AMERICAN
CHAMBER of COMMERCE
IRELAND

Submission on The Consultation Paper on Ireland's Corporation Tax Code

January 2018

AMERICAN CHAMBER of COMMERCE IRELAND

SUMMARY

The American Chamber of Commerce Ireland's priority is that Ireland remains a unique transatlantic trade and investment gateway and a location of choice for US inward investment to Europe. The contribution of Ireland's corporate taxation environment to economic and employment growth has always been based on the certainty surrounding its rate, regime and reputation and it must continue to do so.

The Chamber is strongly supportive of Government's continued commitment to constructive engagement with the international tax reform agendas within relevant multilateral fora promoting international tax rules that are stable, predictable, non-discriminatory and administrable. Continuing to appropriately evolve the corporate taxation regime in response to a changing investment environment including the implementation of the OECD's BEPS agenda, reforms to the US tax code and further tax initiatives emerging from the EU is important to sustaining Ireland's competitiveness for inward investment and jobs.

In analysing the impact of the options open to Ireland outlined in the Department of Finance's "Update on Ireland's International Tax Strategy & Consultation on Coffey Review" in October 2017 the Chamber is strongly of the view that it is imperative that Ireland is not put at a competitive disadvantage vis-à-vis other EU jurisdictions.

Following extensive consultation with members, this submission proceeds based on the questions asked in the consultative document. The main points arising are as follows:

- **Controlled Foreign Company ("CFC") Rules:** Introducing CFC rules in a manner that, while meeting the minimum standards required by ATAD, does not put undue administrative burdens on companies operating from Ireland vis-à-vis other EU jurisdictions thus giving rise to unintended consequences for investment decisions. The options provided for in ATAD in considering what CFC income should be included in the Irish tax base are (1) a test that requires the examination of the nature of the income and activities of each CFC ("Option A"), and (2) a test that applies where "non-genuine arrangements" have been put in place for "the essential purpose of obtaining a tax advantage" ("Option B"). The Chamber recommends that the Department consider giving taxpayers a choice in legislation over which Option above applies when considering what CFC income should be included in the tax base.

- **Exit Tax Provisions:** The Chamber recommends that Irish tax legislation be updated to provided that, where the ATAD exit tax provisions apply, any gain arising should be subject to tax at the 12.5% corporation tax rate where the assets have been used as part of trade carried on in Ireland. In parallel, the Chamber believes that the introduction of new exit tax provisions requires that existing arrangements continue for investment decisions made prior to the introduction of these new provisions or that the capital gains tax "base cost" of assets already within the charge to Irish tax are rebased to their market value for the purposes of applying the new provisions.

- **Hybrid Mismatches:** The Chamber recommends that draft legislation to deal with Hybrids is published early and the Department of Finance engage in an ongoing consultation throughout the process with the

objective of securing clear statutory language on definitions and on operative rules, minimising the administrative burden and cost, and clear guidance on the requirements for the burden of proof and record retention requirements

- **Ireland's Transfer Pricing Regime:** In introducing the changes to Ireland's existing transfer pricing regime as promulgated by the OECD, it is critical that legislative amendments which may be forthcoming consider the overall impact for taxpayers in terms of dealing with such changes in conjunction with other taxation changes arising in future Finance Bills. It is recommended that any material updates to Part 35A of the Taxes Consolidation Act 1997 ("TCA 1997") are implemented in a co-operative manner with industry consultation, a defined roadmap of key changes and a proposed implementation timeline presented.

- **Territorial Regime:** The Chamber recommends that Ireland adopt a territorial regime for the taxation of foreign branch profits and foreign dividends. This will result in a regime, which is simpler to administer, with greater certainty in relation to the amount of Irish tax payable on profits and would make Ireland regime more competitive and easily understood internationally.

- **General Anti-Avoidance Rule(GAAR):** Aligning Ireland's GAAR provisions more closely with the provisions included in Article 6 of ATAD to give greater certainty to multinational taxpayers by providing conformity of these provisions across multiple European jurisdictions is recommended.

- **Resourcing Revenue:** It is critical that the Irish Revenue resources dedicated to dealing with dispute resolution matters (transfer pricing audit team and Competent Authority) continue to receive investment and training to engage effectively with Ireland's treaty partner jurisdictions in a timely manner.

The American Chamber will continue to monitor developments in international taxation. Our members are committed to working with the Government to offer our advice on how Ireland should engage with and respond to these discussions in a manner that seeks to maximise certainty, minimise administrative burdens and sustain competitiveness for investment and employment.

QUESTION 1

Article 6 of ATAD requires the transposition of a General Anti-Abuse Rule (GAAR) by 1 January 2019. As Ireland already has a robust GAAR, what changes, if any, are needed to ensure this meets the minimum standard required by the Directive?

At present, Ireland currently has broad based general anti-avoidance ("GAAR") provisions which are primarily based in Sections 811C and 811D TCA 1997. It is the view of the Chamber that these existing provisions currently meet the minimum standards required to be met under Article 6 of ATAD and accordingly our recommendation is that no further changes are required to Irish tax legislation in this context.

In our opinion the GAAR provisions currently in Irish law go beyond what is proposed under ATAD. Accordingly, it may be worthwhile considering whether the introduction of ATAD is an opportunity to more closely align Ireland's GAAR with the provisions included in Article 6 of ATAD. This would give greater certainty to multinational taxpayers going forward where there was conformity of these provisions across multiple European jurisdictions.

QUESTION 2

Article 7 of ATAD requires Member States to implement Controlled Foreign Company (CFC) rules by 1 January 2019. What are the key considerations regarding the implementation of CFC rules? In terms of the options for CFC legislation set out in Article 7, what are the key factors in determining the preferred approach for Ireland?

Given that Irish tax law does not currently include controlled foreign company ("CFC") rules, the introduction of Article 7 will be a significant change for most companies that operate in Ireland.

