

Revenue Guidance Note on Exchange Traded Funds (ETFs)

The term “Exchange Traded Fund” or “ETF” is a general investment industry term that refers to a wide range of investments. ETF investments can take many different legal and regulatory forms even where they are established within the same jurisdiction.

An ETF is an investment fund that is traded on a regulated stock exchange. A typical ETF can be compared to a tracker fund in that it will seek to replicate a particular index.

There is no separate taxation regime specifically for ETFs. Being collective investment funds, they generally come within the regimes set out in the Taxes Consolidation Act 1997 (TCA) for such funds. However, even though ETFs are investment funds, they are traded on stock exchanges in the same manner as direct share investments in companies, and the units (shares) are held in a recognised clearing system. And they can have many different structures and regulatory oversights. This can cause some confusion as to the correct tax treatment to be applied. On the one hand, one of the specific regimes applicable to income and gains arising from investments made in collective funds may apply and, on the other hand, the general income tax and capital gains tax treatments that apply to dividends and chargeable gains arising from share investments may be applicable.

At the outset, it is acknowledged that, for non specialists, the tax regime governing collective investment funds can be regarded as complex. And insofar as it deals with ETFs as a component part of the collective investment funds industry, it is not any the less complex, which is due to the fact that it deals with ETFs that are domiciled in a wide range of countries, have many different legal structures and are subject to different regulatory regimes. Against that background, the aim of this note is to set out in a clear manner the tax treatment that Revenue will seek to apply to investments in ETFs held by investors that are tax resident in Ireland. In this regard, a brief description of some commonly used words and phrases may be helpful:

- The word “domiciled” is commonly used in the funds industry to indicate the country of origin of a collective investment fund, including an ETF.
- The term “Irish domiciled ETF” (or Irish ETF, for short) refers to ETFs that are established in Ireland and are regulated by the Financial Regulator.
- The term “non-Irish domiciled ETF” or “foreign domiciled ETF” refers to ETFs that are established in foreign countries and are regulated in their home countries. Therefore, for example, the term “US domiciled ETF” (or US ETF, for short) refers to ETFs that are established, and regulated in the United States.
- The term “investment fund” refers to collective investment funds, which are investment vehicles that are owned by the investors and which enables them to invest on a pooled or collective basis. Such funds are also commonly referred to as “collective investment undertakings” or “collective investment schemes.”
- The term “UCITS Directive” or “the Directive” refers to the European Union (EU) UCITS IV Directive that was adopted in 2009 and provides for the coordination of laws, regulations and administrative provisions relating to UCITS.
- The term “UCITS” refers to undertakings for collective investment in transferable securities.
- “EEA state” – refers to Norway, Liechtenstein and Iceland, which are contracting parties to the EEA Agreement with the member states of the EU.

1. Irish domiciled ETFs

In general, income and gains included in payments made from an Irish-domiciled investment fund to investors are subject to deduction of tax at source by the fund at the rate of 41%, which is a final liability tax and is commonly referred to as 'exit tax'. However, in the case of an ETF investment, because the units/shares in the underlying fund are bought and sold between investors on the stock market, tax cannot be deducted at source by the fund. The relevant legislation, therefore, places the onus on the investor to make a self-assessment tax return of the income and gains, including gains arising under the deemed disposal provisions, and to account for income tax at the rate of 41% on all such Irish-domiciled ETF-related income and gains. This 41% rate is applicable to income (dividends) and gains on disposals arising on or after 1 January 2014.

Such income and gains do not attract Pay Related Social Insurance (PRSI) or Universal Social Charge (USC) liabilities.

Irish stamp duty does not apply to the transfer of shares in Irish domiciled ETFs.

2. ETFs domiciled in EU countries other than Ireland

In the case of ETFs that are domiciled in EU countries other than Ireland, it seems to be the case that the majority of such funds are structured and regulated as UCITS under the UCITS Directive (as are the vast majority of Irish domiciled ETFs).

The tax treatment of such investments mirrors the tax treatment applicable to Irish ETFs. In other words, income payments (dividends) and gains on disposals are liable to income tax at the rate of 41% for payments arising on or after 1 January 2014. The investor is obliged to make a self-assessment tax return of the relevant income or gains, and to account for any tax liability arising.

Such income and gains do not attract PRSI or USC liabilities.

It is understood that in the case of EU domiciled ETFs that are regulated as UCITS the investor documentation (even at summary level) will clearly specify that the fund is a UCITS. This should simplify recognition of the investment for tax treatment purposes.

In the case of ETFs domiciled in EU countries other than Ireland that are not regulated under the UCITS Directive it is not possible to give other than a general guidance. However, that said, the Revenue view is that these ETFs should generally be regarded as similar in all material respects to the small number of Irish ETFs that are not regulated as UCITS under the Directive. This is on the basis that they would have comparable legal structures and would generally be subject to comparable regulatory oversight. Therefore, the tax treatment outlined above should apply to investments in such ETFs i.e. liability to income tax at the rate of 41% in respect of income payments (dividends) and gains on disposals, including gains arising under the deemed disposal provisions, with the relevant payments to be returned under the self-assessment system, and appropriate tax accounted for accordingly. And with no PRSI or USC liabilities attaching.

