Irish Tax Institute

January 2018

Response to the Department of Finance "Consultation on Coffey Review"

Table of Contents

1. About the Irish Tax Institute 3
2. Executive Summary 4
3. List of recommendations 7
4. Response to consultation questions 9
4.1. Controlled Foreign Company rules 9
4.2 Moving to a territorial corporation tax base 17
4.3 Transfer Pricing 18
4.3.1 Adoption of OECD 2017 Transfer Pricing Guidelines 18
4.3.2 Extension of transfer pricing rules to pre-1 July 2010 arrangements 20
4.3.3 Extension of transfer pricing rules to SMEs 22
4.3.4 Extension of transfer pricing rules to non-trading transactions 24
4.3.5 Documentation 26
4.4 General Anti-Avoidance Rule 30
4.5 Exit tax 31
4.6 Anti-hybrid rules 33

1. About the Irish Tax Institute

The Irish Tax Institute is the leading representative and educational body for Ireland's Chartered Tax Advisers (CTA) and is the only professional body exclusively dedicated to tax.

The Chartered Tax Adviser (CTA) qualification is the gold standard in tax and the international mark of excellence in tax advice. With over 5,000 members in Ireland, along with the Chartered Institute of Taxation UK and The Tax Institute of Australia, we are part of the 28,000-strong international CTA network and a member of the Confédération Fiscale Européenne, (CFE) the European umbrella body for tax professionals.

Our members provide tax education and expertise to thousands of businesses, multinationals, and individuals in Ireland and internationally. In addition, many hold senior roles within professional service firms, global companies, Government, Revenue, state bodies and the European Commission.

After 50 years, the Institute remains deeply committed to the role it can play in education, tax administration and tax policy in Ireland and in building an efficient and innovative tax system that contributes to a successful economy and society. We are also committed to the future of the tax profession, our members and our role in serving Ireland's taxpayers and best interests in a new international world order. Our *Irish Tax Series* publications and online database *TaxFind* are respected and recognised as Ireland's most extensive tax information sources.

Irish Tax Institute - Leading through tax education.

2. Executive Summary

The Irish Tax Institute welcomes this opportunity to engage with the Department of Finance on the two areas of the Coffey Review[1] where public consultation was recommended. Namely:

- Ireland's commitments under the OECD Base Erosion and Profit Shifting Project (BEPS) and the EU Anti-Tax Avoidance Directive (ATAD)[2]; and
- Delivering tax certainty and maintaining competitiveness.

A range of questions are included in the Department's consultation paper, all of which have been addressed below. However, the two most significant issues are:

1. The Implementation of a Controlled Foreign Company (CFC) regime in Ireland, for the first time; and
2. The introduction of wide-ranging changes to Ireland's transfer pricing regime.

A CFC regime for Ireland

ATAD requires that all EU Member States must have in place an operational CFC regime by 1 January 2019. This is the first time that Ireland, and indeed many other EU Member States, will have a CFC regime and it has the potential to impact widely on a very broad range of taxpayers.

The principles of good tax policy design dictate that policy choices should match the particular circumstances of a country's overall economic strategy. For Ireland, this means that any changes we make when introducing a CFC regime must fit within the framework of Ireland's International Tax Strategy.[3] Indeed, the ATAD recognises that each Member State will develop CFC rules that are in line with their own policy priorities.

Two broad policy approaches to taxing the income of a CFC are permitted under the ATAD. Option A considers the nature of the income in the CFC and whether it is passive (as opposed to trading) income, whereas Option B is primarily focused on whether the CFC is engaged in artificial/non-genuine activities. The choice that is made between Option A and Option B is critical to selecting the most appropriate CFC regime for Ireland.

The aim of the new CFC regime should be to deter companies from shifting profits out of Ireland and into a CFC location, thus eroding the Irish tax base. Addressing this type of behaviour is the primary focus of the Option B model. For this reason and also because Option B is consistent with global transfer pricing methods, the Institute view is that Option B is the most appropriate model to adopt. Such an Option B model would have to comply with EU jurisprudence and the "Four Freedoms", as examined at 4.1 below.

[1] Review of Ireland's Corporation Tax Code, presented to the Minister for Finance and Public Expenditure and Reform by Mr Seamus Coffey, June 2017

[2] Council Directive (EU) 2016/1164 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

[3] Update on Ireland's International Tax Strategy, October 2017

The main disadvantage of an Option A regime is that it could result in broad swathes of income being treated as CFC income, regardless of whether or not that income has any Irish nexus. This clearly would impact on the competitiveness of the Irish regime, particularly given the high 25% rate that is charged in Ireland on passive income.

Although the cost of administering an Option B regime may be higher than Option A, due to the more subjective nature of the test in Option B, this should not be the determining factor in making a choice on the model.

What is absolutely critical to the implementation of a new CFC regime is that taxpayers can obtain certainty from Revenue about their treatment under the regime. Although an Option B regime is the most appropriate choice for Ireland, its viability, attractiveness and sustainability will be severely compromised if a high degree of subjectivity is allowed to develop.

Reaching the best decision on this issue is a difficult and complex matter as different taxpayers will be impacted in a variety of different ways. Further discussion with companies and other stakeholders is essential in order to be fully informed about the consequences of each option before any final decision is taken by the Government.

Transfer Pricing

Businesses in Ireland have been operating OECD transfer pricing rules since 2011. The Coffey Review recommended that there be a public consultation on a number of aspects concerning the Irish transfer pricing regime.

The Institute fully supports the implementation into Irish law of the OECD BEPS Actions 8-10, through the adoption of the 2017 OECD Transfer Pricing Guidelines.

In addition to the updated OECD Guidelines, Mr Coffey recommends consideration of four other features to the Irish transfer pricing regime:

1. On the possible extension of transfer pricing rules to SMEs, the Institute does not believe that SMEs are engaged in high value transactions and therefore this administratively burdensome measure would be disproportion to any tax risk arising.

2. A range of provisions in tax law currently exist to ensure that market value applies to related party capital transactions. Layering transfer pricing provisions on top of these existing measures would place a significant burden on taxpayers in situations where the tax risk has already been addressed.

3. Mr Coffey also recommends that transfer pricing rules are extended to non-trading income where a risk of aggressive tax avoidance exists. Because Ireland has a separate 25% corporation tax rate for non-trading income, a risk exists that mismatches and double taxation could arise, if these rules are broadened. Care therefore needs to be taken in dealing with this structural aspect of the Irish corporate tax regime.

4. If the Government decides to extend transfer pricing rules to transactions that existed pre-1 July 2010, the Institute agrees with Mr Coffey that a reasonable timeframe would be needed to enable businesses to comply with this measure.

To conclude on transfer pricing; the changes to the transfer pricing that need to be implemented are wide-ranging and therefore, it is important that a reasonable timeframe be provided for businesses.

Conclusion

As recently acknowledged by the IMF and OECD in their report on tax certainty *"…legislative and tax policy design issues are a major source of tax uncertainty, mainly through complex and poorly drafted tax legislation and the frequency of legislative changes."*[4]

Given the importance of all the anticipated changes to the corporate tax code over the next 2 years, it is an imperative that we address this problem of tax uncertainty by consulting widely, not only on the policy choices required but also on draft legislation and Revenue guidance well in advance of the measures commencing.

