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FINANCE BILL BULLETIN

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The Finance Bill 2005 was published on 3 February, 2005. By contrast to the absence of any real tax changes on the Budget, the Finance Bill includes a range of tax measures, many of which are effective as and from the date and publication of the Finance Bill.

The introduction of the major tax changes at this point rather than in the Budget mirrors a practice which has grown in recent years. One can expect some more changes between now and the passing of the measures into law in the Finance Act.

Some highlights of the new tax measures referred to in the Finance Bill 2005 are outlined below.

Property

Capital allowances for hotels, holiday hostels and guest houses

Recently, a taxpayer succeeded on appeal against Revenue in arguing that a guest house premises, which was not registered in the Register of Hotels, was a hotel for capital allowances purposes (thereby qualifying for write-off of qualifying expenditure over 7 years). The Finance Bill now confirms that in order to secure capital allowances as a hotel, the premises must be registered as a hotel under the Tourist Traffic Acts.

However, the Finance Bill is also making capital allowances available for qualifying expenditure on guest houses or holiday hostels, both of which did not qualify for capital allowances previously. The rate of allowances will be at 4% per annum. This might be seen as introducing equality into the holiday accommodation sector. As might be expected, there are certain requirements to be observed in order to obtain such allowances.

VAT on transfers of businesses

Previously, the transfer of assets in connection with the transfer of a business was exempt from VAT where the transfer was to a taxable person for VAT purposes. In light of recent case law, both in Ireland and the EU, the circumstances for exemption have been amended somewhat. The exemption will now apply to where there is a transfer of a totality of assets which constitute an undertaking or part of an undertaking capable of being operated on an independent basis.

VAT on leases

Generally, where a person grants a long term lease of a premises liable to VAT, the grant of the long term lease is viewed as passing the property out of the “VAT net”, with the result that a disposal by the holder of the freehold or reversionary interest would be not to liable to VAT on a subsequent sale. However, prior to the Finance Bill, a redevelopment of the property by the tenant or landlord would have the result of bringing the freehold or reversionary interest back into the “VAT net”. Consequently, on a sale of that interest, VAT would be chargeable by the owner. Under the Revenue’s interpretation of the law, such VAT could not be recovered by the purchaser of the interest. This meant that VAT would represent an actual cost in any affected transaction, even where there was a fully commercial transaction.

The Finance Bill now provides that in the circumstances outlined above, the sale of

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the freehold or reversionary interest will not be chargeable to VAT where redevelopment has taken place after the creation of the taxable lease except where such development is carried out by or on behalf of or for the benefit of the landlord. It has been left to the Revenue to make regulations on what is exactly meant by this. Pending these regulations, extreme caution should be exercised in granting commercial leases and dealing in properties subject to commercial leases.

VAT on student accommodation/holiday accommodation

Amendments have been made to the legislation to confirm that any lettings in the student accommodation sector will not qualify for the VAT rate of 13.5%, which in the Revenue's eyes, was only to apply to holiday lettings. The VAT rate of 13.5% is now restricted to short term guest or holiday sector accommodation and other accommodation provided for holiday purposes. These new provisions come into effect as and from 1 July, 2005. For any persons who have been paying VAT at a rate of 13.5% on lettings to students, advice should be taken on the implications of this new provision.

Employment Taxation

Exgratia payments on termination of employment

The Finance Bill has introduced a reporting requirement for employers who make payments to employees on account of injury, disability or death. The information must be furnished to the Revenue fourteen days following the end of the year of assessment.

"Topslicing relief" which is used to offer additional relief in certain cases for where termination payments are taxable has been amended slightly. The calculation of the relief required average remuneration over five years to be taken into account but this has now been reduced to three years.

Pensions

The Finance Bill has introduced a statutory scheme of tax relief for contributions paid by an EU migrant worker to an overseas scheme. The relief will apply to employee and employer contributions As might be expected, there are a number of conditions and information requirements to be satisfied in order to obtain the relief.

The Finance Bill has also introduced provisions permitting Irish resident persons to obtain membership of pension schemes provided by pension providers based in other EU member states. To what extent this option will be taken up by Irish resident persons is unclear at this point.

Share Options

The Finance Bill extends the charge to income tax on exercising share options to the exercise of options granted when an individual is non-resident (applicable to options granted on or after 3 February 2005). This is a reversal of a previous practice of Revenue under which share options would not be liable to Irish tax where they were granted when a person was non-resident and where the options were not connected to an Irish employment

The amendment has been introduced pursuant to a report by the Committee of Fiscal Affairs of the OECD and would seem to be directed at ensuring that double taxation will not arise.

A Statement of Practice is expected from Revenue on the practical aspects of this amendment. Suffice to say at present that this will affect employees of multinationals moving to or from Ireland.

Company and Commercial Taxation

International Financial Reporting Standards

After some amount of uncertainty, the Finance Bill is now setting out extensive provisions on the tax implications of the move by companies to the new International Financial Reporting Standard

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(IFRS). These standards will apply to all EU companies listed on a stock exchange for a period of account commencing on or after 1 January, 2005. Other companies will have an option to adopt such standards.

The provisions provide interpretation rules in relation to the accounting standards. They also provide that taxable trading income is to be computed in accordance with generally accepted accounting standards but applies specific treatment for certain items for tax purposes. The provisions also include transitional rules set out in a new schedule to the Taxes Consolidation Act 1997.

Holding Company Regime/Participation Exemption

The Finance Bill contains the terms under which EU approval was granted for the holding company/participation exemption. The new threshold of qualifying subsidiaries has been removed and the shareholding requirement has been reduced to 5%. These provisions will facilitate the establishment of headquarters and holding companies in Ireland.

Limited Partnerships

The Finance Bill has introduced anti-avoidance provision affecting limited partners. The amendment, which will effectively deny relief to certain partnerships or other arrangements registered outside Ireland, has effect for the income tax year 2005 and subsequent years.

Disposals of shares in companies

Existing anti-avoidance legislation which converts a receipt liable to Capital Gains Tax to a dividend in certain cases has been tightened up arising from perceived "abuses". This legislation will now be applied where there is a disposal of shares by a person without the person (when taken together with his or her relatives and certain other persons) significantly reducing his or her interest in the company. This does not apply in 'bona fide commercial' situations.

The amendments to the legislation mean that in certain transactions involving disposal of shares to family members, it will be necessary to demonstrate a bona fide commercial reason for the disposal in order to avoid any proceeds being treated as liable to income tax.

Accordingly, in share disposals for cash between family members, caution will need to be exercised.

Miscellaneous

Deposit interest from banks in the EU

Since 1994, deposit interests receivable by Irish residents from Irish banks has been subject to the standard rate of income tax only and is not taxed at the higher rate. This treatment did not apply to interest derived from banks abroad. Arising from what is likely to have been EU pressure, deposit interest received by individuals from lending institutions in other EU countries will be subject to income tax at the same rate as individuals receiving interest from lending institutions in Ireland. However, this is provided that the tax on such interest is discharged by the return filing date for income tax returns for the year concerned.

Finally, for those persons who may have claimed tax relief for expenditure in significant buildings and gardens, they can now expect to have Revenue officials signing in their visitor books. Revenue have been given the power to make unannounced visits to such buildings and gardens. New advertising requirements have also been introduced.

For further information on any of the above matters or on any tax matters, please contact John Cuddigan, Head of Tax at 021-4802700 or at john.cuddigan@rdj.ie

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