Revenue Target Foreign Assets

Introduction

Finance Act 2016 was signed on 25 December 2016 and it provides for increased penalties on undisclosed income or gains on foreign assets.

Foreign assets include foreign rental properties or bank accounts. Essentially, any property located outside of Ireland is considered a foreign asset. If tax is due on income or gains relating to these assets, taxpayers have up to 30 April 2017 to disclose the tax liabilities and pay any tax outstanding if they wish to avail of the benefits of a "qualifying disclosure".

Revenue are closing off the ability to make a qualifying disclosure where there are offshore matters contained in the disclosure to encourage taxpayers with outstanding liabilities to make a disclosure in advance of 30 April 2017. The number of sources of information available to Revenue in respect of foreign income and gains has increased. Revenue will be using the new information available to target defaulting taxpayers. From 01 May 2017, the penalties applying to a disclosure will increase significantly.

The incentive for taxpayers is to minimise penalties, as the new regime applying from 01 May 2017 will be more penal.

Offshore Matters

A qualifying disclosure can be made where a taxpayer has an unreturned liability. The taxpayer must forward details of the liability together with payment of tax and interest to Revenue.

The benefits of making a qualifying disclosure by 30 April 2017 are that the tax penalties can be minimised and publication and prosecution can be avoided.

Revenue have published *FAQs on Qualifying Disclosures relating to Offshore Matters* and they have noted that it is not illegal to hold offshore assets but that if those assets were acquired using income or gains which were not returned to Revenue, or income and gains arising on foreign assets have not been returned to Revenue, there may be unpaid tax liabilities.

Penalties as low as 3% can be negotiated with Revenue if an offshore disclosure is made by 30 April 2017 but it is likely that Revenue would seek penalties of at least 75% if a disclosure is made on or after 01 May 2017.

New Regime from 01 May 2017

From 01 May 2017, increased penalties will be applied to any tax payments due and relating to offshore matters. Taxpayers will not be entitled to make a qualifying disclosure in respect of any outstanding liability relating directly or indirectly to:

- a bank account held or situated outside Ireland;
- income or gains arising from a source, or accruing, outside Ireland;
- property situated outside Ireland.

In addition, no protection from publication or prosecution will be available.

There are two main scenarios which can arise:

1. Funds are transferred abroad to hold in a foreign bank account or to invest in foreign assets without paying the Irish tax due on the income or gains e.g. untaxed trading income.

2. Income or a gain arising on foreign assets is not returned to the Irish Revenue, e.g. rental income from a foreign property.

In the case of scenario two, it may be that the income or gain is also taxable in the foreign jurisdiction and a tax credit may be available in respect of the foreign tax paid.

Foreign Tax Credits

Where Ireland provides a tax credit for foreign tax paid, no tax will be payable if the foreign tax is

"Significant changes and restrictions are coming into effect for any corrections that relate to matters outside the Republic of Ireland, or 'offshore matters' … The changes coincide with increased international co-operation whereby Revenue gets more and more information automatically from other jurisdictions. If this affects you … you should come forward and correct your tax returns by making a 'qualifying disclosure' before 1 May 2017. "

- Revenue 17 February 2017

Revenue Example

Revenue have provided an example showing the additional tax which would be due if a disclosure is not made by 30 April 2017. Revenue use an example of a sole trader who transfers untaxed trading income to Northern Ireland (€200,000).

The unpaid tax amounts to €114,800 and the example illustrates that if the disclosure is not made by 30 April 2017, the additional cost to the taxpayer could be €103,320.

This additional cost is due to the penalty increasing from 10% to 100%. Revenue also note that the taxpayer could be published as a tax defaulter and Revenue could take steps to prosecute him, if the disclosure is not made by 30 April 2017.

higher than the Irish tax. However, if the foreign tax is lower than the Irish tax, the taxpayer will end up paying the difference in Ireland.

It should be noted that in many cases, the Irish tax payable can be substantially higher than the tax abroad or there may be no tax payable in the foreign jurisdiction.

Differences in the Irish tax treatment of rental income as compared to the tax treatment abroad include the following:

- In Ireland, from mid 2009 to 2016 a deduction was only available for 75% of the interest paid on a mortgage. Many other jurisdictions will give an interest deduction for 100% of the interest paid.