The Chamber is of the view that this impact will be heightened in Ireland when compared with other EU countries, as many other countries already have CFC provisions included in their tax law. At a minimum these provisions will significantly increase the overall compliance burden on most companies and on the Revenue Commissioners, and without careful implementation have the potential to give rise to a number of unintended consequences for Ireland.

As such, the Chamber is of the view that the introduction of this Article should be implemented in manner that, while meeting the minimum standards required by ATAD, does not put undue burdens on Irish companies.

Against this background, when introducing the provisions of Article 7, the Chamber believes that the following considerations should be taken into account:

- The options provided for in ATAD are (1) a test that requires the examination of the nature of the income and activities of each CFC ("Option A"), and (2) a test that applies where "non-genuine arrangements" have been put in place for "the essential purpose of obtaining a tax advantage" ("Option B"). The Chamber has discussed the two options in detail with members and the conclusion reached is that the Chamber view Option B as the more appropriate from an Irish perspective. In summary, this view has been reached on the basis that it allows Ireland to focus on scenarios where profits have been artificially diverted from Ireland and the Irish tax base. The alternative option would ultimately require Irish

companies to consider all activities of any subsidiary companies, regardless of whether any activity or oversight of such operations is undertaken from Ireland i.e. under this option Ireland would also seek to monitor activities that do not impact Ireland's tax base and which the Irish company has no oversight or control over.

- While having regard to the above point, given our initial comment around the significant impact that the introduction of this Article will have, the Chamber ultimately recommends that the Department consider giving taxpayers the option over which Option detailed in the first paragraph above applies when considering what CFC income should be included in the tax base. The Chamber is of the view that including both options would provide some limited flexibility to companies when applying the new provisions and would reduce the impact of the CFC provisions on genuine operations.

- The proposed implementation of this Article is 1 January 2019. Given the complexities of these provisions, it is important that companies have the opportunity to consider the relevant legislation, the impact that it will have on its operations and, in certain cases, have the opportunity to adjust to the new provisions. Accordingly, given that Ireland does not currently have CFC legislation, the timing of the introduction of this Article must be carefully considered. The Chamber recommends that the Department carefully consults with interested parties on the drafting of this legislation imminently with a view to giving clarity on the final provisions and timing of this legislation by June at the very latest.

- Given the compliance burden on both companies and the Revenue Commissioners that will come with this new legislation, and in line with the approach adopted in many other countries, the Chamber recommends that some specific "carve-outs" such that arrangements and operations which are not intended to be within the ambit of such legislation are clearly not within the application of the CFC provisions. In particular, the Chamber recommends the inclusion of the following "carve outs":

    1. As already provided for in Article 7, the CFC provisions should not apply to operations below a certain turnover/profitability threshold,
    2. As already provided for in ATAD, a list of countries where it is extremely likely that the operations undertaken are fully genuine and commercial should be included in the legislation such that, where a company is tax resident in that country, the CFC provisions would not apply. By way of an example, this list could include all EU countries and countries similar to the US.
    3. As detailed in Article 7, the CFC provisions should only apply to income earned by relevant CFCs. The implementation of the Article should clearly state that any other transactions, such as capital gains, should not be included in the CFC taxable base.

- In addition to the above points, the Chamber would like to highlight the following issues and considerations that should be borne in mind by the Department when introducing Article 7:

    1. The interaction of the application of the CFC provisions across multiple countries should be carefully considered. It would seem extremely inequitable for multiple tax charges to apply on the same income across a number of countries.
    2. When reaching a conclusion on the application of the CFC provisions, Article 7 provides that it is necessary to consider how the operations of a non-Irish subsidiary would be taxed if that entity was subject to Irish tax law. The compliance burden for companies in the very common scenario where several different subsidiaries exist across multiple countries could be significant. Steps that could be

taken to reduce this burden should be actively considered. For example, where a CFC tax charge is imposed in Ireland the tax rate should be consistent with that which would apply if the CFC activities giving rise to taxable income were undertaken in Ireland.

3. The introduction of Article 7 will likely introduce a number of definitions and concepts that are new to Irish tax law e.g. "substantive economic activity", "significant people functions", etc. In order to assist companies, the Chamber believes that it will be important that guidance is provided as quickly as possible on how these key terms will be interpreted.

QUESTION 3

Article 5 of ATAD requires Ireland to have an exit tax in four particular circumstances by 1 January 2020. Ireland currently has an exit tax which will be replaced by the ATAD exit tax. What are the key considerations in transposing Article 5?

The exit tax provisions included in Article 5 are aimed at addressing the transfer of assets or business outside of the Irish tax base in a number of specified circumstances. The Article provides that in the specific circumstances outlined, an entity should, for tax purposes, be regarded as disposing of the relevant assets at their market value, with any gain arising then subject to tax.

It is important to note that Irish tax legislation currently includes a number of provisions that seek to apply Irish tax where various assets are no longer within the charge to Irish tax, either by virtue of an actual disposal of an asset or by virtue of a "deemed" disposal (i.e. Section 627 TCA 1997). In many scenarios, Irish capital gains tax will apply to the relevant disposal thus meaning any gain is subject to Irish tax at rate of 33%.
When introducing the provisions of Article 5, the Chamber believes that the following considerations should be taken into account:

- While many of the "exit" scenarios envisaged in Article 5 are already taxable events under Irish tax legislation, there are certain scenarios which were not previously taxable but will become taxable with the introduction of Article 5. It is the view of the Chamber that the introduction of these new "exit" events will make Ireland a less attractive place to make investments and exploit significant assets due to reduced flexibility to restructure operations going forward given the Ireland's capital gains tax regime which would now apply in such exit scenarios. In order to limit the negative impacts of these provisions and to bring Ireland more in line with a number of other EU countries, we recommend that Irish tax legislation is updated to provide that where the ATAD exit tax provisions apply, any gain arising should be subject to tax at the 12.5% corporation tax rate where the assets have been used as part of trade carried on in Ireland.

