An Overview of the Taxation of Irish Regulated Funds

Broadly the Irish taxation of funds is simple. Generally, authorised Irish funds are tax exempt, except to the extent that they have Irish resident investors. Ireland would not be an attractive location for funds without tax neutrality, which is achieved through various exemptions from direct and indirect taxes. Other popular jurisdictions for funds such as the Channel Islands, Cayman and Luxembourg similarly have no taxes or have a favourable tax regime to allow a fund to achieve tax neutrality.

Tax on Income and Gains

Since 2001 an exit tax regime has applied to particular types of Irish funds. These are, authorised unit trusts, UCITS, authorised Part XIII companies, and investment limited partnerships. Under this regime the fund is exempt from tax on its income and gains on underlying investments but must operate an exit tax on the happening of certain events. The exit tax is collected on behalf of the investors by the fund and is paid to the Revenue.

Broadly, tax at the rate of 30% is levied by the fund on the payment of the income distributions to investors and at the rate of 33% on the effective gain made by the investor in respect of cancellations/redemptions/repurchases or transfers of units. The 33% rate also applies to a chargeable event which is deemed to arise on the passing of eight years from the date of acquisition of a unit by the investor. This eight year event is intended to prevent indefinite deferral of tax. On a payment the fund must deduct the tax and on a cancellation etc., the fund will appropriate and cancel the necessary number of units.

The exit tax should apply only to certain Irish resident investors. It does not apply to non-Irish resident investors and certain categories of Irish exempt investors, provided they have given the fund the appropriate documentation or the fund has been approved to operate certain simplified procedures ("equivalent measures"). It is therefore extremely important that the necessary Revenue prescribed declarations of non-Irish residency (or equivalent for Irish exempt investors) - which may be included as part of the funds application form - are provided to the fund by the investor. Otherwise Irish tax will unnecessarily be required to be operated by the fund, assuming the fund does not have "equivalent measures" approval.

Exit tax is not required to be operated if the fund units are held in a recognised clearing system, for example Clearstream or Euroclear, although in such a circumstance Irish resident investors will have a self assessment liability.

There are a number of categories of Irish resident investor that are entitled to an exemption from this exit tax including: pension schemes, insurance companies, charities, approved retirement funds, approved minimum retirement funds, special savings incentive accounts, PRSAs and credit unions.

Indirect taxes, such as stamp duty and VAT, could potentially arise for Irish funds. However, to maximise the tax efficiency of such funds a number of exemptions apply from these times.

Stamp Duty and Gift/Inheritance Tax

Transfers of units in Irish funds are exempt from Irish stamp duty. A gift or inheritance between foreign residents of units in an Irish fund is exempt from capital acquisitions tax (i.e. gift and inheritance tax).

VAT

Generally, the Irish Revenue accepts that a fund may register for Irish VAT. Registration would be relevant where the fund is seeking to recover VAT charged to it, where it is in receipt of services in respect of which it is obliged to self-account for VAT, or where an Irish VAT registration number is needed in order for a foreign service provider not to charge foreign VAT on the service. VAT registration does not in itself entitle a fund to recover VAT incurred by it. VAT recovery is available to the extent the fund is considered to provide services to entities established outside the EU. In practice this can be determined by reference to the extent the fund has non-EU investors. VAT therefore is not necessarily a cost to a fund. VAT will be chargeable on certain services supplied to a fund e.g. legal services provided to the fund. However, there are exemptions for certain services. The principal exemption is for management services and applies to discretionary investment management services, administration services and marketing services.

Taxation of Common Contractual Funds

Common contractual funds are intended to facilitate the obtaining of relief from withholding tax in jurisdictions where investments are held and are largely "designed" for cross border pension pooling arrangements, although they are not restricted to such a use. For Irish tax purposes, the income and gains of CCFs are treated as accruing directly to the investors and therefore, there is no exposure to Irish tax for investors outside the scope of Irish tax. A CCF is tax transparent under Irish law so as to facilitate the CCF investor in obtaining relief under the terms of a double tax treaty between their home jurisdiction and the jurisdiction where the withholding is suffered, effectively ignoring the existence of Irish CCF. The CCF itself is not liable to tax in Ireland on its income or gains.

Double Tax Relief

Whether the benefits of a double tax agreement can be availed of by an Irish fund is determined under normal treaty principles. Usually, a double tax agreement with Ireland will provide that for a fund to be able to avail of the treaty provisions, it must be resident in Ireland for tax purposes.

