reflects a strong recommendation arising from the public consultation process undertaken last year and demonstrates the Government's commitment to enhancing Ireland's offering in this area.

These reliefs are, of course, also of relevance and benefit to the domestic sector.

So….are we there yet?

Overall, Budget 2015 has been positive for the private business sector. While some further areas could have been addressed, the changes underline the government's commitment to giving Irish businesses a platform for growth. Irish businesses should consider Budget 2015 as a starting point in a new cycle, rather than the finish line for the "austerity years".

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