- As the Department are aware, many companies have made significant investments in Ireland in recent years. When evaluating these steps, one of the issues considered by many companies was the existing Irish "exit tax" legislation in place. The introduction of Article 5 as drafted would impact these companies as the provisions would apply to all assets currently in Ireland. In order to take this into account, the Chamber recommends that the Department considers adopting one of the following approaches when implementing Article 5:

    1. Provisions are included such that the new Article 5 provisions would only apply to assets that have been brought into the charge to Irish tax after the implementation of Article 5. Ireland's

existing “exit tax” provisions could continue to apply to all assets within the charge to Irish tax before this implementation date, or

2. Provisions are included such that the capital gains tax “base cost” of assets already within the charge to Irish tax are rebased to their market value for the purposes of applying the provisions of Article 5. This would mean that only gains arising on such assets from the point following the introduction of Article 5 would be subject to the ATAD “exit tax”. Again, Ireland’s existing “exit tax” provisions would continue to apply to all assets within the charge to Irish tax before this implementation date. The Chamber understands that this approach would be similar to the approach adopted when Ireland first introduced Irish capital gains tax a number of years ago.

- The provisions included in Article 5 provide that when calculating the tax payable in an “exit tax” scenario, the deemed consideration received is the market value of the relevant assets at the time of exit. In considering the implementation of these provisions, the Chamber is of the view that it would be equitable to amend Irish tax law to reflect that when assets come within the charge to Irish tax for the first time (e.g. when a company becomes Irish tax resident, etc.), the “base cost” of such assets for Irish capital gains tax/”exit tax” purposes should be the market value of the assets at that time.

Question 4

“Article 9 of ATAD originally set out concise anti-hybrid rules, applicable to intra-EU payments. In February 2017, the ECOFIN Council agreed an amendment to ATAD, ATAD 2, which extended the hybrid mismatch rules to third countries. ATAD 2 delays the implementation date for the introduction of any anti-hybrid rules to 1 January 2020 and allows a longer period, until 1 January 2022, to implement the elements of the rules which target so-called ‘reverse hybrids’, a type of hybrid entity that is treated as transparent for tax purposes in the payor jurisdiction and a taxable entity in the payee jurisdiction. What are the key considerations regarding the implementation of the hybrid mismatch rules?”

We suggest that an important consideration of any new legislation should be to not cause any uncertainty or accidental damage. Legislation should include clear statutory language both on definitions and on operative rules The legislation being introduced should include clear statutory language both on definitions and on operative rules.

ATAD and ATAD 2 make clear that the intention is to give effect to BEPS Action 2, and indeed the Preamble to both documents makes specific reference to Action 2. The content of the Directives needs to be considered in detail in order to produce a set of legislative rules for Ireland that minimise uncertainty and accidental damage. We agree that the Action 2 documents should be used as the framework for this, and we recommend that the Irish legislation should take care not to go further than the Action 2 documents (including the July 2017 update on branch mismatches).

The legislation should also keep the administrative burden and costs to a minimum and provide clear guidance on the requirements for the burden of proof and for retention of records.

The new anti-hybrid rule should only apply to transactions which flow from a truly hybrid entity or hybrid financial instrument while at all times respecting the jurisdiction of the payee’s tax code. The definition of ‘structured arrangement’ in particular will need to be supplemented either with legislation or guidance.

Effectively an Irish company may be denied a deduction for a payment to an unrelated party where the Irish company could reasonably have been expected to be aware of a hybrid feature undertaken by the counterparty. This is a specific area where the burden of proof and administrative burdens need to be set appropriately.

The legislation being introduced should also take account of the both existing and proposed Irish tax law e.g. transfer pricing, CFC etc and not duplicate or unnecessarily complicate the overall Irish tax system. ATAD specifically states that it is not intended to create double taxation.

Cognisant of the experience of Hybrid legislation introduced in other jurisdictions e.g. the UK, we should learn from their experience and avoid the practical issues they are now facing. Our counterparties' experience shows that very technical and lengthy legislation is required and therefore we strongly recommend that draft legislation is published early and the Department of Finance engage in an ongoing consultation throughout the process.

QUESTION 5:

Following their adoption by the OECD Council in June 2016, the 2017 OECD Transfer Pricing Guidelines are now the appropriate reference point for transfer pricing rules. Recommendation 6 of the Review of Ireland's Corporation Tax Code states that "Ireland should provide for the application of the OECD 2017 Transfer Pricing Guidelines incorporating BEPS Actions 8, 9 and 10 in Irish legislation." When incorporating the OECD 2017 Transfer Pricing Guidelines, what are the key considerations?

In its 2015 report on Action 8-10: "Aligning Transfer Pricing Outcomes with Value Creation", the OECD requires the development of transfer pricing rules which create transfer pricing outcomes in line with value creation.
The Action 8-10 report results in a substantial revision of the 2010 OECD Transfer Pricing Guidelines ("the 2010 Guidelines"), in particular revised guidance in chapters I, II, VI, VII and VIII. These material changes are included in the updated 2017 OECD Transfer Pricing Guidelines ("the 2017 Guidelines"). The OECD indicates that the report provides additional further clarification to existing rules but it is clear that the 2017 Guidelines represents a substantial revision of the 2010 Guidelines with the introduction of new concepts and not merely further clarification of the existing guidance. In addition, guidance for key sectors (for example financial services) remain outstanding and the OECD are working on guidance relating to the application of BEPS principles, including Action 8-10, to financial transactions (such as guidance relating to group synergies and the issue of passive association/implicit support and contractual allocation of risk), profits splits, profit attribution, digital business etc.

