PUBLIC CONSULTATION

REVIEW OF THE CORPORATION TAX CODE

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INTRODUCTION

OVERVIEW

At BDO we focus on entrepreneurial and growing businesses in Ireland. As such, our clients consist primarily of Small and Medium Enterprises ("SMEs"), many of whom are involved in international operations, such is the nature of business today. As a member firm of the BDO global network, we also work with many large multi-national operations.

We have prepared our response to this consultation taking into account the potential impact on our clients, particularly those in the SME sector. It is important that any new changes and provisions introduced strike the right balance between targeted anti-tax avoidance without creating unnecessary and burdensome administration for taxpayers.

SUMMARY OF RECOMMENDATIONS

In summary, our recommendations are:

- Draft legislation to implement any proposed changes should be introduced as early as possible and subject to consultation and discussion with industry and practitioners to ensure that legislation does not have unintended consequences. Draft legislation should be released outside of the current budget process as October – December is too restrictive a timeframe for such extensive legislative changes as will be required to implement BEPS/EU ATAD.

- While there are existing GAAR provisions, it might be reasonable to align the Irish GAAR with that proposed under EU ATAD. This could give more certainty to taxpayers over the medium-to-long term as guidance could be sought from EU case law on interpretation of a GAAR that is consistent across the EU, rather than only having Irish case law as guidance.

- We recommend Option B for implementation of CFC rules into Irish law. For our SME clients in particular it will be important that there are de minimus limits which can be applied in determining potential CFC exposure in order to minimise the administrative burden on those clients. A "substantive economic activity" exclusion should also be included with a clear definition of the term.

- Legislation on the implementation of Anti-Hybrid provisions should be clearly drafted with definitions which are aligned with existing definitions already contained in Irish tax law (where possible). The definitions contained in the directive are not aligned to Irish tax law and would make interpretation of the legislation in Ireland difficult.

- The existing exclusion for SME's from transfer pricing should be kept in order to minimise the administrative burden on SME's.

- To the extent that transfer pricing is extended to SME's, reduced documentation requirements should be introduced for the SME sector.

- Where transfer pricing is extended to non-trading transactions, an exemption for domestic transactions should be included.

- Transfer pricing should not be extended to capital gains as the existing legislation already contains market value substitution for related party transactions.

- It is our strong recommendation that we move to a territorial system for branch and dividend income in order to increase Ireland's tax competitiveness. To the extent that a partial territorial system is introduced (e.g. with restrictions for say non-EU/DTA sources) a simplification of Schedule 24 should also be undertaken.

- Simplification of Schedule 24 should be carried out for other sources of foreign income not subject to territorial system (e.g. interest and royalties).

GENERAL ANTI-AVOIDANCE RULE

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?

BDO Response:

While we consider that our existing GAAR should be sufficient to meet the minimum standard required by the Directive, we also believe that there is merit in considering alignment of our existing GAAR with that provided under the Directive.

A persisting issue with our domestic GAAR has been the interpretation of same over the years. We recognise that the replacement of Section 811 of the Taxes Consolidation Act 1997 ("TCA 1997") with Section 811C TCA 1997 in Finance Act 2014 sought to address this issue, however, the introduction of the "new GAAR" means that there is currently no published Irish case law which has considered the interpretation of Section 811C.

For our clients, as is the case for all taxpayers, certainty in the interpretation of tax law is vital. Where our domestic GAAR is aligned with that of each of the other Member States of the EU, Irish taxpayers should be able to take guidance from the interpretation of that same legislation in those other jurisdictions. This is already the case for many other examples of EU tax law. This should provide welcome clarity to taxpayers.

CONTROLLED FOREIGN CORPORATION

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?

BDO Response:

Irish tax law does not contain any general CFC rules, therefore, the concept of introducing such rules into Irish tax law is novel and will be a significant issue for Irish taxpayers operating internationally. Therefore, it is vital that any new rules introduced are clear and unambiguous, and achieve the outcomes desired from such rules without creating any unnecessary administrative burden for impacted taxpayers.