[4] Tax Certainty, IMF/OECD Report for the G20 Finance Ministers, March 2017

3. List of recommendations

Controlled Foreign Company (CFC)

1. It is our view, that an Option B approach which focuses on CFC income that is diverted from Ireland would, on balance, be a proportionate response to profit shifting risks in an Irish context and therefore, an appropriate tax base for an Irish CFC regime.

2. In designing an Option B type regime, it is important that an appropriate substance-based test and targeted exemptions support its application, to ensure it is proportionate in addressing BEPS risks and does not infringe EU fundamental freedoms.

3. As a broad range of taxpayers will be affected by the introduction of CFC rules in Ireland, it is essential that all stakeholders are given the opportunity to consult well in advance on draft legislation and draft Revenue guidance. The UK spent 5 years consulting on their CFC regime before opting to introduce a CFC regime based on an Option B type approach.

4. Investment in dedicated Revenue resources to deal with the increased administrative burdens of the CFC regime is essential.

Territorial regime

5. Ireland should move to a territorial regime with a participation exemption for dividends and foreign branches when CFC rules are introduced into Ireland.

Transfer Pricing

6. A reasonable lead-in time should be given for the 2017 OECD guidelines. This would allow Irish businesses adequate time to assess the impact of the guidelines on their operations and for Revenue to publish clear and comprehensive guidance on how they will administer the transfer pricing rules under the new framework. A well-resourced Competent Authority will also be vital to deal with the increase in international disputes and Mutual Agreement Procedures that are likely to occur.

7. If the grandfathering provisions are removed from Irish transfer pricing legislation, businesses should be given a reasonable lead-in time to evaluate any pre-1 July 2010 arrangements which may remain in place.

8. We support the continued exemption for SMEs from the Irish transfer pricing regime. However, if the general exemption is removed, it is essential that *de minimis* thresholds from documentation be introduced to balance the administrative burden for SMEs relative to the tax at risk.

9. Careful consideration should be given to unintended mismatches and consequential double taxation that could arise for intragroup lending in domestic situations, should the transfer pricing rules be broadened to include non-trading income.

10. Existing domestic law provisions already apply pricing requirements to capital transactions that have the same or very similar effect as arm's length transfer pricing rules. Introducing transfer pricing rules would place an unnecessary additional burden on taxpayers.

11. In relation to transfer pricing documentation:
    - Ireland should adopt the OECD set of common criteria in Annex I and II of the guidelines for Master and Local Files as the standard for content for transfer pricing documentation.
    - The revenue threshold for Master File requirements in Ireland should be the same threshold used for Country-by-Country Reporting in Ireland.
    - Local File requirements in Ireland could consider a 'Country File' as a simplification measure and have *de minimis* thresholds for materiality purposes.
    - The timing for transfer pricing documentation should remain in line with current practice; being available when the Irish corporation tax return is due.
    - Revenue guidance, which has been consulted on well in advance, is essential once the new document requirements are introduced.
    - The filing of Master and Local Files should be upon written request by Revenue rather than imposed as a mandatory filing requirement.

GAAR

12. In our view, the current Irish GAAR provisions are well understood in established case law over many years. They are more than robust enough to meet the minimum standard required by the Directive and should not be amended.

Exit tax

13. Existing legislation should be broadened to include the four particular circumstances for exit taxation contained in the ATAD. Trading assets should be chargeable to Irish tax at the trading rate of 12.5% on exit when the new rules come into effect by 2020. Irish tax law should also be updated to provide for a rebasing of all assets currently outside of the existing Irish exit tax provisions, to the market value of those assets at 1 January 2020. Further consideration of any rebasing impact on Irish-owned businesses may be required.

Anti-hybrid rules

14. Critical choices by the Irish Government on CFC implementation, as well as the impact of US tax reform measures, will have an impact on the most appropriate anti-hybrid rules for Ireland. In our view, a separate consultation on anti-hybrid rules is necessary later in the year when the design of the Irish CFC regime has been determined and the impact of US tax reform measures is better understood.

4. Response to consultation questions

4.1. Controlled Foreign Company rules

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, if any, are needed to ensure this meets the minimum standard required by the Directive?

Ireland is required under the ATAD[5] to introduce CFC rules into the Irish corporate tax code for the first time, from 1 January next year. This will represent one of the most fundamental changes to the Irish corporate tax system in decades. We acknowledge that Ireland is committed[6] to implementing the OECD BEPS measures and must bring in a CFC regime that is fully compliant with European Law and meets the minimum standard required under the Directive.

Members States must implement the provisions of the ATAD in a way that *"best fits their corporate tax systems"*[7] and so, Ireland must design Irish CFC rules that are appropriate for its own corporate tax regime.

The ATAD[8] recognises that each Member State will develop CFC rules that are in line with their own policy priorities. Ireland is a small, open economy with a strong reliance on exports and has developed its corporate tax code over many years to support this economic strategy. Ireland's corporate tax policy has always been a key factor in its economic strategy of attracting and maintaining investment and jobs in Ireland. Therefore, Ireland should design a CFC regime that is consistent with its broader international tax strategy[9] and the economic goals for the country.

A fundamental pillar of Irish corporate tax policy has always been that profits are taxed to the extent that they are attributable to Ireland. When framing a CFC policy therefore, it would be appropriate for Ireland to adopt CFC rules that target *"income which has artificially been diverted"*[10] from Ireland.

In recommending the design of a CFC regime for Ireland, we address below the two main elements of a CFC regime:

1. When will an overseas company be treated as a CFC for Irish tax purposes?

2. How will the taxable income of an Irish CFC be calculated?

---

[5] Council Directive (EU) 2016/1164 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.
[6] Update on Ireland's International Tax Strategy, October 2017
[7] Paragraph 3 of the Preamble to the ATAD
[8] Paragraph 12 of the Preamble to the ATAD
[9] Update on Ireland's International Tax Strategy, October 2017
[10] Paragraph 12 of the Preamble to the ATAD

When will an overseas company be treated as a CFC for Irish tax purposes?

The ATAD provides that an entity or a permanent establishment (PE) will be considered a CFC if two basic conditions are met. These are;

- the participation (control) condition; and
- the taxation condition.[11]

If the taxpayer parent company holds (directly or indirectly) more than 50% of the voting rights, capital or profits of a foreign company then it will have satisfied the participation (control) condition.

The taxation condition requires taxpayers to compare the tax paid by the foreign company and the tax that would have been paid if the foreign company had been subject to tax in the country where the parent company is tax resident. The taxation condition is met if the actual tax paid by the foreign company is less than half what would have been paid if that foreign company was taxed under the tax rules of the jurisdiction of the parent company.

In order to meet the minimum standard required under the ATAD, Ireland's CFC rules should impose a "greater than 50%" threshold to determine the participation condition for related party companies. Control should be determined by reference to legal control, based on the percentage of voting rights and economic control (the right to receive economic benefits, capital and assets of the foreign company) in order to satisfy the standard in the Directive. Existing related party tests under Irish law are well understood and should be used to aggregate indirect ownership and influence to determine the level of control of the foreign company for Irish CFC purposes.

How will the taxable income of an Irish CFC be calculated?

If a foreign company falls within both the participation (control) condition and the taxation condition, it will be treated as a CFC. This means that the parent company will be taxed on 'certain' income of the CFC, depending on how the EU Member State chooses to implement the Directive.