Our members have observed that this has led a number of countries to defer adoption of the 2017 Guidelines and/or implement at different rates and in different way. The Chamber believes that Ireland should adopt the same considered approach to full implementation of Action 8-10 taking into account the final draft of guidance that has achieved consensus at OECD level. In the Chamber's view, adoption of the 2017 Guidelines should be deferred until 2019 or 2020. when more certainty in relation to guidance on profit splits and application to certain sectors such as the financial services sector is forthcoming and also interactions with other tax changes can be more clearly understood

To the extent that Action 8-10 is implemented in Ireland at a future point, a number of key issues to consider in relation to amending Ireland's domestic transfer pricing law as contained in Part 35A TCA 1997 are outlined below.

(i) The commencement of application of Action 8-10 for domestic audit purposes.

The OECD view is that the 2017 Guidelines provide more clarity in relation to the application of the arm's length principle. On that basis many tax authorities are using the Action 8-10 principles in audits for past periods. The 2017 Guidelines are in fact a material change with Chapter VI of the 2010 Guidelines rewritten and the introduction of new concepts such as the right to receive intangible ("IP") related returns and performance of key functions known as DEMPE functions.

The right to receive IP related returns is based on the functions performed, assets used and risks assumed in the development, enhancement, maintenance, protection and exploitation ("DEMPE") of intangible assets. In accordance with the changes contained in Chapter I of the 2017 Guidelines, the assumption of risk relating to DEMPE activities, in particular the management and control of risk with respect to those activities, is intended to drive the entitlement to IP related returns.

As these concepts are new and taxpayers would not have considered them in past periods when establishing transfer pricing policies, once Ireland's domestic transfer pricing rules are updated, clarity in relation to which periods the revised law applies to is critical for companies. Companies would have put in place arrangements with a view to adhering to prevailing transfer pricing principles such as the 2010 Guidelines and the Chamber's view is that it is unreasonable to expect that prior periods would be audited using the new principles contained in Action 8-10.

(ii) Interpretation of Action 8-10 principles for dispute resolution purposes

The premise adopted by the OECD as contained in Action 8-10 is that members of a multinational group ("MNE") should be allocated compensation for functions performed, assets used, and risks assumed. In the context of IP, this approach gives priority to important functions (DEMPE functions) that contribute to the creation of the value from IP. In order for the legal owner of intangible assets to be entitled to the returns from exploiting the IP, it must perform key DEMPE functions. The premise of Action 8-10 is that bare legal ownership does not provide the right to retain all of the IP related returns arising. The IP related return in excess of a risk-free / risk-adjusted return are attributable to people functions rather than the provision of capital and any excess economic returns should be allocated to parties who perform key DEMPE functions and manage and control the key risks.

The foundation of the arm's length principle is that related parties should transact with each other under in a similar manner as to how independent third parties operate. In the context of Action 8-10, there is evidence from members to support the view that the providers of capital receive more than a risk-free (or risk adjusted) return for ownership or participation in an investment. In the private equity sector for example, the role of limited partners is typically passive in nature and limited to the provision of capital. They do not make any key investment decisions; these functions are undertaken by others usually the general partner. In the sector, a 2/20 fee structure is in place whereby the private equity firm receives a 2% management fee plus 20% fee on a fund's profits. The balance of 80% is generated by the passive investor or limited partner who provides the capital. Based on real market conditions, it is important not to downplay the critical role of capital when considering the new Action 8-10 principles.

Regarding the allocation of returns from exploiting IP, the Action 8-10 report does not seek to recharacterise legal ownership of intangible assets from the legal owner. The new guidelines outline how members of a multinational

group performing important functions, controlling economically significant risks and contributing assets should be remunerated by way of an appropriate return reflecting the value of their contributions.[1] Therefore, it is clear that it is the legal owner of the IP is the party which must allocate any IP related profits to other group companies to adequately compensate those companies for their contributions. To the extent that an Irish company in the group is not the legal owner of the IP, it should not be responsible to perform such allocations or retain profits over and above what it is entitled to as determined by transfer pricing rules. An Irish company may sub-license IP rights from an IP company to develop in a particular market. Once the Irish company is adequately compensated for its functions, risks and assets, the license fee payment to the IP owner should be respected for Irish tax purposes.

Upon audit, the principles outlined in the Action 8-10 paper as contained in the 2017 Guidelines need to be considered bearing in mind the positon of the Irish group company in the entire value chain and the relevant group company which is responsible for allocating IP related returns under Action 8-10. In many circumstances the arm's length return for the Irish company can be determined by way of one of the five OECD approved methods such as the Transactional Net Margin Method ("TNMM") or Comparable Uncontrolled Price Method ("CUP"). In many circumstances the TNMM or CUP method will be the most reliable method to use where the Irish company is performing routine functions and is not undertaking DEMPE functions or managing and controlling key risks. The use of other methods such as the profit split method should only be used as a last resort where other methods are deemed less reliable.

This consideration is equally applicable in tax disputes involving the Irish company and a foreign related party. Where a transfer pricing adjustment arises, the Mutual Agreement Procedure ("MAP") is invoked involving both the Irish and foreign tax authorities to ensure double taxation is avoided. The role of the Irish Competent Authority is critical in this new environment. The Chamber recommends is that the Irish Competent Authority needs to be adequately resourced and trained to ensure that Ireland's tax base is protected where such challenges arise.

QUESTION 6:

The Coffey Review recommends that "domestic transfer pricing legislation should be applied to arrangements the terms of which were agreed before 1 July 2010."

What are the key considerations regarding the implementation of this recommendation?

With the introduction of Ireland's transfer pricing regime on 1 January 2011, the legislative provision governing related party transactions included provisions for certain arrangements in place before 1 July 2010. With that certainty provided, many groups took the opportunity before 1 July 2010 to formalise their related party transactions. In that context, the Chamber is of the view that such existing arrangements put in place where a defined term was agreed should be allowed to continue until the end of the relevant term in the agreement.

