Response to consultation on Ireland's Tax Treaty Policy

7 May 2021

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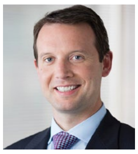

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7 May 2021

Dear Sir

Tax Treaty Policy Consultation

KPMG welcomes the opportunity to respond to this consultation on Ireland's Tax Treaty Policy. KPMG is the largest provider of business taxation advice in Ireland. We have drawn on our experience of providing advice to businesses across a range of sectors to provide comments to the consultation questions.

To date, Ireland has negotiated 74 double tax agreements. We welcome this achievement and encourage officials to continue to expand Ireland's tax treaty network as part of the effort to reboot the Irish economy through removing barriers to trade and maintaining Ireland's competitiveness in both exporting and attracting Foreign Direct Investment (FDI).

We have outlined below our response to the questions contained in the consultation in two sections, economic considerations and policy on developing countries.

The contact point for this submission is Tom Woods. Tom's contact details are: Email: tom.woods@kpmg.ie ; Direct telephone: (01) 410 2589.

Should you wish to discuss any aspect of the attached submission please do not hesitate to contact us.

Yours faithfully

Tom Woods

Tom Woods
Partner

Economic Considerations

There have been significant developments internationally regarding Corporate Tax Reform and Ireland has implemented or will implement provisions to prevent Base Erosion and Profit Shifting (BEPS). In negotiating any double tax treaty, Ireland should in our view ensure we meet minimum OECD standards whilst balancing the need to retain the effectiveness of the tax treaty network to support trade by Irish based business.

As noted in the Stability Programme update[1] in April 2021, international corporate tax reform could undermine Ireland's attractiveness as a location for inward investment. In the address by Minister Donohoe as part of the International Tax Seminar[2], as a result of international tax reform, Ireland's corporate tax receipts are expected to fall over the coming years. In this context it will be important that Ireland's tax treaty policy continues to adopt provisions that attract FDI and facilitate growth of Irish based businesses internationally.

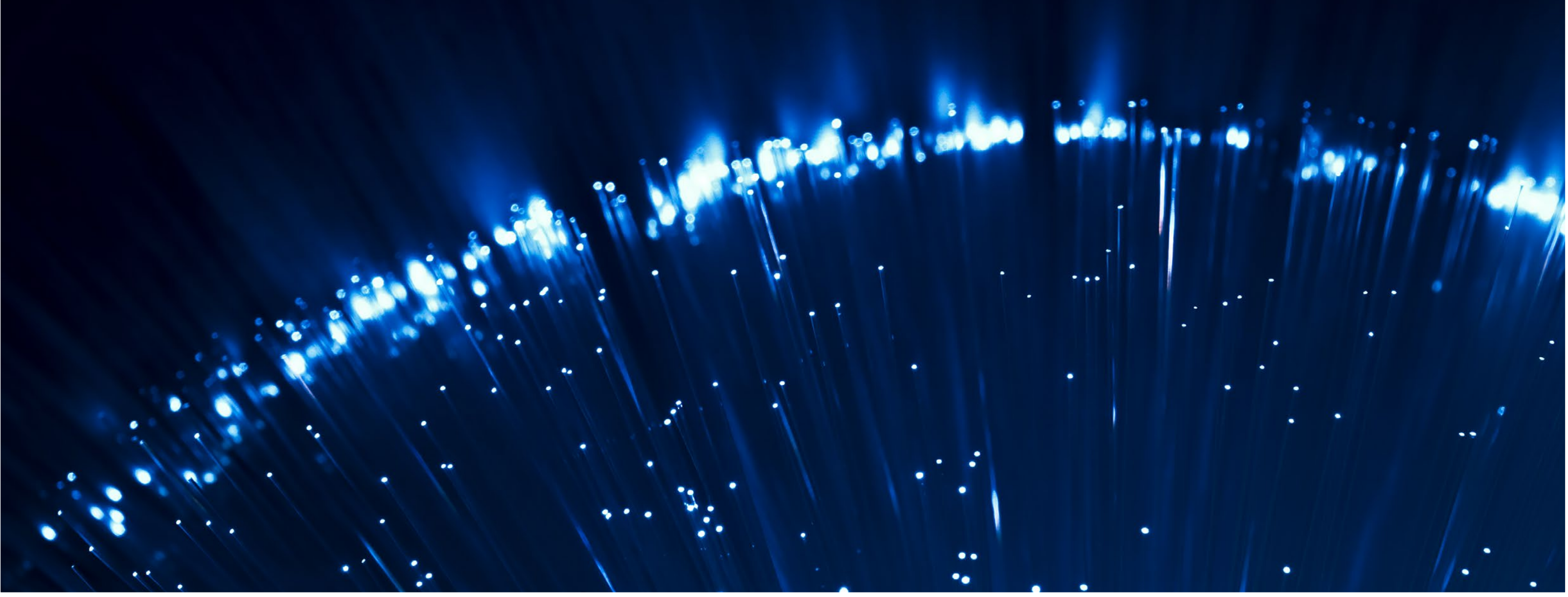
An expansive treaty network will provide an incentive for Irish based business to expand through growth in export markets. As a response to Brexit, expanding our treaty network further facilitates Irish SMEs from relying heavily on exports to UK markets and instead can gain access to other international markets. Importantly, we believe that an extensive treaty network also serves to incentivise senior executives who exercise management and oversight of the business with overseas jurisdictions at the most senior level by preventing double taxation. This will also ensure alignment of taxing business profits in the jurisdiction where the value is created, and the decisions are made.