In practice, if a confirmation of the Irish residence of a fund is requested from the Irish Revenue Commissioners, they will normally issue a letter, where they are satisfied that the fund concerned is resident in Ireland, that the fund is so resident but will note that the fund is only liable to tax in Ireland to the extent that it has Irish resident investors. As to whether this would be sufficient for the foreign tax authority to grant treaty relief is obviously dependent on the practice of the foreign tax authority. Where this is a potential difficulty, in a fund obtaining treaty relief commonly an Irish securitisation company is interposed between the fund and the underlying assets to address this concern.

FATCA

This is a particularly topical issue. FATCA (the Foreign Account Tax Compliance Act) is legislation aimed at combatting US individuals avoiding taxation on foreign held investments. It is very broad in nature and potentially requires non US financial institutions, including funds, to register with the US Revenue Service (IRS), obtain details of US investors, report such details to the IRS and in certain circumstances withhold US tax. This gave rise to a number of practical difficulties and a number of countries have indicated that they will enter into intergovernmental arrangements with the US, where as an alternative, those countries will collect the relevant information under their own laws and then share the information with the US.

In early 2012 the US Treasury and the Inland Revenue Service (IRS) issued a joint statement together with France, Germany, Italy, Spain and the UK setting out a framework for the establishment of intergovernmental agreements to better facilitate the implementation of FATCA.

Essentially these agreements would establish a framework under which entities resident in the relevant countries would be required to report certain information to their home country taxing authorities who would then share this information with the IRS under the exchange of information provisions in the relevant double taxation treaties. This would replace the position under which the US was going to require such entities to register for and directly comply with US legislation.

On 26 July the US Treasury, following on from that initial joint statement, released two versions of the Model I Intergovernmental Agreement (Model IGA) - one dealing with reciprocal information exchange where the FATCA partner country has an existing tax treaty or tax information exchange agreement with the US and one dealing with information exchange on a non-reciprocal basis where no such agreements exist. Under the Model IGA foreign financial institutions (FFIs) a FATCA Partner country will be able to comply with FATCA by collecting and reporting the information required to their home tax authorities rather than the IRS. Those FFIs will be deemed "FATCA compliant" and should not be subject to the 30% FATCA withholding on payments made to them.

On 12 September 2012 the UK became the first country to sign an IGA with the US to implement FATCA. This is significant in an Irish context as it increases the likelihood that Ireland will follow suit sooner rather than later. The text of the agreement closely replicates the Model IGA published in July with the addition at Annex II of a country specific list of financial institutions and financial products to be treated as exempt or deemed compliant for FATCA purposes. Among those non-reporting UK financial institutions listed at Annex II are certain UK Governmental organisations, the Central Bank, the UK offices of certain international organisations (e.g. of the IMF, World Bank and the EC), retirement funds, non-profit organisations (e.g. registered charities), credit unions, industrial and provident societies, friendly societies, investment trust companies etc.

Ireland has a comprehensive tax treaty with the US containing information exchange provisions. As such it is anticipated that Ireland will seek to 'come on board' with the reciprocal Model IGA. As early as April the Irish tax authorities announced they had commenced discussions with the US Treasury over a model agreement for implementing FATCA. It is now even more likely, in light of the published UK IGA, that Ireland will seek to conclude a similar agreement with the US. While there is no official timetable for those discussions it has been reported in various quarters that the Irish tax authorities are currently discussing with a number of representative organisations (e.g. the IFIA and Banking and Treasury Group) the categories of financial institutions and products that should be exempt or deemed FATCA compliant under an IGA with Ireland and with a view to concluding an agreement with the US before year end. It is likely that the UK list will inform Ireland's approach when negotiating Annex II to its proposed IGA with the US.

Once agreed it is anticipated that Irish domestic tax legislation will be amended later in the year to facilitate implementation of FATCA thereby enabling Irish funds and similar financial entities to collect and report the relevant information to the Irish tax authorities rather than direct to the IRS. The Irish tax authorities will then share this information with the IRS through the existing double taxation treaty arrangements.

EU Savings Directive

The EU Savings Directive may be relevant in the context of Irish funds which are UCITS, or deemed UCITS, where there are investments in underlying debt securities. The Directive requires the reporting of, or in the case of Austria and Luxembourg the withholding on, interest paid cross border to EU resident individual beneficial owners. This is EU derived legislation with a similar purpose to FATCA to prevent the avoidance of tax on a cross border basis.

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