The preparation of transfer pricing documentation is an expensive and time-consuming exercise and many groups, especially smaller groups, took this opportunity to cement longer term arrangements to manage costs and resources. In most instances, the transactions were routine in nature such as low risk service transactions. Changes now will have a disproportional effect on smaller groups and we recommend that consideration be given

[1] Paragraph 32, Chapter VI of 2017 Guidelines.

to retaining the current provisions until at least 2020. This provides adequate time for companies to prepare and plan ahead to deal with the new principles contained in the 2017 Guidelines.

QUESTION 7:

The Coffey Review recommends that *"consideration should be given to extending transfer pricing rules to SMEs, having regard to whether the concomitant imposition of the administrative burden associated with keeping transfer pricing documentation on SMEs would be proportional to the risks of transfer mispricing occurring."*

If Ireland is to introduce transfer pricing rules for small and medium sized enterprises1 (SMEs) what are the key considerations? Should all enterprises be subject to transfer pricing rules or should the scope of the rules exclude entities below a certain threshold? If Ireland introduces transfer pricing rules for SMEs what would be the appropriate documentation requirements?

Ireland's current transfer pricing law exempts certain SMEs from the requirement to prepare transfer pricing documentation[2]. The exemption is an EU based exemption - Commission Recommendation 2003/361/EC. The exemption was introduced by the EU as SMEs are considered as key to ensuring economic growth, innovation, job creation, and social integration in the region. In addition, we believe that it is the Commission's overarching commitment to ensure such groups operate in a business-friendly environment.

The preparation of transfer pricing documentation is an expensive and time-consuming burden for smaller groups. Many of these smaller groups have limited resources to devote to complex transfer pricing issues and the availability of the SME exemption provides certainty to such groups in relation to what resources they need to plan ahead for.

The SME exemption is used by many other EU jurisdictions in their domestic transfer pricing laws to provide a measure of relief from the burden of having to prepare transfer pricing documentation. Any change in Ireland's approach to SMEs from a transfer pricing perspective disadvantages smaller groups who are striving to expand domestically and internationally and the priority should be to ensure such groups can expand without undue additional burdens such as transfer pricing obligations.

To the extent that any amendments to Ireland's domestic transfer pricing law arise as a result of the consultation, consideration should be given to reducing the compliance burden placed on the SME sector. In its Action 13 report, the OECD recommends that SMEs should not be required to produce documentation that might be expected from larger enterprises[3]. On that basis, the Chamber is of the view that any change in our law should ensure that thresholds are introduced, and simplified documentation requirements are in place[4].

QUESTION 8:

The Coffey Review recommends that "consideration should be given to extending domestic transfer pricing rules to non-trading income. There is a strong rationale to extend domestic transfer pricing rules to non-trading

[2] Section 835E, TCA 1997.

[3] Paragraphs 32-34 of Action 13 on materiality.

[4] For example, France new rules since the end of 2016 introduced simplified documentation for small and medium groups with annual turnover or gross assets exceeding €50m. French companies that are part of a multinational group in which one entity has annual turnover or gross assets in excess of €400m are obliged to have available full transfer pricing documentation in the form of Master File and Local File.

income where it would reduce the risk of aggressive tax planning. Consideration should also be given to extending transfer pricing rules to capital transactions, having regard to whether such an extension would improve the existing provisions which already apply arm's length values to companies' transactions relevant to chargeable gains and capital allowances."
In relation to the extension of transfer pricing rules to non-trading income, what are the key considerations of this proposal?
In relation to the extension of transfer pricing rules to capital transactions, what are the key considerations of this proposal, bearing in mind existing market value rules?

Ireland has had two corporation tax rates in place since 1 January 2000 with the introduction of a 12.5% rate for trading income and 25% for passive income. The new transfer pricing enhancements introduced from 1 January 2011 is confined to trading transactions only. The extension of transfer pricing laws to include non-trading transactions brings into focus Ireland's corporation tax regime and issues related to whether operations are considered trading or non-trading in nature. The Chamber recommends that extending Ireland's transfer pricing law to non-trading income should be deferred until a full review of this aspect of the corporation tax regime takes place. At the time when the 25% passive rate of corporation tax was introduced in 2000, the rate could be considered as competitive by international standards. The worldwide average statutory corporation tax rate, measured across 202 tax jurisdictions, is 22.96% with Europe having a regional average of 18.35%[5]. Today, this 25% rate is uncompetitive and a review needs to consider whether this rate should be abolished and the 12.5% rate applied to all income heads Case I to V of Schedule D.

In certain circumstances, Irish companies extended interest free loans to other group companies arising from the generation of excess funds from operations. One of the recommendations is that Ireland's domestic transfer pricing law be amended to bring interest free loans within Ireland's transfer pricing law. It is important to point out that such loans in many cases arise due to the fact that Irish companies have excess cash from trading operations which are on-lent intergroup to maximise efficiencies and fund ongoing development of the overall activities of the multinational group. The granting of an interest-free loan in such cases from an affiliate should not be considered as a loan with a profit motive.

When considering whether an interest-free funding transaction constitutes a loan, there are a number of important point to consider relating to the form of the transaction:

(i) Whether in substance the financing is actually equity and hence no interest would arise;
(ii) Whether in substance the financing provided is a loan but the thin capitalisation position of the borrower means that no interest would be imputed; or
(iii) Whether in substance the financing provided is a loan and the borrower is not thinly capitalised and interest should be imputed using arm's length principles.

In many situations a funding balance may be treated as equivalent to a contribution to equity. The 1979 Report of the OECD Committee on Fiscal Affairs entitled "Transfer Pricing and Multinational Enterprises" provides that: *"Since for tax and other reasons equity contributions may be disguised as loans, a distinction has to be made between the two. Where it is determined that a financial transaction is a contribution to the equity of an enterprise, it follows that no interest is due."*

In many countries, it is recognised in business, law and accounting that capital can be made available in more than one form – equity contribution. It is therefore imperative to consider whether the transaction is intended by

[5] Source: taxfoundation.org - Corporate Income Tax Rates around the World, 2017

the parties to have the character of capital or a loan. Any changes to Ireland's transfer pricing rules needs to be cognisant of this matter.

