

INDIRECT TAX

RELEVANT CONTRACTS TAX

The new eRelevant tax system

RCT – the new eRelevant Tax system

Relevant Contracts Tax (RCT) was introduced by Revenue in the early 1970s to address tax slippage in the construction industry. RCT imposes obligations on defined entities (Principals) to withhold 35% of certain construction related payments, in the absence of specific paperwork. The legislation was later extended to cover both the meat processing and forestry sectors. After 40 years in operation, it might seem that RCT would be second nature within these industries, but its obligations and deductions can still come as a surprise to many businesses operating within them. Though the paperwork can be complex, the idea behind RCT is relatively simple: when a payment is made to a subcontractor, the Principal retains 35% tax and is obliged 'to forward it directly to Revenue, unless the necessary paperwork is in place to allow the payment without deduction of tax'. This paperwork is only issued when a subcontractor is tax compliant and, in its absence, the subcontractor will ultimately reclaim any RCT deducted or offset it against other tax liabilities arising (VAT, PAYE/PRSI, etc.)

Liability

If a Principal neglects to deduct RCT, it is still liable to Revenue for any RCT that should have been deducted together with any related interest and penalties. A review of published Revenue defaulter lists over the past few years shows that this situation has arisen on a regular basis, mainly because businesses failed to recognise they were Principals. According to Revenue records, there are c.115, 000 registered Principals. In excess of 95% of these fall within the construction sector, meaning it is likely that quite a lot of these are not currently active. Although the RCT system has been relatively successful, time has caught up with what is a cumbersome administration process. In a review of the system over the last 18 months, Revenue has recognised its excessive bureaucracy must finally be addressed. Under the current system, every single payment made by a Principal

to a sub-contractor on which RCT is deducted requires the Principal to:

- Issue a deduction certificate to the payee
- Reflect the RCT deducted on the periodic RCT 30
- Pay any RCT reflected on the periodic RCT 30 to Revenue, and
- Show details of accumulated annual payments made to all subcontractors each year on Form RCT 35.

Revenue has also established that almost 50% of RCT deducted is subsequently refunded, making its collection and related repayments a poor use of Revenue resources. There is also a recognition that fraudulent repayment claims and other unorthodox practices have impacted on the credibility of the current system.

eRCT

In January 2012, RCT is set to become eRCT, with the paperwork surrounding it – C2 Cards, Relevant Payments Cards and Relevant Contracts Tax Deduction Certificates – consigned to history. Revenue has also decided that, as VAT is generally no longer charged by subcontractors to Principals, 20% is a more appropriate standard withholding rate, with the 35% rate reserved for contractors either unknown to Revenue or notoriously non-compliant. As with the current system, where a contractor can demonstrate a good track record of tax compliance to Revenue, the Principal will be e-vised (that is, advised on line) that no RCT deductions are necessary from any payments being made. The new system isn't about taking short cuts – every Relevant Contract must be registered online and advance instruction on the appropriate RCT rate to be applied must be requested in advance of each payment being made. However, once the system is fully operational, through ROS, much of the heavy lifting will be taken out of RCT compliance. A good example is the periodic RCT Return. In advance of each periodic eRCT filing,

Revenue will provide a pre-populated deduction summary, based on the information received from the Principal. By amending or verifying this and paying the tax due, the Principal will have met their obligations. In addition, once this return has been finalised, the sub-contractors' RCT deductions will be automatically credited to their tax records, and so will be immediately available for offset against VAT, payroll or tax liabilities. One downside of the proposed system is that RCT refunds will not be possible until the income/corporation tax return covering the period in question has been filed, although this provision is likely to be relaxed for 'non-chargeable persons'. The 0% deduction rate may also take some sub-contractors time to secure (particularly new and non-Irish based contractors), resulting in negative cashflow issues for a time.

Broad outline of new system

- Principals will be obliged to register all Relevant Contracts online and each of these contracts will be assigned a reference number.
- Revenue will e-visit an indicative deduction rate likely to apply to payments due under the contract at the time of its registration.
- Principal must notify Revenue online each time a payment is being made under a contract.
- Revenue will respond immediately ('real-time') with details of the RCT rate applicable and the Principal should provide a copy to the contractor, who can appeal the rate within 30 days.
- Contractors will continue to engage directly with Revenue as necessary to secure 0% or 20% deduction rate
- In advance of each periodic eRCT filing, Revenue will provide the Principal with a pre-populated deduction summary based on online communications of payments being made and RCT rates notified during the period.
- The Principal can confirm or amend this information in the course of e-filing the RCT

return for that period.

- Any RCT deductions reflected in the Principal's eRCT filing will be automatically credited to the contractor's tax records.
- RCT deductions can be offset against VAT or payroll tax liabilities or, ultimately, against income/corporation tax liability for the year.
- No RCT repayments are envisaged for 'chargeable persons' in advance of income/corporation Tax filing
- Consideration is currently being given by Revenue to periodic RCT refunds for 'non-chargeable persons'.

Information

All things considered, the new eRCT system is an excellent example of a Government agency maximising its use of resources and obtaining earlier and more accurate intelligence by better use of technology. This real-time information on what is happening in each of the three sectors to which RCT applies will help avoid duplication and assist Revenue to more effectively monitor compliance and better plan for the use of its increasingly scarce resources. From the industry's perspective, eRCT will be more transparent and a lot less cumbersome to operate. The different rates applicable should help alert contractors and, in particular, foreign contractors to the nuances of RCT system at an earlier stage and, thereby, enable them to commence working towards securing the 0% deduction status from Revenue. The thorny issue of businesses realising too late that they are Principals, and the obligations that arise with this, has not gone away and, as part of the new system, Principals must initially account for RCT at 35% in relation to any relevant gross payments that were inadvertently missed at the time of payment. After five years of decline, the construction sector is one still in the recovery mode. However, from January 2012, the Government will be able to monitor its heartbeat more accurately than ever before.

**FOR FURTHER INFORMATION
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