There are two potential approaches to identifying the income that is included in the CFC "tax base" under the ATAD. These are;

- the category of income approach (Option A)[12] and
- the "significant people function" approach (Option B).[13]

Option A

The tax base under Option A includes non-distributed passive income. Passive income in this context refers to intercompany interest, dividends, capital gains, royalties, leasing, licensing, insurance and related party services. Income will not be included under Option A where the CFC is based in an EU/EEA country and carries on a substantive economic activity supported by staff, equipment, assets and premises (with an option for a similar exclusion for CFCs located in countries outside the EEA).

---

[11] Article 7 (1) (b) of the ATAD
[12] Article 7(2)(a) of the ATAD
[13] Article 7(2)(b) of the ATAD

Option B

In contrast, the tax base under Option B applies to a broader type of income but with a particular focus on artificial or non-genuine arrangements. Option B includes all types of non-distributed income arising from *"non-genuine arrangements which have been put in place for the essential purpose of obtaining a tax advantage."* Arrangements are non-genuine where the CFC "*would not own the assets or would not have undertaken the risks which generate all, or part of, its income if it were not controlled by a company where the significant people functions, which are relevant to those assets and risks, are carried out and are instrumental in generating the controlled company's income*."[14]

There are benefits and limitations to both tax base options.

Option A (benefits)	**Option B (benefits)**
› Deters profit shifting to low-tax jurisdictions especially in the attribution of royalty income to intellectual property. › Reduces the risk of double taxation as activities would be taxed by the source country. › Includes a safe harbour rule to reduce the administrative burden. › There is an incentive to comply with CFC rules and lessen the tax burden for Irish resident companies.	› Deters companies from setting up CFCs for tax planning purposes and captures tax from group passive income. › It is consistent with global transfer pricing methods, which attributes the level of income to economic activity within the related party company. › Provides a safe harbour feature to lower the administrative burden.
Option A (limitations)	**Option B (limitations)**
› It will reduce competitiveness of the Irish regime against other countries with lower (or no) tax on passive income. › There is a potentially high administrative cost beyond safe harbours. › Threshold management by companies could counteract the BEPS objective of the CFC › This approach could trigger tax planning to ensure losses and avoid future tax liabilities.	› It may be costly to administer and compliance cost could be high depending on the documentation required. › Without anti-defragmentation rules, it could result in the break-up of shareholder control to fall below the threshold.

Making a policy choice between Option A and B is not a straightforward matter because a broad range of taxpayers will be affected by the introduction of CFC rules in Ireland. However, on balance it is our view that an Option B approach which focuses on CFC income that is diverted from Ireland would be a proportionate response to profit shifting risks in an Irish context and therefore, an appropriate tax base for an Irish CFC regime. This is subject to the conditions set out below.

[14] Article 7(2)(b) of the ATAD

Calculating the taxable income of the CFC under an Option B type regime

Option B targets mismatches that arise in cases where a CFC's income is generated from significant people functions based in Ireland rather than in the CFC. Under Option B, the Irish company would need the relevant information to demonstrate nexus between Irish activities and Irish income and between CFC activities and CFC income.

However, in designing an Option B type regime, it is important that an appropriate substance-based test and targeted entity exemptions support its application, to ensure it is proportionate in addressing BEPS risks and does not infringe EU fundamental freedoms.

Most CFCs are held for genuine commercial reasons and do not pose a risk to the Irish tax base. There are concerns that CFC rules using the Option B approach, which can target the profits and activity of an entity as a whole, could create an Irish tax liability for income streams that are not artificially diverted and are not the intended target of the rules. CFCs, with genuine substance-based activities, should not be included under the Irish regime, where they can demonstrate that foreign profits have not been artificially diverted from Ireland.

The nature of the Option B approach is such that it can result in a significant level of administration in the first year of operation, as the companies are all examined to determine whether any of the companies would be deemed to be a CFC. Nevertheless, once the analysis has been undertaken, the subsequent years' analysis should be easier to undertake, as it is unlikely that much would have changed in many of the companies. This does impose an additional burden following merger and acquisitions, but again the administration reduces in the second and subsequent years.

We have set out below some features that should be introduced into the Irish CFC regime when implementing an Option B approach. These features would ensure that the design of the CFC is in keeping with existing corporate tax policy of taxing profits that are attributable to Ireland but at the same time meeting the minimum standard of the Directive and respecting the fundamental freedoms of European Law.

Substance-based test

According to the ATAD, Ireland can limit its CFC rules to *"income which has artificially been diverted to the subsidiary"*[15] depending on its policy priority. A central principle of Irish corporate tax policy has always been to tax only profits that are considered Irish profits and the recognition of substance has been at its core.

In an Irish context, the types of profits in a CFC that are at most risk of being diverted from the Irish tax base are those taxed at higher rates (i.e. passive activities that do not meet the trading standard due to the lack of substance - taxable at 25% and capital gains taxable at 33%). As these two categories of profits are taxed at higher rates in Ireland, these are the profits that should be the focus of an Irish CFC regime.

[15] Paragraph 12 of the Preamble to the ATAD

However, whatever Irish CFC regime is implemented must respect the fundamental freedoms of European Law. The Court of Justice of the European Union (CJEU) has stated in *Cadbury Schweppes*[16] and subsequent decisions, that CFC rules and other tax provisions which apply to cross border transactions for the purposes of preventing tax avoidance must *"specifically target wholly artificial arrangements which do not reflect economic reality and whose only purpose would be to obtain a tax advantage.*"

BEPS Action 3 Final Report[17] suggests that EU Member States consider "*including a substance analysis that would only subject taxpayers to CFC rules if the CFCs did not engage in genuine economic activities"*[18] when implementing *"adaptable and durable CFC rules"*[19] that are compliant with the CJEU interpretation of EU treaty freedoms in *Cadbury Schweppes*.[20] The Final Report on BEPS Action 3 further notes that CFC rules which attribute income on a transactional basis[21] may be more consistent with EU law, as they would be more narrowly focused on income that raises BEPS concerns.

Companies with significant headquarter operations in Ireland, may have valid concerns about meeting the significant people function test in Option B. Irish CFC rules should only tackle artificial arrangements in line with European case law. Having a design feature in the Irish CFC regime which only seeks to tax what is 'wholly artificial' and does not have substantial economic activity could help to address these concerns. It would also safeguard the application of Option B against potentially infringing the EU fundamental freedoms.