The extension of transfer pricing principles to such financing transactions leads to uncertainty regarding whether the 12.5% or 25% rate of corporation tax is applicable and hence the importance of updated guidance on what activities are taxed at 12.5% or 25% as discussed above. Many such interest free loan arrangements are between two Irish tax resident companies and to the extent that transfer pricing rules are applied, an important change needed to Ireland's domestic transfer pricing law will be to update Section 835G TCA 1997 to ensure no double taxation arises.

Section 247 TCA 1997 provides for the deduction of charges on income against total profits of a company. Many Irish groups have existing structures in place where funds are on-lent by one company to a second company. In many cases, the income derived by the first company on lending to the second company and the interest expense of the second company do not fall within the scope of Ireland's transfer pricing laws as presently enacted on the basis the income and associated expense is not a Case I or II trading item. To the extent that Ireland's transfer pricing law is amended to include non-trading income, consideration needs to be given to ensuring that no double taxation arises where an adjustment arises to increase/decrease the interest income/expense to an arm's length amount. Section 835G TCA 1997 as currently enacted, provides a measure of relief for transactions between two domestic Irish companies by allowing a corresponding adjustment to avoid double taxation. Amendments to this section would be required where Ireland's transfer pricing law is changed to include non-trading transactions. In many cases where interest as a charge arises, the lending Irish company or "the first named person" as noted in Section 835G(1)(a) would not be taxed under Case I or II of Schedule D. This subsection would need to be amended to include all cases of Schedule D.

In relation to extending Ireland's transfer pricing rules to capital transactions, there is an existing body of tax law that deals with the taxation of capital gains.

- Section 547 TCA 1997 deals with the imposition of market value for actual consideration given or received on the transfer of an asset.
- Section 548 TCA 1997 contains rules for determining market value of assets.
- Section 549 TCA 1997 contains anti-avoidance provisions where assets are transferred between connected parties. Such transfers are treated as made at market value.
- Section 913 TCA 1997 provides for a statutory obligation on taxpayers to provide information in relation to the acquisition of assets, details of persons from whom assets were acquired and the price at which assets were acquired.

To the extent Ireland's transfer pricing rules are extended to capital transactions, a conflict will arise in relation to which sections of the tax acts take precedence and how to interpret two sets of rules. It is contended by the Chamber that the existing law dealing with the taxation of capital transactions is sufficiently robust and the imposition of an additional layer of law would be complex and burdensome to manage. It is noteworthy that the UK transfer pricing legislation as contained in Part 4 of Taxation (International and Other Provisions) Act 2010 ("TIOPA") does not apply to the calculation of chargeable gains/losses. Instead, market value rules may be imposed under the Taxation of Chargeable Gains Act 1992.

QUESTION 9:

The Coffey Review recommends that "there should be a specific obligation on Irish taxpayers who are subject to domestic transfer pricing legislation to have available the transfer pricing documentation outlined in Annex I and II of Chapter V of the OECD 2017 Transfer Pricing Guidelines to ensure implementation of BEPS Action 13." Since May 2016, Annex I and II of Chapter V of the OECD Transfer Pricing Guidelines contain a list of the information which should be included on the master file and local file respectively. When providing for Annex I and II what will be the effects for business?

In its Action 13 report "Transfer Pricing Documentation and Country-by-Country Reporting" issued in October 2015, the OECD notes three objectives of transfer pricing documentation:

1) To ensure taxpayers can give appropriate consideration to transfer pricing requirements in establishing prices and other conditions for transactions between associated enterprises and in reporting the income derived from such transactions in their tax returns;
2) To provide tax administrations with the information necessary to conduct an informed transfer pricing risk assessment; and
3) To provide tax administrations with useful information to employ in conducting an appropriately thorough audit of the transfer pricing practices of entities subject tax in their jurisdiction.

The current transfer pricing documentation requirement in Ireland's domestic transfer pricing law is considered sufficiently robust to satisfy the OECD objectives noted above. The new two-tier Master File / Local File approach as promulgated in Action 13 contains most of the key elements that current robustly prepared documentation should contain. Together with other information in the public domain and held by tax authorities on companies from tax filings, it is considered that the imposition of a new set of documentation rules is unnecessary and adds to the compliance burden and cost for taxpayers to adhere to.

To the extent that Ireland's transfer pricing documentation rules are amended to align with the Action 13 two-tier approach, there are a number of important aspects that need to be considered:

- Ireland's current transfer pricing documentation rules allow for counterparty documentation to satisfy requirements under Part 35A TCA 1997. This provision should be allowed to continue to ensure that where related party transactions involving Irish companies are sufficiently documented by an affiliate company in another jurisdiction to ensure that additional cost and burden is not placed upon the Irish taxpayer.

- Not all transactions that occur between related parties are sufficiently material to require full documentation in a Local File. Paragraph 32-34 of the Action 13 OECD report recommends that Individual country transfer pricing documentation requirements should include specific materiality thresholds to account for the size and nature of the local economy, the importance of the multinational group in that economy, the size and nature of local operating entities and overall size and nature of the multinational group. Measures of materiality may be considered in relative terms or in absolute amount terms. It is recommended by the Chamber that Ireland align with this approach to the extent Action 13 two-tier transfer pricing documentation is introduced.

- The OECD recommends that SMEs should not be obliged to produce the amount of documentation that may be expected of larger enterprises. As previously discussed, the current positon of SMEs under Ireland's transfer pricing regime should continue. However, to the extent that transfer pricing

documentation rules are extended to include SMEs, a reduced compliance burden should be placed on such companies.

