Budget 2018 – the 'Balanced' Budget

What does the 'Balanced Budget' delivered by Pascal Donohoe mean for family businesses, and how is it going to affect these businesses in an increasingly uncertain and complex marketplace, both domestically and internationally? Tax partner Teresa McColgan and Tax Director Niall Cogan in PwC Private Business Services explain below.

Ongoing uncertainty in the global political and tax environments increases the focus on and importance of having a domestic tax regime that supports indigenous Irish businesses. With the economy continuing to perform well, the clear goal of the 2018 Budget was to maintain a positive outlook while creating a roadmap for the years ahead. However, despite greater fiscal space being available than first anticipated (€1.2 billion rather than the expected €350 million), the 2018 Budget did not deliver as much as we had hoped for private businesses. A summary of the relevant changes is included below.

Increase in Stamp Duty on Commercial Property

One of the primary ways in which the Government increased the fiscal space was through the introduction of a number of new revenue generating measures. One such measure that could have a significant impact on some family businesses was the increase in the rate of stamp duty from 2% to 6%. This rate doesn't just apply to land and commercial buildings, it also applies to business asset transfers such as debtors/loans, goodwill, prepayments, IP (subject to IP exemption) and any other Irish intangibles. As expected, transitional measures have been included in the Finance Bill in respect of transactions entered into before 11 October 2017. Where a binding contract to acquire land or commercial buildings was entered into before 11 October, the 2% rate of duty will still apply to the acquisition provided a conveyance/assignment of that property is executed before 1 January 2018. This is a relatively short transition period, so it will important for businesses to keep an eye on that clock to ensure any deals struck before 11 October are completed by year-end.

Succession planning

Rather surprisingly, the lifetime threshold for gifts and inheritances taken from a parent did not get the increase in Budget 2018 that was widely anticipated. In fact, there was very little in the Budget or Finance Bill on succession other than for the agribusiness sector.

The special 1% rate of stamp duty on transfers of farm land between close relatives is to be preserved until the end of 2020, and the requirement for the transferor to be under 67 years of age is to be abolished (from the date of passing of the Finance Act). This is undoubtedly good news for those planning to pass on their farm land to the next generation. Certain other conditions must still be satisfied for this relief to be available, such as the transferee (or a lessee of the transferee) farming the land for at least 50% of their normal working time, or holding an appropriate agricultural qualification. To address EU State Aid rules, the relief available for transfers of land to young trained farmers will now require the young trained farmer to submit a business plan to Teagasc, and to come within the meaning of “micro, small and medium-sized enterprises” in the 2014 EU Regulations on aid in the agricultural and forestry sectors.

SME-focused Share Option Incentive Scheme

A welcome move for scaling businesses is the introduction of the ‘Key Employee Engagement Programme’ (KEEP), an SME-focused share option incentive scheme. This incentive, which applies to unquoted trading Irish companies, will allow cash-strapped SMEs the opportunity to offer share options to employees in a tax efficient manner (although certain trading activities are specifically excluded). Share options are particularly valuable to scaling businesses, who need talented staff but struggle to compete with more established employers.

SMEs for the purposes of the incentive include companies who employ less than 250 people and have an annual turnover not exceeding €50m and/or an annual balance sheet not exceeding €43m.

In a positive move, the gains arising on the exercise of KEEP share options will be liable to CGT on disposal, rather than income tax, USC and PRSI on exercise, similar to the UK regime. The incentive will be available for five years for options granted between 1 January 2018 and 31 December 2023. A qualifying company can grant share options to employees up to a total market value of €3m with the total market value of the share options granted to any one individual not exceeding €100k in any one tax year, €250k over three consecutive years or 50% of the individual’s annual emoluments. KEEP will only apply to share options granted to full time employees or directors who spend a minimum of 30 hours per week working for the company. The share options must be held for a minimum of 12 months before being exercised and must be exercised within 10 years of the date of grant. Importantly, the KEEP programme will not apply if the individual (either alone or with connected persons) can control directly or indirectly more than 15% of the ordinary share capital of the company.

Employer PRSI to increase

This was one of the main talking points following Minister Donohoe's speech, and one which will affect all family businesses and their payroll costs. As part of his package to improve "education for all", an increase in the National Training Fund Levy was announced. This will increase by 0.1% per annum over the next three years, bringing the Levy from 0.7% to 1%. This is significant for employers as the Levy is a component part of the Employer PRSI charge. Therefore, employers are facing an increase in their PRSI costs from 10.75% to 11.05% by 2020.