In this regard, our preference is for the introduction of option (b), rather than option (a). The primary reason for this is the presence under option (b) of an objective de minimus limit (refer paragraph 4, Article 7).

Furthermore, we would recommend that this de minimus limit should be applied as a first step and in priority to carrying out the exercise required under Paragraph 1(b). In this regard, Paragraph 1(b) requires that the Irish parent company must first establish whether the actual corporation tax paid by the subsidiary / permanent establishment ("PE") is lower than the difference between the corporation tax that would have been charged on the entity / PE under Irish tax rules and the actual tax paid by the entity / PE. Performing this calculation is an involved process and creates significant additional administrative burden for Irish companies with foreign subsidiaries or branches. In order to ensure that this calculation is only required to be performed in respect of targeted CFC's, the aforementioned de minimus limits should first be applied. This would allow Irish taxpayers to exclude their smaller foreign entities from the scope of the new CFC rules from the outset.

This would be particularly important in the SME sector where foreign operations are less likely to breach the thresholds set out in Article 7, Paragraph 4.

Ireland's competitiveness as a holding company location must also be considered in the drafting of an Irish CFC regime that meets the minimum standard required. In this regard, we should consider the inclusion of a "white list" of acceptable subsidiary jurisdictions (potentially consisting of all EU and DTA countries).

Furthermore, in order to have clarity in the interpretation of the new rules, it will be important that any new terms introduced into Irish tax law have clear definitions which are aligned, insofar as possible, with terminology already contained in Irish tax law.

Finally, we would strongly recommend that draft legislation for the introduction of CFC rules into Irish tax law is published as soon as possible given the effective date of 1 January 2019 in order to allow taxpayers and their advisors sufficient time to prepare their systems and processes, and to evaluate the impact of the new rules on their group structure.

ANTI-HYBRID RULES

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?

BDO Response:

As mentioned elsewhere in this submission, clarity in interpretation of new legislation is vital. In this regard, legislation implementing Anti-Hybrid provisions should be clearly drafted with definitions which are aligned with existing definitions already contained in Irish tax law, insofar as possible. The definitions contained in ATAD 2 are not aligned to Irish tax law and would make interpretation of the legislation in Ireland unnecessarily difficult.

Furthermore, we would strongly recommend that draft legislation for the introduction of anti-hybrid rules into Irish tax law is published as soon as possible in order to allow taxpayers and their advisors to consult with the Department of Finance on the draft legislation in order to minimise uncertainty and unintended consequences.

TRANSFER PRICING

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?

BDO Response:

Consideration should be given to the impact of the removal of the grandfathering provision on tax revenues. In our experience, there are few remaining inter-company arrangements of non-SME clients which rely on the grandfathering provisions as business models change and evolve over time. We commend the inclusion of the grandfathering provision when transfer pricing was first introduced and would welcome similar provisions in the introduction of other new tax rules. Grandfathering is important as it means that new tax legislation does not have retrospective effect, which is important in ensuring stability and certainty in tax law. It also allows time for taxpayers to assess the impact of changes in tax law on their business, and prepare for new administrative requirements.

We therefore recommend that grandfathering provisions remain in place.

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?

BDO Response:

Our strong recommendation is that the SME exemption should not be removed from Irish transfer pricing legislation. We do not believe that the risk of transfer mispricing and associated impact on tax revenues would justify the administrative burden that transfer pricing requirements would impose on SMEs.

Furthermore, we note that many other jurisdictions have SME exemptions as a feature of their transfer pricing legislation. For example, in the UK the general rule is that transfer pricing does not apply to SMEs. However, there are conditions attached to the exemption. For example, the SME exemption does not apply to transactions with connected parties if the connected parties are in territories where the UK does not have a double tax treaty with an appropriate non-discrimination article. Also, for medium sized enterprises HMRC can apply to have the SME exemption dis-applied (this would usually happen in circumstances where they feel that some abusive tax avoidance is taking place). Furthermore, SMEs themselves can also elect to be outside the exemption so that they can make transfer pricing adjustments.