- In relation to the frequency of updates to transfer pricing documentation, the OECD recommends that documentation be periodically reviewed to determine whether functional and economic analyses are still up to date and that the Master File and Local File should be updated annually. Consideration should be given to providing more guidance on this to the extent Ireland's documentation rules are updated. It is recommended that for Irish purposes, the Master File and Local File should only be updated to the extent there is a material change in the functional and risk profile of the parties to a transaction. In addition, in order to simplify compliance burden on taxpayers, benchmarking searches should only be required to be updated every three years and not on an annual basis.

The interaction with other potential tax changes as discussed in the Consultation Paper is also critical to consider. Article 7 of the Anti-Tax Avoidance Directive ("ATAD") requires Member States to implement Controlled Foreign Companies ("CFC") rules by 1 January 2019. The key considerations are discussed earlier in this submission but the interaction with transfer pricing principles is a key issue to consider.

Chapter 3 of the OECD BEPS Action 3 report "Designing Effective Controlled Foreign Company Rules" outlines policy considerations and objectives which underlie CFC rules which are of relevance in the context of implementing CFC rules. These considerations include interaction with transfer pricing rules. To the extent CFC rules are introduced in Ireland, relevant changes to Ireland's domestic transfer pricing law will need to be enacted to ensure double taxation does not arise.

QUESTION 10

With the introduction of CFC rules under Article 7 of ATAD, the Coffey Review recommends that "consideration should be given to whether it is appropriate to move to a territorial corporation tax base in respect of the income of the foreign branches of Irish-resident companies and, in respect of connected companies, the payment of foreign-source dividends."
Would moving to a territorial corporation tax base be a positive development for Ireland? What would be the effects for Ireland of such a move?
To what extent does Ireland's ultimate choice of how CFC rules are implemented under Article 7 of ATAD impact on the question of moving to a territorial corporation tax base?
The Coffey review recommends that should Ireland not move to a territorial corporation tax base, Schedule 24 should be simplified on a policy and tax neutral basis. Could such a simplification be an appropriate alternative to a territorial corporation tax base, particularly in the context of specific CFC implementation choices? How might such simplification be achieved?

Current taxation of foreign branches and foreign dividends

Irish resident companies are subject to corporation tax on worldwide profits including the profits of foreign branches. Companies are then entitled to claim credit relief for foreign corporate income tax suffered on trading profits of foreign branches. Differences in the timing and measure of taxable profits between Ireland and the foreign branch jurisdiction can give rise to considerable complexities in claiming the credit relief. Where Irish companies pay tax on trading profits at 12.5%, in most cases no additional Irish tax should arise.

Ireland exempts from corporation tax dividends received from Irish resident companies. Foreign dividends are subject to corporation tax at either the 12.5% or 25% rate. Credit relief is available for both for foreign withholding taxes suffered on the payment of the dividend and corporate taxes paid on the profits out of which

the dividend is paid. However, considerable complexity exists in both tracing the source of foreign dividends received in Ireland and evidencing the availability of credit relief.

In most cases, additional Irish tax is not paid on branch profits or foreign dividends. It is not expected that moving to a territorial regime (see below for features) would result in significant loss to the Irish exchequer. It would however mean that Ireland would move to a regime which is more comparable to many of our European and near neighbours, including the UK, and help to make Ireland a more competitive holding company location.

The benefits of moving to a territorial regime for foreign branch profits and foreign dividends

The Chamber is of the view that adopting a territorial regime for the taxation of foreign branch profits and foreign dividends would result in a regime, that is simpler to administer, with greater certainty in relation to the amount of Irish tax payable on profits, and that is more competitive and easily understood internationally. As it stands, it is the Chamber's view that the complexity of the current regime often deters international companies from using Ireland as a head office or holding company location.

While branch structures have not tended to be used extensively outside of the financial services industries, the Chamber expects that as a result of changing business practices and indeed the changing understanding of what constitutes a permanent establishment, it is expected that branches are likely to become more prevalent operating models for international companies.

Chamber members know based on experience to date, that those companies that operate branch structures can suffer differences in the timing and measure of taxable profits when determining the profits which are subject to tax in the branch territory and Ireland. For businesses based in Ireland this can create significant uncertainty as to whether sufficient credit relief will be available in a particular year. Complexity can also arise where there are losses. Businesses based in other European countries with exemption-based regimes do not face this challenge. In that context it is important that we address the complexity now and adopt an exemption/participation exemption-based regime.

The adoption of a branch exemption regime in addition to an exemption regime for foreign dividends would also equalise more closely the Irish tax position of companies choosing to conduct their businesses through a branch and a subsidiary company. At present, branch profits are taxed in the current period, whereas the profits of foreign subsidiaries are only taxed when repatriated. Equalising the tax position of business conducted through branches with that of subsidiaries is more the norm throughout the EU. It reduces the potential for discrimination to arise where businesses choose one operating model over the other for non-tax/commercial reasons which seems to make good business sense.

Outline of suggested Irish branch exemption regime

In the Chamber's view an exemption from corporation tax should be available to profits arising from a genuine economic activity conducted through a foreign branch in any jurisdiction outside Ireland. It would be prudent to consider excluding countries which do not meet acceptable corporate tax governance standards. Based on our review of other international exemption regimes, we have set out below the key features of a proposed regime:

- The branch exemption would be available to profits arising from a genuine economic activity conducted through a foreign branch in any jurisdiction outside Ireland.

- The branch exemption would cover all foreign branch profits (income and gains) from such genuine economic activity. In addition to income, it would also include gains arising on the disposal of branch assets.

- Ireland's CFC regime (covered earlier) would also apply to the profits of foreign branches which are subject to an exemption regime.

- The branch exemption would only be available where the branch is recognised as having a taxable presence in the foreign jurisdiction, and is subject to tax, in the foreign jurisdiction.

- Relief would not be available for foreign taxes where the exemption regime applies.