However, Revenue are prepared to look at the documentation in relation to any particular investment in such an ETF and to give a view as to the tax treatment to be applied in the context of the legal structure of the ETF and the applicable regulatory regime.

It should be noted that in the case of such investments in non-UCITS ETFs in other EU countries, it is always open to an investor and his/her tax advisors to take a different view to that outlined above and to make a tax return and account for tax (and any appropriate PRSI and USC) liabilities under the self-assessment system of taxation, with or without an expression of doubt in regard to the tax treatment disclosed on the return. This would be on

the basis of a detailed consideration, which would conclude that the structure and regulatory background attaching to such a fund would serve to take it out of the offshore funds meaning in section 747B (2A) TCA 1997, and would instead bring it in to the mainstream income tax and capital gains tax treatment that would apply to share investments generally.

Such tax returns will of course be within the normal audit procedures applied by Revenue to self-assessment returns generally.

3. ETFs domiciled in the US, EEA and other OECD countries

In the case of ETFs domiciled in the US, it is not possible to give other than a general guidance. This is because the details of underlying legal structure and regulatory oversight can be so different between one ETF product and another, with legal structures and regulatory requirements varying from state to state within the US. However, following detailed consideration, Revenue will accept that with effect from 1 January 2014 investments in such ETFs will be outside the tax regime attaching to investment funds.

On this basis, Revenue will accept that, in the case of investments made on or after 1 January 2014 in US ETFs, income payments (dividends) will be subject to income tax at the standard or higher rate as appropriate, and gains on disposals will be subject to capital gains tax. In other words, that such ETFs would not be regarded as having structures and regulation that would be similar in all material respects to Irish ETFs, which would then take them out of the tax regime applicable to offshore funds and instead bring them in to the mainstream income tax and capital gains tax treatment that would apply to share investments generally. And tax returns should be submitted, and appropriate tax payments should be made, accordingly.

It should be noted that such amounts assessable as income will attract PRSI and USC.

In the case of ETFs domiciled in an EEA state, or in an OECD member state (other than the US) with which Ireland has a double taxation treaty, Revenue are prepared to accept that, in the case of investments made on or after 1 January 2014, income payments (dividends) will be subject to income tax at the standard or higher rate as appropriate, and gains on disposals will be subject to capital gains tax. In other words, those ETFs will be treated as being outside of the tax regime attaching to investment funds. And tax returns should be submitted, and appropriate tax payments should be made, accordingly.

It should be noted that such amounts assessable as income will attract PRSI and USC.

4. Other ETFs – (Singapore, Jersey etc.)

In the case of ETFs domiciled in a country that is not an EU member state, an EEA state or an OECD member state with which Ireland has a double taxation treaty, taxpayers should consider, by reference to the relevant facts, whether such an ETF investment represents “a material interest in an offshore fund.”

It is the Revenue view that such an ETF investment would generally represent “a material interest in an offshore fund” within the meaning of section 743 TCA 1997 (it cannot come within the enhanced definition in section 747B (2A) TCA 1997), and accordingly is taxable by reference to the provisions of section 745 TCA 1997, i.e. income payments (dividends) and gains on disposals are subject to income tax at the standard or higher rate as appropriate, and tax returns and appropriate tax payments should be submitted accordingly.

It should be noted that such income payments and gains on disposals which are assessable as income will attract PRSI and USC.

5. Exchange Traded Commodities (ETCs)

ETFs are distinct from other types of exchange-traded product such as ETCs, which should be considered separately from ETFs, and on a case by case basis. ETCs are, typically, securities that track the prices of physical commodities such as gold, silver and platinum, and also track commodity indices based on commodity futures prices.

However, Revenue will accept that ETC investments are generally structured as debt instruments and accordingly, such an ETC investment will not come within the tax regime for offshore funds, but will instead come within general taxation principles, with any income payments being liable to income tax at the standard or higher rate as appropriate, and gains on disposals being liable to capital gains tax. This tax treatment may be applied to ETC investments made on or after 1 January 2014.

6. Companies

The intention of this note is to give guidance on tax treatment of ETF investments by individuals. But it is the Revenue view that the principles outlined will apply also to companies and other taxable bodies which are not dealers in such securities or which do not realise the receipts from such investments in the course of the conduct of a trade.

7. Deemed disposal provisions

In the case of ETFs in paragraphs 1 and 2 that come within the investment funds tax provisions, it should also be noted that a taxable event is deemed to take place on the ending of the 8 year period beginning with the date of investment in the ETF, and on every subsequent 8 year period. This is known as the "*Deemed Disposal*" and it applies to all investments that come within the special tax regime for investment funds, including ETFs. The effect of this provision is that the investor is obliged to account for tax on the same basis as would apply if the investment had been disposed of by the investor on that deemed disposal date. Whenever an actual disposal of an investment subsequently occurs, a tax credit is given for the tax paid on the deemed disposal event.

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