The UK CFC regime, which operates an Option B type test, ensures that only those business profits which have been artificially diverted from the UK pass through the gateway[22] and are subject to a UK CFC charge. In this context, UK CFC rules require that the CFC has no UK managed assets and bears no UK managed risks. But not all activities carried on in the UK are caught by the meaning 'UK managed.' HMRC guidance recognises the role headquarters can play in setting parameters for how some of the business of overseas group companies must be conducted. Provided the "*active decision making in respect of the asset or risk does not take place in the UK, the fact that management is carried out within the general parameters or guidelines set in the UK would not by itself be sufficient to justify a conclusion that the CFC's assets or risks are UK managed."*[23] The HMRC guidance acknowledges that *"a UK company's overseas subsidiaries may also be required to follow a particular operating model."*[24]

Concerns of Irish headquartered companies should be capable of being addressed with the inclusion of a substance-based feature in Option B and the publication of clear guidance from the Revenue

---

[16] *Cadbury Schweppes Overseas Ltd v. Commissioners of Inland Revenue*, C-196/04
[17] OECD (2015), *Designing Effective Controlled Foreign company Rules, Action 3 – 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing Paris
[18] Paragraph 20 - OECD (2015), *Designing Effective Controlled Foreign company Rules, Action 3 – 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing Paris
[19] Paragraph 22 - OECD (2015), *Designing Effective Controlled Foreign company Rules, Action 3 – 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing Paris
[20] *Cadbury Schweppes Overseas Ltd v. Commissioners of Inland Revenue*, C-196/04
[21] Paragraph 97 - OECD (2015), *Designing Effective Controlled Foreign company Rules, Action 3 – 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing Paris
[22] Chapter 4 of Gateway: business profits
[23] INTM197320, International Manual, HMRC internal manual, (updated 9 January 2018)
[24] INTM197320, International Manual, HMRC internal manual, (updated 9 January 2018)

Commissioners on the matter. However, this is an area where much more detailed consultation is required.

Safe harbour feature for low profits/ low value entities

The ATAD permits a "safe harbour" feature under the Option B approach for subsidiaries with low profits or low profit margins, that do not pose BEPS risks. Ireland should avail of the reliefs[25] specifically outlined in the ATAD for smaller groups and subsidiaries/PEs with routine returns on low value adding activities.

Transitional arrangements for acquired subsidiaries

Ireland should consider introducing an exempt period from the CFC rules for subsidiaries that are acquired from third parties during the relevant taxable period. This would allow Irish companies time to evaluate the application of the Irish CFC rules to the acquired subsidiaries. This is a design feature of other CFC regimes, including the UK, which permits a one-year entity-level exemption for CFCs that have come under UK control for the first time.

Operate a white list to partially alleviate compliance burden

Much of the work in applying CFC rules can be a process to confirm that no additional tax charge is due. Many of the taxpayers that could potentially be subject to Irish CFC rules will have hundreds of subsidiaries and so, the compliance burden cannot be underestimated. Measures to mitigate that burden would be welcome, on the understanding that they do not undermine the purpose of the CFC regime (i.e. to protect Ireland's tax base).

The publication of a white list would be a practical way to alleviate the compliance burden associated with the "taxation condition" [26] test. A published white list is a feature of many CFC regimes around the world and is acceptable under the ATAD. As outlined earlier, the taxation condition test requires taxpayers to compare the tax paid by the foreign company and the tax that would have been paid if that company was Irish tax resident. A detailed computation is required to assess whether a company has met the taxation condition, which can be a very significant administrative burden. The burden of this requirement should be minimised in circumstances where it does not undermine the overall purpose of the CFC rules to act as a BEPS deterrent.

A white list could be used to reduce the compliance burden associated with this test in Ireland. The white list could include for example, EU Member States and tax treaty countries, provided the CFC has genuine activities and is tax resident and subject to tax in the white listed country.

Prevention of double taxation

As CFC rules effectively tax the income of a company's foreign subsidiary in the jurisdiction of the parent company (i.e. Ireland), it can lead to double taxation, if the CFC is also subject to tax overseas.

---

[25] Article 7(4) of the ATAD permits EU Members States to exclude a subsidiary/PE from CFC rules that has accounting profits of <€750K and non-trading profits of <€75K or accountings profits that are <10% of its operating costs.

[26] Article 7(1)(b) of the ATAD

There are three common situations where double taxation may arise:

- CFC income attributed to Ireland is also subject to foreign taxes.
- The CFC rules of more than one country applies to the same CFC income.
- A CFC distributes dividends out of income that has already been attributed to its shareholders or participants under the CFC rules, or a shareholder or participant disposes of the shares in the CFC.

Both the ATAD[27] and BEPS Action 3[28] highlight that anti-avoidance measures should not result in double taxation. Introducing measures to avoid double taxation arising under the CFC regime in Ireland would ensure the country remains an attractive place for businesses to invest and operate.

To alleviate the risk of double taxation, we recommend that:

- Ireland should exempt CFCs located in jurisdictions with a similar or higher income tax rate than Ireland for passive income. This is permitted under Article 7(2) and Article 8(7) of the ATAD.

- Ireland should provide a credit for foreign taxes actually paid by the CFC, including withholding taxes and all taxes on income that have not qualified for other reliefs i.e. where the attributed CFC income is also subject to foreign taxes and more than one countries' CFC rules apply to the same CFC income. This is permitted under Article 8(7) of the ATAD.

- Ireland should exempt dividends and gains arising on the disposal of CFC shares, where the income of the CFC was previously taxed. This is permitted under Article 8(5) of the ATAD.

Other factors to consider

An Irish CFC regime must address:

- how much income should be attributed to taxpayers;
- when the income should be included in the return; and
- what tax rate should be applied to the income.

The same domestic tax rules should be used to attribute income to a CFC as would be used for an Irish tax resident company, to maintain a competitive regime that is attractive for investment. This approach ensures tax neutrality and does not confer an advantage nor penalise a company for establishing a subsidiary.

Taxable income attributed to shareholders of a CFC under Irish CFC rules should be calculated in proportion to their control (ownership) of the CFC; the CFC income should be included in the tax period of the taxpayer in line with Irish domestic law and the applicable rate on CFC income should be the same rate that applies to an Irish tax resident company to which the CFC income is attributed.

CFC rules should also address the treatment of losses, and how passive losses can be used.

---

[27]Paragraph 5 of the Preamble to the ATAD
[28] OECD (2015), *Designing Effective Controlled Foreign company Rules, Action 3 – 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing Paris

All taxable income, whether it is earned on Irish territory or by an Irish CFC abroad, should be calculated on the same basis with the same method. This would ensure there is no profit shifting advantage to establishing a foreign subsidiary and would maintain a favourable tax environment for investment in Ireland.

To address this, Ireland should apply Irish domestic law provisions on passive income to calculate CFC income on an arm's length basis, which is required under Article 7(1) of the ATAD. It should also introduce a specific rule to restrict the offset of CFC losses to Irish territorial earned income, which is required under Article 8(1) of the ATAD. Finally, the Irish CFC regime should allow CFC losses to be carried forward for offset in future periods, which is permitted under Article 8(1) and (5) of the ATAD.

Institute recommendations:
It is our view, that an Option B approach which focuses on CFC income that is diverted from Ireland would, on balance, be a proportionate response to profit shifting risks in an Irish context and therefore, an appropriate tax base for an Irish CFC regime.

In designing an Option B type regime, it is important that an appropriate substance-based test and targeted exemptions support its application, to ensure it is proportionate in addressing BEPS risks and does not infringe EU fundamental freedoms.

As a broad range of taxpayers will be affected by the introduction of CFC rules in Ireland, it is essential that all stakeholders are given the opportunity to consult well in advance on draft legislation and draft Revenue guidance. The UK spent 5 years consulting on their CFC regime before opting to introduce a CFC regime based on an Option B type approach.

Investment in dedicated Revenue resources to deal with the increased administrative burdens of the CFC regime is essential.

4.2 Moving to a territorial corporation tax base

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?

In assessing attractiveness, international investors consider how dividends, branches and capital gains on share disposals are taxed and what CFC provisions exist to protect the country's tax base.

The operation of a worldwide regime requires foreign dividends to be taxed at the domestic rate, with credit for foreign tax incurred. As tax rates are decreasing globally, the level of tax collected from worldwide regimes diminishes, even though the administration remains.