- Under Irish tax law, no deduction is available for the capital cost of a property. However, some foreign jurisdictions will allow a deduction for the capital value of the property e.g. the United States.

- If all of a taxpayer's income is taxable in Ireland and only the foreign income is taxable in the other jurisdiction, the income may be taxed at a standard rate in the foreign jurisdiction, but at a higher rate in Ireland. This is on the basis that the total income taxable in the foreign jurisdiction is too low to be subject to the higher rates of tax.

Mismatches in tax treatment can result in a substantial differential between the tax paid in Ireland and the other jurisdiction, so that although tax is paid abroad, there is an additional amount payable in Ireland.

Applicable Penalties

Revenue consider the concealment of foreign income and assets to be *"deliberate behaviour"*. This means that the lowest penalty applicable to a qualifying disclosure of an offshore issue is 10%.

A taxpayer who is in a position to satisfy Revenue that the category of behaviour that applies is *"careless behaviour with significant consequences"* may be eligible for a penalty as low as 5%.

The lowest penalty available (3%) only applies where a qualifying disclosure is made, the taxpayer fully cooperate with Revenue and the category of behaviour that applies is *"careless behaviour <u>without</u> significant consequences"*.

Consequences are considered "significant" where the tax underpaid exceeds 15% of the tax correctly payable.

Onshore Matters

This new regime for matters arising in relation to assets, income and gains outside Ireland ("offshore") will also affect any disclosure which is made in respect of assets, income or gains in Ireland ("onshore") if offshore matters are known (or become known) to Revenue.

Offshore Information Available to Revenue

- Bank accounts
- Property (ownership, income and gains)
- Employment income
- Director's fees (company income)
- Life insurance products
- Pensions

From 01 May 2017, it will not be possible to avail of the benefit of a qualifying disclosure for an onshore disclosure, where offshore defaults arise. However, the Revenue FAQs indicate that a taxpayer will be able to make a qualifying disclosure for an onshore issue, where in relation to the offshore issue:

- the penalty applied was on the basis that it was careless behaviour and not deliberate,

- the taxpayer co-operated fully with any Revenue investigation

- the tax underpaid on the offshore issue was 15% or less of the total tax due.

Revenue have also confirmed that if an offshore disclosure was made and it dealt with all the offshore matters at that time and the disclosure has been finalised with Revenue, that this will not preclude a taxpayer from availing of the benefits of a qualifying disclosure on or after 01 May 2017.

Conclusion

Taxpayers should consider their tax position prior to 01 May 2017. If there are any issues which may give rise to unpaid tax liabilities relating directly or indirectly to offshore assets, income or gains, it is advisable to seek advice with a view to making a qualifying disclosure before 01 May 2017.

Offshore Disclosure Example:

Mary and Andy run a successful business and having paid off the mortgage on their Dublin property. They decide to sell it and move to Kerry.

After purchasing a small property in Kerry, Andy and Mary purchase a holiday home in Florida. Andy and Mary spend circa 8 weeks a year in Florida and the property is rented for the balance of the year.

Andy and Mary do not return the rental income from the US property in Ireland as they file a US tax return. However, no tax is paid in the US, as the US allow a deduction for the capital cost of the property.

The net rental income calculated for Irish income tax purposes over the 3 years from 2013 to 2015 is €82,000.

The marginal rate of tax for Andy and Mary was 55% (income tax, PRSI, and USC).

- The additional tax payable is €45,100.
- If Andy and Mary make an unprompted voluntary disclosure prior to 30 April 2017, the penalty is likely to be 10% (€4,510).
- If Andy and Mary make a disclosure on or after 01 May 2017, Revenue are likely to seek a penalty of at least 75% (€33,825).
- The additional cost to not making a disclosure before 30 April 2017 would be circa €29,315.

This calculation does not include the additional interest which will continue to accrue until the tax liability is paid (circa €10 per day).

It should be noted that in addition to the increased penalties the taxpayer may be published or prosecuted by Revenue, if the disclosure is made on or after 01 May 2017.

Caveat: *These notes are intended as a general guide only. OHT has endeavoured to provide an accurate commentary but the notes cannot cover all circumstances. OHT strongly recommends that formal tax advice be obtained before any steps are taken that may have a tax effect.*