Relief for employees

The Government has stressed its focus on rewarding work and enterprise, benefitting those who pay the highest rates of tax on modest incomes. The Minister announced two main initiatives to achieve this. Firstly, the point at which people begin to pay the top rate of income tax has increased by €750 to €34,550 for a single person and €43,550 for a married couple with one spouse earning. The increase in this ceiling means an additional €150 a year, or €3 a week, to a worker who pays the top rate of tax. While this is a positive move, it is still a very low entry point by international standards to a tax rate of this magnitude.

Secondly, Minister Donohoe has reduced the 2.5% rate of USC to 2% and increased the ceiling on which this applies from €18,772 to €19,372 (the entry point remains at €13,000). The 5% rate of USC has also been reduced to 4.75%, which will apply to income from €19,373 to €70,044. Undoubtedly, measures that result in workers having more take-home pay, and that can stimulate spending in the local economy, are generally good for Irish business.

The Minister also announced a number of measures to tackle climate change, including a 0% benefit in kind (BIK) rate on electric vehicles provided as company cars for 2018 only. Electricity used in the workplace for charging electric vehicles will also be exempt from BIK, provided all employees can avail of the facility. These interim measures are intended to allow time for a comprehensive review of the taxation of employer provided vehicles, the results of which may mean further changes in next year's Finance Bill.

A well-documented change as regards income tax is the establishment of a working group to plan for the amalgamation of USC and PRSI.

PAYE – Real Time Reporting

Finance Bill 2017 sets out the main changes necessary to underpin the introduction of Real Time Reporting (RTR) on 1 January 2019. One such change is to the basis of taxation under which PAYE will apply, from an earnings basis to a receipts (or a real time) basis. This will apply for emoluments paid on or after 1 January 2018. Transitional arrangements are included for emoluments which may have been taxed in 2017 (on an earnings basis) but are then received (and taxed) in 2018. This is a significant change, with potential relevance for PAYE taxpayers in receipt of bonuses which may be earned in one period but paid in another.

Employers will need to understand how their payroll systems and procedures are equipped to deal with RTR well in advance of 1 January 2019, and we're seeing a lot of interest from businesses seeking to prepare for its introduction.

Sugar Tax

The Finance Bill provides further detail on the application of a new tax, known as Sugar Sweetened Drinks tax, which was first announced in Budget 2017, and again in Budget 2018. Sugar Tax is expected to be introduced from April 2018.

In short, the tax will apply on the first supply of relevant beverages within the State where the sugar content of the beverage product is in excess of 5 grams or more per 100ml. A rate of €0.30 per litre will apply for drinks with a sugar content of 8g or more per 100ml, with a €0.20 rate being applied to drinks with a sugar content between 5g and 8g per 100ml.

Companies who may be affected by this tax include manufacturers, bottlers, distributors, wholesalers and retailers.

VAT

Despite much pre-2018 Budget discussion around the potential increase, amendment or abolition of the 9% VAT rate for the tourism and hospitality sectors, the Minister for Finance has announced that there will be no change to the rate.

The retention of the 9% rate in the tourism and hospitality sectors is welcome for those family businesses operating in such sectors, particularly given the value of the UK market to these sectors and the potential impact of the fall in Sterling's value.

Other relevant measures

Other measures introduced in the Budget/Finance Bill that may be relevant to business owners include:

- The Earned Income Credit for self-employed individuals has been increased from €950 to €1,150, bringing it closer to the €1,650 credit available to employees.

- Mortgage interest relief has been extended for another three years. However, the tax relief will be reduced gradually by 25% over each of those three years (75% for 2018, 50% for 2019 and 25% for 2020). The relief will cease entirely from 2021.

- The scheme of accelerated capital allowances, which provides a 100% up-front tax deduction for qualifying energy equipment, has now been extended to 31 December 2020, promoting energy-efficiency amongst next generation businesses.

Conclusion

Some may say the Minister has not gone far enough in terms of the changes he has made but, if paving the way forward was the goal, he has started down the road, illustrating confidence in where Ireland can go as a nation. Budget 2018 has not overwhelmingly altered the tax environment for Irish family businesses, but businesses wishing to expand must stay in touch with the changes affecting them.

Note to reader: This article was written following the publication of Finance Bill 2017 "as initiated". There may be further changes as the legislation is moved to enactment as Finance Act 2017.