The majority of the largest 50 economies by GDP now operate a territorial system, delivered through a range of options, including participation exemptions for dividends and exemptions for foreign branches. The recent trend in tax policy has been a move towards territorial systems, for example in Japan, the UK and, most recently in the US.

With the development of BEPS and the Inclusive Framework, each country is now adopting tools to ensure that profits are being properly aligned to where value is created, which protects their regimes from BEPS risks. As domestic tax laws are strengthened globally through the implementation of the BEPS Actions and the Inclusive Framework, the need to have a worldwide regime to address foreign base erosion concerns is diminishing.

Any extension beyond protecting the domestic tax base is likely to make the host country less competitive, given the additional administration created by a worldwide regime. Onerous CFC rules that have high compliance costs, together with a worldwide regime could act as a deterrent to the use of Ireland as a regional headquarters.

Based on the above, we believe that Ireland should move to a territorial regime with a participation exemption for dividends and foreign branches when CFC rules are introduced into Ireland.

Institute recommendations:
Ireland should move to a territorial regime with a participation exemption for dividends and foreign branches when CFC rules are introduced into Ireland.

4.3 Transfer Pricing

4.3.1 Adoption of OECD 2017 Transfer Pricing Guidelines

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?

Ireland has had transfer pricing legislation[29] since 2011. It applies arm's length pricing to arrangements agreed after 1 July 2010,[30] in accordance with the OECD Transfer Pricing Guidelines published in July 2010.[31] Irish transfer pricing rules now need to be updated to meet the standards in BEPS Actions 8, 9 and 10[32] and we must consider how best to effect this change to Irish domestic law.

The purpose of BEPS Actions 8, 9 and 10 was to develop a suite of transfer pricing rules that would result in transfer pricing outcomes which are more closely aligned with value creation.

To ensure effective compliance and implementation of the transfer pricing rules going forward, it is essential that careful consideration is given to the sequencing of the change to Irish law to reflect the new source OECD guidelines, including the publication of comprehensive Revenue guidance.

Timing

Irish businesses are facing great economic uncertainty over the next couple of years, arising from Brexit, tax reform in the US and the ongoing implementation of BEPS and the ATAD. They will have to contend with new detailed and extremely complex legislation in a very short space of time, as BEPS measures and the ATAD are implemented into Irish domestic law. These new BEPS and ATAD provisions will place significant obligations on Irish businesses to re-evaluate legal and operating structures, so that they can be satisfied with their continued compliance with the law and indeed, they may even present completely new issues for some businesses to address.

There may be no difference to the arm's length analysis for many types of intercompany transactions, whether applying the 2010 or the 2017 OECD guidelines. However, for some transactions the application of the 2017 guidelines could result in a different price and underlying framework of analysis, compared with the 2010 version.

Irish businesses need to be given sufficient time to evaluate the potential impact of the adoption of the 2017 OECD guidelines into Irish law may have on their operations. It would create a very

[29] Part 35A TCA 1997
[30] Section 835A (1) TCA 1997
[31] Section 835D TCA 1997
[32] OECD/G20 base Erosion and Profit Shifting Project: Aligning Transfer Pricing Outcomes with Value Creation, Actions 8-10 - 2015 Final Reports - http://dx.doi.org/10.1787/9789264241244-en

significant and disproportionate burden on businesses should Finance Bill 2018 signal a revision to the transfer pricing provisions to reflect the new source OECD guidelines to become law within 3 months (i.e. beginning of 2019), particularly when very complex CFC legislation will be introduced at the same time.

Revenue guidance

Multinationals have expressed some concern that the application of the arm's length principle under the 2017 OECD guidelines could give rise to greater uncertainty, which could occur when opposing conclusions are reached by different tax authorities regarding the same transaction and fact pattern.

There are specific conditions set out in the 2017 OECD guidelines that may result in a tax authority concluding that an entity in a multinational organisation has earned profits that are not proportionate to its relative value contribution. More than one tax authority may wish to effectively tax such profits of that entity, ultimately resulting in the same income being taxed multiple times.

Tax uncertainty influences business investment and location decisions and issues relating to tax administration have been ranked by business as a major driver of uncertainty in a tax system.[33] The IMF/OECD in their report to G20 Finance Ministers on tax certainty recommend *"announcing changes in advance and with timely issuance of guidance and information would ideally give enough lead-time to business to adapt to the new environment and consequently, reduce uncertainty."*

Irish taxpayers will need clear and comprehensive guidance from the Revenue Commissioners on how the 2017 guidelines will be implemented in practice to reduce tax uncertainty and this should be available when the new framework becomes law. A well-resourced Competent Authority will also be vital to deal with the increase in international disputes and Mutual Agreement Procedures that are likely to occur.

Some lead-in time for the adoption of the 2017 OECD guidelines into Irish law would allow Irish businesses a more reasonable time to assess the impact of the new rules on their operations and for the Revenue Commissioners to have prepared and published clear and comprehensive guidance on the matter.

Institute recommendations:
A reasonable lead-in time should be given for the 2017 OECD guidelines. This would allow Irish businesses adequate time to assess the impact of the guidelines on their operations and for the Revenue to publish clear and comprehensive guidance on how they will administer the transfer pricing rules under the new framework.

A well-resourced Competent Authority will also be vital to deal with the increase in international disputes and Mutual Agreement Procedures that are likely to occur.

[33] Tax Certainty, IMF/OECD report for G20 Finance Ministers, March 2017

4.3.2 Extension of transfer pricing rules to pre-1 July 2010 arrangements

Question 6: The Coffey Review recommends that "domestic transfer pricing legislation should be applied to arrangement the terms of which were agreed before 1 July 2010." What are the key considerations regarding the implementation of this recommendation?

When transfer pricing rules were introduced in Ireland for the first time in 2011, a policy decision was taken to apply the new rules on a going forward basis, so that any existing arrangements (agreements) that were in place before 1 July 2010 would be excluded from the regime.[34]

Without the grandfathering provisions, businesses would have been automatically required to restructure or re-price all pre-existing transactions from 1 January 2011.

There was no indication at the time that the grandfathering provisions would expire in the future, but rather arrangements would gradually become un-grandfathered as and when terms of an arrangement were altered. However, a business which entered into a long-term binding contract before 1 July 2010 would have had a reasonable expectation at the time that this contract would remain outside the transfer pricing rules, provided the terms of the arrangement remained unchanged.

There have been very significant advances in tax transparency in recent years with the implementation of automatic exchange of information. In efforts to adopt global best practice for tax transparency in Ireland, Revenue now provide that opinions and confirmations[35] from them have a maximum period of five years and so, we understand providing for a grandfathering exemption beyond those timeframes may be considered problematic.

However, should the grandfathering provisions be removed from Irish transfer pricing rules, we agree with Mr Coffey in his Report[36] that careful consideration must be given to the commencement date "given *the volume and value of pre-1 July 2010 arrangements outstanding are unknown."*[37]

To the extent that some businesses have pre-1 July 2010 intercompany agreements that remain in place, for example, long-term licences for trademarks or loans with long-term maturity, it would be critical that they are given a sufficient lead-in time to evaluate those transactions and restructure them where necessary. Particularly given they would have entered those arrangements on the understanding that they would not be subject to Irish transfer pricing rules if they remained unaltered.