Other jurisdictions have different variations of the SME exemption. For example, in Germany the requirement to comply with transfer pricing legislation is based on the volume of inter-company transactions rather than the size of the group.

If it is decided to remove the SME exemption, we would recommend that a partial removal only applies such that the removal is targeted towards higher risk businesses, for example, those engaged in business with say non-treaty jurisdictions, or those undertaking large volumes of connected party transactions.

Furthermore, consideration should be given to introducing grandfathering provisions for a specific period of time (for example, 5 years) so that SMEs have time to assess the impact of the changes on their business and put the necessary documentation in place.

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 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?

BDO Response:

Where transfer pricing is extended to non-trading income, we would recommend that any rule change is targeted towards instances where the exclusion is currently being, or has the potential to be, used for aggressive tax planning.

In particular, we see little benefit in extending transfer pricing to non-trading transactions undertaken between domestic companies. For example, an interest-free loan between two Irish taxable entities. We would, therefore, recommend that such transactions should remain outside the scope of Irish transfer pricing legislation.

Our existing tax legislation contains market value substitution for capital assets sold between connected parties. Therefore, we do not see a rationale for the extension of transfer pricing to capital transactions.

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?

BDO Response:

Where transfer pricing rules are extended to SMEs, the simultaneous introduction of master file and local file reporting would place an unreasonable administrative burden on SMEs without a corresponding benefit to tax revenues. Therefore, if the SME exemption is to be removed it would be vital that reduced documentation requirements would apply for the SME sector.

Other countries already have such rules as a feature of their transfer pricing requirements. For example, in the Netherlands, the OECD 3-tier documentation guidelines have already been incorporated into their domestic legislation. However, the master file and local file requirements only apply to domestic companies which are part of a multinational group with a consolidated turnover in excess of €50m. A Dutch company which is part of a group which does not exceed that threshold is still required to document its intercompany transactions and to be able to substantiate these as being in line with the arm's length pricing. However, in general, this documentation is simplified and does not contain the level of detail required under the master file, local file requirements.

TERRITORIAL SYSTEM

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?

BDO Response:

It is our strong recommendation that Ireland move to a territorial corporate tax base for branch and dividend income.

Not having a foreign dividend exclusion, in particular, places Ireland at a competitive disadvantage internationally as many of our competitor countries have such an exemption as a feature of their domestic law. For example, the Netherlands offers a full tax exemption for foreign dividend income where the participation exemption applies. Germany offers a full tax exemption, with a 5% add-back to allow for non-deductible expenses. The UK offers an exemption for foreign dividends received by large and medium-sized companies, and by small companies in certain cases.

Due consideration should be given to the likely impact of introducing such an exclusion on tax revenues. In our experience there is generally little or no incremental Irish tax payable on the receipt of foreign dividend income, unless it has been received from zero-tax or non-treaty countries. However, the calculation of foreign tax credits available (to include the pooling of credits) is very complex. If a territorial system is introduced there may be merit in applying conditions to any exemption such that the Irish tax take is protected. For example, Ireland may wish to consider introducing an exclusion that would only apply where the dividend is received from an EEA or treaty jurisdiction, or where Ireland's participation exemption (section 626B TCA 1997) would apply.

Similarly for branches, we would recommend that Ireland move to a territorial corporate tax base in order to improve our international tax competitiveness and reduce the compliance burden. Again, it may be advisable to attach conditions to any exemption introduced to protect against any potential misuse of the exemption.

Regardless of whether a territorial system for branch and dividend income is introduced or not, we would still recommend that simplification of Schedule 24 is undertaken as the Schedule is overly complex with different rules applying for different income sources. For example, excess foreign branch credits can be carried forward, while excess credits on interest and royalties cannot. Credit pooling is available for branches and interest (inter-company only) but only deduction pooling is available for royalty income.

Furthermore, to the extent that new exemptions are introduced for branch and dividend income, but with conditions attached, the existing provisions which would continue to apply for non-exempt income should be simplified.

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