- Ideally in order to afford taxpayer flexibility, especially on the transition, the branch exemption regime should be available at the election of companies. This could mean that, even after adoption of the regime, existing branches could remain taxed in Ireland on a worldwide basis should the company choose not to make an election for a branch exemption. Alternatively, consideration could be given to introducing the exemption regime as the default position, with and election to tax and secure credit if this worked better with the rules which will now apply in the US under the provisions of the US Tax Reform. Further consideration may be required to determine which alternative takes precedence. Transitional measures would also be required to deal with losses.

We believe that the combination of design features outlined above would achieve the desired result by simplifying the regime and afford companies certainty, at the same time as protecting the Irish tax base.

Dividend exemption regime

The Chamber suggests that a dividend exemption regime would have the following characteristics:

- Would apply to dividends received by an Irish company from a foreign company where the Irish resident company has a direct or indirect interest of at least 5% in the foreign company from which the dividend is sourced.
- Similar to the branch exemption, the dividend exemption would apply to dividends received from companies resident in all countries. It would be prudent to consider excluding countries which do not meet acceptable corporate tax governance standards.
- To be eligible for exemption, the dividend (which may be tracked through any number of intermediary layers of a company) should be paid by a company which is resident for tax purposes in a qualifying jurisdiction i.e. in a jurisdiction with which Ireland has a double tax treaty in place.
- A dividend exemption should not be available where the payor has secured a tax deduction for the dividend.
- Tax relief would not be available for taxes (direct or withholding tax) suffered on dividends where the exemption regime applied.

To what extent does Ireland's ultimate choice of how CFC rules are implemented under Article 7 of ATAD impact on the question of moving to a territorial corporation tax base?

A CFC regime should extend to both the profits of tax exempt foreign branches as well as subsidiaries which are more than 50% owned by an Irish resident company.

The Chamber believes that the recommended model of CFC that Ireland should adopt is well aligned with a foreign branch and foreign dividend exemption regime as discussed earlier in this paper regarding the application of the CFC provisions

Should some of the profits of a foreign branch or of a foreign subsidiary be subject to current taxation under the CFC regime, the profits can be repatriated on a tax-free basis whether from the branch or from a subsidiary (if it is based in a qualifying jurisdiction). Where the subsidiary is not based in a jurisdiction which is eligible for the exemption from corporation tax on dividends, it would be necessary to ensure that profits already taxed in Ireland under the CFC regime are not subject to tax again when repatriated as dividends.

Simplification of Schedule 24 if Ireland does not move to a territorial corporation tax base

If Ireland does not move to adopt a territorial tax base for foreign branch profits and foreign dividends, then a number of changes should be made to improve the operation of the credit relief regime for foreign branch profits:

- Amend the legislation to ensure that corporate income tax paid on branch profits which is in excess of the Irish capacity to absorb credit relief, because for example of losses in the Irish company as a whole, is available as a corporate expense deduction (under section 81, TCA 1997) in the same way as other business expenses might be.
- Amend the calculation of the unrelieved foreign tax in Para 9FA to ensure that credit relief is made available for foreign taxes on branch profits on a pooled basis in all cases (including where there are tax adjusted losses in the Irish company).
- Consideration should be given to moving to the calculation of credit relief by reference to the local nominal or standard rate of tax.

In the case of the operation of credit relief for foreign dividends, the following simplifications are suggested:

- Permit taxpayers to track and attribute the credits related to dividends solely by reference to a taxpayer election which is not required to be mirrored in dividend resolutions based by the paying company. Under current legislation it can be very difficult if not practically impossible to align dividend declarations and resolutions under foreign law with the provisions included in our tax credit legislation.
- Update Paragraph 9I, Schedule 24 to reflect evolving case law insights from the UK courts on the interpretation of the decision handed down in the FII case[6] to conforming the taxation of dividends from Irish resident and non-resident sources and where possible simplify the operation of relief/calculation under this provision.

These are the principal measures suggested on Schedule 24 as they relate to foreign dividends and foreign branch profits.

Double tax credit relief for royalty income

If changes are to be made to Schedule 24 to simplify and afford more certainty to tax payers, the provisions related to securing relief for withholding tax suffered on royalties should also be amended. We are not suggesting that foreign royalties would benefit from any form of exemption regime. Rather we are calling for an overhaul of the provisions relating to credit/relief from foreign withholding taxes suffered on royalties, to simplify and make them fit-for-purpose.

Specifically, with Schedule 24 and the related provisions, there is an opportunity to provide a more coherent and user-friendly mechanism for securing relief for withholding tax suffered on both royalty, and services income. The Chamber would welcome dialogue with the Department on the business scenarios where improved provisions would enhance the attractiveness of Ireland to retain and grow investment and employment.

[6] Test Claimants in the FII Group Litigation [C-35/11 and C-446/04]

Ireland's credit relief regime for royalties (and services fees where relevant) could be made more effective in affording relief for foreign taxes borne on royalty income by introducing a regime which would allow the company to:

- calculate the net income measure (which operates to limit the amount of credit relief) by reference to net margins from the royalty profits instead of by reference to the margins of the trade as a whole,
- offset excess unused credits against other income of the trade,
- pool surplus tax credits to carry forward for use in future periods (in a similar manner to the operation of the current pooling relief for foreign dividends and branch profits – in lieu of claiming a deduction or where there is limited capacity to deduct.),
- extend the provisions of Paragraph 9DB to cover service fees (not just royalties) which have suffered withholding tax, and
- clarify that where relief is not available under the credit or unilateral credit provisions, that relief is available under the general principals of Section 81, recognising the withholding tax as the business expense it is.

It is important in the current phase of international tax reform that tax payers secure clarity and certainty in relation to the approach to relief for withholding tax on royalties and service fees and that the rules are streamlined and simplified to sustain and attract investment and business operations in Ireland.