Mr Coffey suggests that should his recommendation to extend domestic transfer pricing legislation to arrangements that were agreed before 1 July 2010 be implemented, that *"this should take place no later than end 2020, which is the year to which all the OECD and G20 have agreed to extend their co-operation on BEPS to complete the current work."*

[34] Part 35A TCA 1997
[35] eBrief No. 79/16, September 2016
[36] Review of Ireland's Corporation Tax Code, presented to the Minister for Finance and Public Expenditure and Reform by Mr Seamus Coffey, June 2017
[37] Review of Ireland's Corporation Tax Code, presented to the Minister for Finance and Public Expenditure and Reform by Mr Seamus Coffey, June 2017

Institute recommendations:
If the grandfathering provisions are removed from Irish transfer pricing legislation, businesses should be given a reasonable lead-in time to evaluate any pre-1 July 2010 arrangements which may remain in place.

4.3.3 Extension of transfer pricing rules to SMEs

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 enterprises (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?

The Institute supports the continued exemption[38] for SMEs both from transfer pricing rules in general and from the same documentation obligations normally imposed on large multinational businesses.

There is a long-standing approach under European law to distinguish SMEs from larger businesses because of their different economic and financial requirements and contributions. The current SME definition[39] in Irish legislation refers to the European Commission Recommendation that was adopted on 6 May 2003, which replaced the previous definition agreed in 1996.

SME operations generally do not have high-value transactions and so the risk they pose from a transfer pricing perspective is limited. We believe a lower compliance burden is appropriate for SMEs, as it reflects their reduced capacity and expertise to manage complex tax provisions, such as transfer pricing. SMEs are the backbone of the Irish economy and the administrative burden placed upon them should be minimised to encourage them to expand and grow their businesses.

It is worth noting that SMEs in Ireland are subject to tax provisions that require taxpayers to apply arm's length or fair market value pricing principles in a related party context. For example, expenses incurred by any Irish taxpayer are only deductible to the extent that the amount is "wholly and exclusively"[40] incurred for the purposes of the trade of the taxpayer.

Similarly, the price paid for the sale and purchase of capital assets is automatically deemed to take place at market value, where the transaction is between related parties. These are examples of some of the provisions in Irish tax law which apply to all Irish businesses, including SMEs.

If the policymakers decide to remove the current general exemption[41] applicable to SMEs, we would strongly recommend that a specific exemption from the documentation requirements[42] is introduced. This would ensure that SMEs are not subjected to the same prescribed documentation obligations that are enforced on larger multinational businesses, which can be very burdensome.

[38] Section 835E Taxes Consolidation Act 1997
[39] Commission Recommendation 2003/361/EC of 6 May 2003
[40] Section 81(2)(a) Taxes Consolidation Act 1997
[41] Section 835E Taxes Consolidation Act 1997
[42] Section 835 Taxes Consolidation Act 1997

If the basic transfer pricing rules[43] apply to SMEs, there should be a just and reasonable documentation burden placed on SMEs for them to demonstrate compliance with the arm's length principle, with no prescriptive content based on OECD, EU or other criteria. To impose such prescriptive content would place an inordinate level of cost and pressure on smaller businesses.

If policymakers wish to remove the exemption for SMEs, introducing *de minimis* thresholds into both the pricing provisions[44] and the documentation requirements[45] should be considered.

De minimus thresholds would allow companies with smaller scale transactions not to bear the onerous task of applying OECD arm's length analyses in all cases. It is not possible in practice for businesses to spend substantial time and effort on smaller-sized transactions. It is worth noting that *de minimis* exemptions for transfer pricing rules do not create an opportunity for tax avoidance as other tax measures continue to apply to prevent such risks.

De minimis thresholds can be structured in absolute or relative terms.

› For example, an "absolute threshold" could be framed so that any transactions cumulatively lower than €500,000 per accounting year would be exempt from transfer pricing rules and documentation requirements.

› A "relative threshold" could be defined so that any transactions cumulatively below 0.5% of the taxpayer's net turnover in an accounting year would be exempt from transfer pricing rules and documentation requirements.

› Absolute and relative *de minimis* thresholds could be introduced on a statutory basis to work in parallel to provide more than one way to reduce the obligation for all taxpayers on transactions that are unlikely to pose a significant tax risk.

Institute recommendation:
We support the continued exemption for SMEs from the Irish transfer pricing regime. However, if the general exemption is removed, it is essential that de minimis thresholds from documentation be introduced to balance the administrative burden for SMEs relative to the tax at risk.

[43] Section 835C Taxes Consolidation Act 1997
[44] Section 835C Taxes Consolidation Act 1997
[45] Section 835D Taxes Consolidation Act 1997

4.3.4 Extension of transfer pricing rules to non-trading transactions

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?

Extension of transfer pricing rules to non-trading income

We understand that the rationale for extending Irish transfer pricing rules to non-trading income is to address BEPS risks associated with the provision of cross border interest-free loans.

However, Ireland has two corporation tax rates; 12.5% on trading income and 25% on passive, non-trading income. If transfer pricing rules are extended to include both trading and non-trading transactions it will be necessary to consider the interaction of both rates, as this could give rise to unintended mismatches and consequential double taxation.

The impact of the two rates is particularly relevant if the scope of transfer pricing legislation is broadened to include non-trading income, whereby interest income could be taxed in a non-trading entity at 25% with either no deduction or only a deduction at 12.5%; thus leading to effective double taxation.

It would be important to maintain tax neutrality should the transfer pricing rules be extended to non-trading income in Ireland.

Institute recommendation:
Careful consideration should be given to unintended mismatches and consequential double taxation that could arise for intragroup lending in domestic situations, should the transfer pricing rules be broadened to include non-trading income.

Extension of transfer pricing rules to capital transactions

Fair market value and open market value tests already apply to the transfer or receipt of capital assets. Also extending transfer pricing to capital transactions would place an unnecessary and unreasonable burden on taxpayers who would be required to consider the potential application of existing tax rules on capital transactions, together with new transfer pricing provisions.

The following are examples of some of the existing provisions that effectively apply pricing requirements which are the same or very similar to the arm's length rules under section 835 TCA 1997;

- Section 547 TCA 1997 imposes market value on the transfers of assets for capital gains tax purposes, in circumstances where the transfer is not at arm's length; such as gifts, capital distributions from a company to its shareholders, transactions where consideration cannot be valued, and acquisitions relating to loss of employment or reduction of emoluments or in recognition for past services. Market value is also substituted for proceeds (if any) given or received on the transfer of an asset, either because there is no actual purchase and sale price, or the price does not represent the true value of the asset.

- Section 289 TCA 1997 imposes open market value when calculating a balancing allowance or charge in circumstances where no proceeds have been received for the disposal of machinery or plant.

- Section 312 TCA 1997 substitutes open market value for the purposes of capital allowances available on industrial buildings or structures, plant or machinery, dredging, mining and scientific research, in circumstances where the asset is sold at a price other than its open market value and the sale is between associated persons.

- Section 291A (7)(b) TCA 1997 which imposes an arm's length basis for expenditure incurred on specified intangible assets.

Institute recommendation:
Existing domestic law provisions already apply pricing requirements to capital transactions that have the same or very similar effect as arm's length transfer pricing rules. Introducing transfer pricing rules would place an unnecessary additional burden on taxpayers.