Ireland should expand its treaty network in order to be the country of choice when seeking access to EU markets. Whilst remaining competitive with other European jurisdictions which have an expansive treaty network[3], Ireland should maintain the quality of the provisions included in its treaties when negotiating.

Since a main objective of tax treaties is the avoidance of double taxation in order to reduce tax obstacles to cross-border services, trade and investment, the existence of risks of double taxation resulting from the interaction of the tax systems of the two jurisdictions involved will be a primary tax policy concern.[4]

We recommend that Ireland's tax policy strategy should continue to seek certainty and stability for taxpayers in relation to international matters as it will encourage investment and trade. Trade and investment will also be facilitated where withholding taxes on cross border flows of money are minimised.

[1] Stability programme update 2021
[2] Speech by Minister for Finance, Paschal Donohoe TD, to Virtual Seminar on International Taxation
[3] UK have over 130 treaties, the Netherlands have over 100 treaties and Luxembourg have over 90 treaties
[4] OECD Model Tax Convention on Income and Capital



In line with Minister Donohoe's address at the international tax seminar in April 2021[5], we recommend that Ireland continues to engage constructively in any international tax reform and ensure any action taken by Ireland is implemented in tandem with other jurisdictions.

Ireland's treaty network will need to take account of emerging taxes, such as digital taxation and carbon taxes, ensuring they are covered as much as foreseeable so as to prevent double taxation.

Leasing

Ireland has a relatively unique position as a centre of excellence for international leasing activities. Irish based lessors (under international ownership) have substantial leasing operations based in Ireland that lease to international operators and receive leasing payments throughout the life of the lease that are potentially subject to tax in the lessee jurisdiction. Most countries accept that there should not be lessee jurisdiction taxes for aircraft and aircraft engine leases and that is what most of Ireland's tax treaties provide. Ireland should continue to seek this outcome in treaty negotiations and in those minority of cases where the lessee jurisdiction insists on levying some tax the rate should be no worse than that provided to other countries.

To further grow and support Ireland's international leasing activities, we recommend that Ireland seeks to negotiate or renegotiate a double tax treaty with several jurisdictions outlined below.

New treaties with the following jurisdictions:

- Indonesia
- Brazil
- Argentina
- Taiwan
- Colombia
- Bolivia
- Mongolia
- Myanmar
- Nigeria
- Philippines
- Sri Lanka

Renegotiate existing treaties with the following jurisdictions:

- Australia
- Japan

[5] Speech by Minister for Finance, Paschal Donohoe TD, to Virtual Seminar on International Taxation

- Malaysia

We also recommend that engine and helicopter lessors are entitled to the same benefits conferred on aircraft lessors under tax treaty provisions.

Fiscally Transparent Entities

Ireland should continue to adopt the article 3 provision in the Multilateral Instrument (MLI) which aligns with the broad Irish approach to treaty reliefs for transparent entities; looking to the residence status of partners/members and seek to establish if they are subject to tax on the income.

Funds

Ireland’s corporate funds require access to Ireland’s double taxation treaty network. To provide the taxpayer with certainty, Ireland should ensure that the meaning of “liable to tax” (at least insofar as the treatment of tax-exempt persons such as pension funds, charities, and regulated funds are concerned) is addressed properly in the treaty.

Irish transparent funds should be treated as transparent for the purposes of the treaty and treaty benefits should be afforded based on the membership/investors in those funds.

In recent years, Ireland has sought to include in its tax treaties (or protocols thereto) a statement that Irish common contractual funds (“CCFs”) are to be treated as transparent for the purposes of the treaty concerned. We endorse this approach and we recommend that this policy is expanded so that it covers both CCFs and investment limited partnerships (“ILPs”).

Shipping

Based on discussions with clients in the international freight shipping industry there is a strong view that a wider treaty network will support the growth and development of the sector in Ireland.

The context here is that Freight taxes are a barrier for businesses operating international fleets in the sector. The standard OECD International Shipping clause typically provides protection against the imposition of these taxes.

The countries the sector would benefit from having such a treaty with are:

- Argentina
- Brazil
- Colombia
- Ecuador
- India (the current treaty allows India to impose such taxes at one-third of the standard level)
- Indonesia

Dividends

To encourage free movement of capital and remove a barrier to trade, we believe that the object of treaty negotiations should be a zero withholding tax rate on dividends between associated entities. A zero withholding tax would be consistent with the introduction of a dividend exemption as part of a move to a territorial tax regime.

Royalties and Interest

To further encourage free movement of capital and remove a barrier to trade, we believe that the object of treaty negotiations should be a zero withholding on interest and royalties.

Mutual Agreement Procedure (MAP) and mandatory binding arbitration provisions

Ireland has chosen to adopt MAP and corresponding adjustment provisions as well as binding arbitration under the MLI provisions. Enhanced treaty dispute resolution measures under all our treaties including those potentially offered by an agreed arbitration mechanism would increase the fairness and effectiveness of treaties.

Given this is an important tax treaty policy provision to adopt, it will be important our tax administration is adequately resourced to deal with the quantum of disputes.

"Most Favoured Nation" Clause

To date Ireland has negotiated a most favoured nations clause with several jurisdictions[6]. The extent and application of this clause is dependent on the treaty and to date, has related to interest, royalties, and dividends.

A most favoured nation clause provides that where either jurisdiction enters into a double tax agreement with a third OECD jurisdiction on more favourable terms with respect to a specific article in the treaty, persons in Ireland will be able to claim the more favourable terms under the Irish tax treaty. We recommend, where possible, Ireland seek to negotiate a most favoured nations clause with all treaty partners.

Where this is not be possible, an alternative is to include a favoured nations clause that allows for renegotiation of the treaty where either country enters into more favourable terms with a third jurisdiction. This would not result in an immediate change to our tax treaty network but would provide the opportunity to renegotiate a more favourable treaty in the future.

Non-Discrimination rules

In addition to the above most favoured nation clause, to encourage and foster economic ties between countries, Ireland should seek protection from discriminatory tax treatment through adoption of the non-discrimination rules as contained in Article 24 of the OECD Model Tax Convention.

[6] Armenia, Chile, Estonia, Ghana, Latvia, Lithuania, South Africa, Switzerland, Ukraine, and United Arab Emirates

Permanent Establishment

We recommend that Ireland continues to reserve under Article 12 of the MLI on the relatively new test for when an agent can constitute a permanent establishment due to the significant uncertainty as to how this test would be applied in practice. The exact shape of how Pillar 1 will apply in the future also needs to be agreed. Furthermore, protections against BEPS are currently afforded under the preamble and the principle purposes test within the treaty.

Furthermore, Ireland's domestic taxing regime affords protections through operating a worldwide taxing regime, OECD transfer pricing, a controlled foreign company (CFC) regime and anti-hybrid provisions.

Developing countries

In July 2015, Department of Finance published a report 'IBFD Spillover Analysis Possible Effects of the Irish Tax System on Developing Economies'. The report indicated that there is no distortion of capital flows between Ireland and developing countries. Furthermore, the terms of Ireland's treaties with developing countries follow what is regarded as general best practice for treaties with developing countries.

This analysis is helpful, and we recommend that it is carried out periodically in the future as our tax treaty network with developing countries expands.

Withholding taxes

We believe that the recommendations above regarding withholding taxes apply for treaties with developing countries also. There is a negative correlation between withholding taxes and attracting inward investment and therefore, withholding taxes are not in the interest of developing countries. The protections afforded by the preamble, the principal purposes test (PPT) and exchange of information provisions should prevent base erosion and profit shifting.

Model Double Tax Agreements

Whilst several developing countries are participating in the Inclusive Framework and leverage from the OECD's model double tax agreement, the choice to follow the OECD treaty or the UN treaty will be dependent on the circumstances of the developing country and the tax treaty strategy they have in place. Ireland should be open to considering both types of model agreements going forward.

Tax Sparing provisions

As noted in the spillover analysis, some of our treaties with developing countries contain tax sparing provisions and these facilitate investment in developing countries[7]. These provisions allow developing countries to offer tax incentives (such as a tax holiday) without the benefit being lost. As Ireland uses the credit method to afford foreign tax relief, the inclusion of tax sparing provisions under a tax treaty can ensure that the benefit of tax incentives of the source country (in this instance the developing country) is maintained. We recommend that Ireland continues to include tax sparing credits for a set period of time.

[7] Papers on Selected Topics in Negotiation of Tax Treaties for Developing Countries Paper No. 1-N May 2013 Why Negotiate Tax Treaties

Treaties with developing countries

We recommend that Ireland negotiate tax treaties with as many developing countries as possible. In terms of prioritisation, the jurisdictions where significant trade is most likely are as follows;

- Argentina
- Bolivia
- Brazil
- Colombia
- Ecuador
- Indonesia
- Mongolia
- Myanmar
- Nigeria
- Philippines
- Sri Lanka
- Taiwan[8]

[8] As classified under the UN World Economic Situation and Prospects 2020 (un.org)

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