4.3.5 Documentation

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 on business?

Chapter V of the 2017 OECD Guidelines sets out the three-tier documentation structure for multinational business, comprising of the Master File, the Local File and the Country-by-Country Report. Country-by-County Reporting[46] was introduced into Irish tax legislation in 2016 and now policymakers must consider how to implement Master File and Local File documentation into Irish tax law. Annex I and II of Chapter V outlines the content required for a Master File and Local File, respectively. Many OECD countries have already introduced legislation which mandatorily requires taxpayers in their jurisdiction to prepare (and possibly file) a Master File and/or Local File.

When determining an appropriate documentation regime, the following issues should be considered:

Content for Master Files/Local Files

The OECD has developed a set of common criteria in Annex I and II of the guidelines for Master and Local Files, based on consultations with tax authorities. Some countries have adopted local documentation requirements which differ from Annex I and II, however, we recommend that the OECD standard should be adopted in Ireland. This would be considered a consistent approach to take for Irish business.

Master File threshold

The Master File is intended to cover large groups with global operations. The Master File is a group document and so, a revenue threshold based on a group test would be appropriate. We believe that the revenue threshold for Master File requirements in Ireland should be the same group threshold as for Country-by-Country Reporting.[47] Australia has taken a similar approach when implementing Master File/Local File requirements into Australian tax law.

The Master File requirement should not apply to multinational groups on a medium or smaller scale, as the Local File should contain sufficient information to evaluate the reasonableness of their transfer pricing policies. In our view, multinational groups that do not exceed the revenue thresholds to be regarded as a large group (together with all their Irish subsidiaries) should not be obliged to maintain a Master File to satisfy Irish legislative provisions.

[46] Section 891H TCA 1997

[47] Section 891H TCA 1997 - multinational groups with third party revenue exceeding €750 million.

Local File – implementation considerations

There are two elements that should be considered when developing Local File documentation requirements.[48] Firstly, Irish taxpayers could be allowed to prepare a consolidated 'Country File', which would contain the same content required by the OECD standard, but would be provided in a single file for all taxpayers that are Irish. This would simplify the obligations of a multinational group operating in Ireland, reduce potential duplication of information to be prepared by taxpayers and reduce the quantity of documentation received by Revenue during a tax audit. Both the US and Italy currently operate a "Country File" to satisfy documentation requirements in their jurisdictions.

Secondly, the concept of "materiality" should be addressed in the context of Local Files. The OECD definition of the Local File refers to "*material transfer pricing positions*"[49] and "*which are material in the context of the local country's tax system.*"[50]

In our response earlier to consultation question 7, relating to SMEs', we suggested *de minimis* thresholds for determining whether a transaction should be documented, analysed and validated in a Local File. We believe that the same *de minimis* thresholds outlined in section 4.3.3 could equally apply to documentation requirements for the Local File.

Timing for documentation

We believe that the timing for taxpayers to prepare adequate documentation in support of transactions for an accounting year, should remain in line with current practice of being available when the Irish corporation tax return is due (i.e. within nine months of the accounting year end).[51] The level of adequate documentation (Master and Local Files) should be considered in accordance with the taxpayer's size and complexity of transactions.

Revenue guidance

Current transfer pricing documentation requirements are set out in section 835F TCA 1997. Revenue has published guidance[52] on what transfer pricing documentation is required to comply with the legislation, as part of their Transfer Pricing Compliance Review programme.

If Ireland enacts legislation to require taxpayers to prepare a Local File, it would be important for Revenue to publish practical guidance on the new requirements, which could help to alleviate the costly burden on taxpayers of complying with the strict content of the OECD Local File requirements.

Four areas where guidance from Revenue would be beneficial are:

---

[48] In this section, we have not separately cited our request to alleviate SMEs from the burden of complying with specific and evolving transfer pricing legislation and associated documentation requirements.
[49] Chapter V, Transfer Pricing Documentation, OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017.
[50] Chapter V, Transfer Pricing Documentation, OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017.
[51] Section 959A TCA 1997.
[52] Revenue eBrief No. 62/12: Monitoring Compliance with Transfer Pricing rules contained in Part 35A TCA 1997

a. *Benchmarking sets* – How frequently would Revenue require comparable benchmarking analyses to be updated? Tax authorities in other jurisdictions allow for a comparable set to be relied upon for three years, with an obligation to update in the fourth year.

b. *Arm's Length Range* – Under OECD principles, the full arm's length range shall be the appropriate range by which to set or test the price or result of an intercompany transaction. A relatively small number of countries have requirements that statistical measures of the range (the inter-quartile or the median alone) forms the basis of the arm's length price. Firstly, it would be helpful for Revenue to publish its view on this matter.

   Secondly, where the price of an intercompany transaction falls outside the arm's length range, it would be beneficial for taxpayers to know how Revenue might adjust the transfer price. For example, some tax authorities compute the adjustment by ensuring the median of the arm's length range is achieved, others compute the adjustment by ensuring the inter-quartile range is achieved.

c. *Bundling of transactions* – Under what circumstances could the financial results of one transaction be bundled with the financial results of another transaction, with the intent to assess the combined results of both transactions?

d. *Multiple year data* – Under what circumstances could a taxpayer evaluate financial results of a single transaction over multiple years rather than on a year-by-year basis?

Submission of Master File/ Local File upon request

The Country-by-Country Report,[53] which forms part of the three-tier documentation package for large multinational groups, is an automatic filing obligation for the group and its subsidiaries. For Ireland, it would be appropriate for this Report to be the only form of automatic filing obligation and that the Master Files and Local Files should be provided upon a written request from Revenue.

We think a mandatory formal submission procedure for Master Files or Local Files would only increase the burden for both taxpayers and the Revenue Commissioners. In order to facilitate automatic filing obligations, Revenue would be required to ensure adequate additional resources and technology to accept, review and respond to the numerous and lengthy documents to be submitted every year.

The volume would be significant as Irish parented companies and subsidiaries meeting the documentation requirements would all be required to make these submissions. If Revenue does not have the capacity to review taxpayers' submissions, then the automatic filing obligation will effectively create compliance burdens without a clear benefit to any stakeholder involved.

[53] Section 891H TCA 1997

Institute recommendations:
Ireland should adopt the OECD set of common criteria in Annex I and II of the guidelines for Master and Local Files as the standard for content for transfer pricing documentation.

The revenue threshold for Master File requirements in Ireland should be the same threshold used for Country-by-Country Reporting in Ireland.

Local File requirements in Ireland could consider a 'Country File' as a simplification measure and have de minimis thresholds for materiality purposes.

The timing for transfer pricing documentation should remain in line with current practice; being available when the Irish corporation tax return is due.

Revenue guidance, which has been consulted on well in advance, is essential once the new document requirements are introduced.

The filing of Master and Local Files should be upon written request by Revenue rather than imposed as a mandatory filing requirement.

4.4 General Anti-Avoidance Rule

Question 1: Article 6 of ATAD requires the transposition of a General Anti-Avoidance 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?

Article 6(1) of the ATAD[54] requires Members States to ignore arrangements that the main purpose of which is to obtain a tax advantage. An arrangement will be treated as *"non-genuine"*[55] for the purposes of the Directive to the extent that it is not entered for valid commercial reasons that reflect economic reality.

Ireland has had a GAAR since 1989[56] which was completely overhauled in 2014 with the introduction of section 811C TCA 1997. The new test[57] broadly now focuses on whether it would be "*reasonable to consider*" that a transaction's primary purpose was to give rise to a tax advantage. Revenue guidance[58] provides that if a transaction is "*a genuine business transaction carried out with a view to the realisation of profit and not primarily for tax avoidance"*, then GAAR does not apply. In our view, the current Irish GAAR provisions are sufficiently robust and do not need to be amended to meet the minimum standard required by the Directive.

Institute recommendation:
In our view, the current Irish GAAR provisions are well understood in established case law over many years. They are more than robust enough to meet the minimum standard required by the Directive and should not be amended.

[54] Council Directive (EU) 2016/1164 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.
[55] Article 6(2) of the ATAD
[56] Section 811 TCA 1997
[57] Section 811C (2)(a) TCA 1997
[58] Notes for Guidance – Taxes Consolidation Act 1997 – Finance Act 2017 Edition - Part 33

4.5 Exit tax

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?

Article 5 of the ATAD[59] requires EU Member States to impose an exit tax on the following transactions:

- the transfer of assets to a PE of the taxpayer in another country, which must be taxed by the head-office jurisdiction if the assets leave the tax net of the country of where the head-office is located;
- the transfer of assets of a PE to its head office or to a PE in another country, which must be taxed by the transferring PE jurisdiction if the assets leave the tax net of that jurisdiction;
- the migration of residence of a taxpayer to another country; and
- the transfer of a business carried on by a PE in a Member State to another country if the assets leave the tax net of the transferring PE jurisdiction.

The Directive requires the exit tax to be applied on the difference between the market value of the asset and the value for tax purposes at the time of the relevant transaction. Member States to which the assets are transferred are obliged to accept the market value of the assets that has been determined by the Member State imposing the exit tax.[60]

The ATAD does not outline how EU Member States should determine the value for tax purposes of assets that enter their tax net from a third country. In our view, the tax value of such assets should equal the market value of the assets when they enter the Irish tax net. However, unlike other EU Member States, Ireland does not currently provide for a general step-up in tax value when assets come within the charge to Irish tax. This means that the imposition of exit taxation under the ATAD could place a greater burden on assets exiting Ireland than compared with other EU countries. To address this, Irish tax law could be updated to provide for a rebasing of all assets currently outside the existing Irish exit tax provisions, to the market value of those assets at 1 January 2020. However further consideration of any rebasing impact on Irish-owned businesses may be required.

The existing Irish exit tax provisions[61] impose a tax charge on companies that cease to be Irish tax resident. The exit tax is triggered by way of a deemed disposal and reacquisition of the migrating company's assets at market value.

Under existing Irish tax law, the transactions listed under the ATAD would not generally trigger an Irish tax charge. This is because the exit tax charge arising on the migration of a company from

---

[59] Council Directive (EU) 2016/1164 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

[60] Article 5(5) of the ATAD

[61] Section 627 TCA 1997

Ireland is intended to apply in narrow circumstances and the allocation of assets to a PE or back to head office (or to another PE of the same taxpayer) is generally not treated as a disposal for Irish tax purposes. Although, there is a provision[62] to tax such assets transferred outside of Ireland, where the assets were previously acquired as part of an intragroup transfer.[63] However, to broaden the existing Irish exit tax rules, the "excluded company"[64] test will need to be amended as it is incompatible with the ATAD.

Ireland currently applies CGT at 33% on exit in narrowly defined circumstances. The ATAD does not specify a rate to be used for exit tax purposes. Ireland's 33% CGT rate is the fourth highest in the OECD and 10 percentage points above the median OECD CGT rate. We know investors consider exit even before making an investment in a country and so, Ireland's very high CGT rates can act as a barrier to investment.

Now that Irish exit tax rules must be extended to include a very broader range of assets and circumstances, careful consideration should be given to the tax rate imposed on exit for Ireland to maintain competitive with other EU Members States. Trading assets, which would never have come within the exit tax provisions before, could be subject to a very penal CGT rate of 33% on exit compared with other EU countries. We believe therefore that Irish tax legislation should be updated to ensure that trading assets are chargeable to Irish tax at the trading rate of 12.5% on exit when the new rules come into effect by 2020.

Institute recommendation:
Existing legislation should be broadened to include the four particular circumstances for exit taxation contained in the ATAD. Trading assets should be chargeable to Irish tax at the trading rate of 12.5% on exit when the new rules come into effect by 2020. Irish tax law could also be updated to provide for a rebasing of all assets currently outside of the existing Irish exit tax provisions, to the market value of those assets at 1 January 2020. Further consideration of any rebasing impact on Irish-owned businesses may be required.

---

[62] Section 620A TCA 1997
[63] Sections 615, 617 and 620 TCA 1997
[64] Section 627 TCA 1997 defines an excluded company as a company of which not less than 90% of its issued share capital is held by a foreign company or foreign companies, or by a person or persons directly or indirectly controlled by a foreign company or foreign companies. A foreign company under the section refers to a company which (i) is not resident in the State, (ii) is under the control of a person or persons resident in a relevant territory, and (iii) is not under the control of a person or persons resident in the State. A relevant territory for this purpose means (i) the USA or (ii) an Irish tax treaty country.

4.6 Anti-hybrid rules

Question 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 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?

Anti-hybrid rules are extremely complex and require very careful consideration before implementing into Irish domestic law. Critical choices that have yet to be made on the design of an Irish CFC regime and the evolving tax landscape in the US, resulting from new tax reform measures, will impact hybrids.

In practice, Ireland does not have many hybrid mismatches with EU jurisdictions; rather this is an issue that arises much more in a US context. The US are beginning to implement new anti-hybrid rules into their domestic law, as part of the overhaul of their corporate tax code agreed before Christmas. Ireland needs to consider carefully how the new US rules and regulations on anti-hybrids are implemented before policymakers can fully understand how hybrid mismatch rules should be implemented here.

As anti-hybrid rules are so complex, we believe a separate consultation on them is necessary later in the year when the design of the Irish CFC regime has been determined and the impact of US tax reform measures is better understood.

In the interim however, we have set out below some initial observations on the implementation of hybrid mismatch rules into Irish tax legislation:

› Ireland should be mindful of hybrid mismatches when devising an Irish participation exemption regime. For example, there should be no foreign branch exemption given unless the foreign branch is subject to foreign tax.

› Ireland should not go beyond the framework for hybrid mismatch rules in the ATAD. Any changes to Irish tax legislation should be limited to payments that are actually hybrid payments and not for mismatches arising because of another country's tax system or from transfer pricing adjustments.

› Irish legislation should only treat as "included in" income payments that are taxed in another jurisdiction in the relevant period, even if these payments are not taxed upon the same entity, as the entity that is considered the taxable entity from an Irish perspective. We should not deny a tax deduction if a payment is not taxed in the immediate recipient company, as it may ultimately be taxed in the US for example, say under the new US global intangible low-taxed income (GILTI) provisions.

Institute recommendation:
Critical choices by the Irish Government on CFC implementation, as well as the impact of US tax reform measures will have an impact on the most appropriate anti-hybrid rules for Ireland. In our view, a separate consultation on anti-hybrid rules is necessary later in the year when the design of the Irish CFC regime has been determined and the impact of US tax reform measures is better understood.