

Consultation on Territoriality  
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Government Buildings  
Upper Merrion Street  
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12 December 2023

### **Consultation on a territorial system of taxation**

We welcome the Minister's commitment to formally adopt a participation exemption for dividends effective 1 January 2025 and the consideration of introducing an exemption for the profits of foreign branches. While we appreciate the opportunity to make a further submission on the implementation of a territorial system of taxation, we view a participation exemption for dividends as being long overdue. You might note that we recommended that Ireland commence the consultation process for the implementation of the participation exemption for dividends in our submission of 10 June 2020. Further, with Ireland's enactment of Pillar 2 from 1 January 2024, Irish companies face a much higher risk of double taxation on their global earnings until a participation exemption for dividends and foreign branches is effective given the complex requirements of the current antiquated foreign tax credit system.

With regards to the most recent consultation, we appreciate that there are a number of complexities in introducing a participation exemption for dividends. However, the vast majority of the questions posed relating to the participation exemption for dividends have already been answered in a number of responses to the previous consultations on the matter. We are also aware that a detailed submission was made by MKC on 18 April 2023 which provided an in-depth analysis of a significant portion of the questions posed in the current consultation. This memo also provided a detailed overview of the UK territorial regime and the policy decisions made in introducing the same. We would recommend that this submission is reviewed in detail. Further to this we are aware that a number of other discussions were held, and submissions were made to the Department of Finance during the course of 2023, which provided detailed technical answers to the questions now being posed again.

We have provided answers to a number of the questions posed in Appendix 1, noting that the questions have been answered through various submissions on the matter. We note that further work is required in respect of the introduction of a branch exemption, and we would welcome the opportunity to further engage with respect to this. However, a number of the questions posed in the current consultation are too specific to answer by this group and as such we have not answered these questions. We would note that the MKC submission of 18 April 2023 has provided detailed commentary on an exemption for profits of foreign branches. We would, however, recommend that a branch exemption be introduced on an electable basis.

From the perspective of the introduction of the participation exemption for dividends, we would reiterate the recommendations that we provided in our response of 7 March 2022 to the previous consultation on the territorial system of taxation, as well as the submission made by MKC in 2023, most notably:

- The regime should be as broad as possible, and should provide for a full exemption for all dividends;
- Given the fact that profits of foreign subsidiaries will now be subject to a minimum level of tax of 15%, the exemption should apply irrespective as to the residence location of the subsidiary;
- The regime should be as simple and as uncomplicated as possible, and should not include conditionality as included within sections 21B or 626B TCA 1997;
- As there are significant similarities in the tax regimes of the UK and Ireland, we would recommend that Ireland should introduce a regime broadly similar to the UK participation exemption regime;
- Ireland should not look to further restrict interest deductibility or the deductibility of other expenses, as the current rules are already too restrictive;
- The new regime should contain optionality, so that taxpayers could elect into the existing tax credit regime (schedule 24 TCA 1997); and
- The participation exemption for dividends and for foreign branches (on elective basis) should be introduced as a matter of urgency.

We note that 2 further consultations are proposed for 2024 with respect to the participation exemption for dividends. Given that answers have already been provided in respect of the vast majority of the questions posed and given the level of complexity, we are unclear as to the necessity of 2 further consultations. We would view these as superfluous. As such, we would recommend that the time and resources that have been allocated to these consultations should be repurposed to a more robust and detailed review of the Irish tax code, with a particular emphasis on interest deductibility and the simplification of the various corporate tax rates that are applicable to business profits.

We would welcome the opportunity to discuss this proposal further with you at your earliest convenience.

Yours sincerely

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## APPENDIX 1

### Response to Questions Posed

#### Structural Considerations

*1. Would the introduction of a participation exemption for dividends prompt changes to current or future corporate group structures? Please provide details of relevant considerations, including information on group structures and sectors as appropriate.*

The expectation is that a participation exemption would be a positive for Ireland as a holding company location as it would support cash repatriation to Ireland from global operations which would be used to increase investment in Ireland and return value to shareholders, together with attracting and retaining ancillary activities. If Ireland is to become a competitive holding location, consideration will certainly be given at eliminating and simplifying current holding company structures in different existing locations.

*2. Are there design features in other jurisdictions that operate a dividend participation exemption regime that should or should not feature in the design of an Irish regime? Please provide details.*

As noted in multiple submissions, given the similarities between the UK and Irish tax regimes, Ireland should adopt a comparable participation exemption regime to that of the UK. Considering the ongoing implementation of OECD Pillar 2 model rules across more than 130 jurisdictions, there should be little sense in including any type of subject to tax test as a precondition for dividend exemption eligibility.

*3. Are there design features in other reliefs provided for in the Taxes Consolidation Act, 1997 that should or should not feature in the design of an Irish participation exemption? Please provide details.*

Ireland should look to adopt a regime that is simple and uncomplicated. There are a number of complexities associated with both Section 626B and Schedule 24 TCA 1997. As recommended in a number of submissions, a simple change to the legislation would be to amend section 129 to detail that dividends shall not be chargeable to corporation tax, irrespective of where they are sourced.

*4. How can complexity be reduced in the design of a participation exemption, while also ensuring the objectives of the regime are achieved and eliminating opportunity for aggressive tax planning?*

Similar to the UK, anti-avoidance legislation could be included to deny exemption treatment where a deduction had been claimed for the dividend in the payor location. Any potential risk for aggressive tax planning will be greatly reduced or eliminated for companies that will also be subject to the Pillar 2 rules and thus should be considered in the design of any anti-avoidance provisions.

#### Specified Jurisdictions

*5. What are your views on the potential scope of jurisdictions that should be eligible for an Irish participation exemption?*

Similarly to the UK, the scope of the regime should be as broad as possible and should apply to all dividends irrespective of the residence location of the payor. Given the fact that Pillar 2 will apply for all profits of corporate groups with turnover exceeding €750 million, it is unclear what the policy

objective would be to restrict the participation exemption for dividends sourced from a certain location.

*6. Should Ireland seek to align with international norms and, if so, what other country or countries should Ireland seek to align with in terms of the list of specified jurisdictions that qualify for a participation exemption?*

As noted, Ireland should look to adopt a regime comparable to that of the UK including applying to all dividends irrespective of the residence location of the payor.

*7. Should the scope of qualifying jurisdictions for a participation exemption align with the scope of existing Irish reliefs relating to foreign subsidiaries, such as relief under section 21B or the section 626B participation exemption for gains?*

As noted, given the advent of Pillar 2, it is unclear as to the policy objectives of restricting the application of the participation exemption or including further conditionality. Schedule 24 TCA 1997 is cumbersome and almost unworkable. Amending sections 626B and 21B TCA 1997 would likely lead to similar complexities as is currently the case with Schedule 24 TCA 1997.

### **Method of Relief**

*8. A participation exemption could operate as an exemption, in that the income is excluded from the charge to tax, or alternatively the income could be included in scope but with a deduction in arriving at taxable income. In your view, are there any advantages and/or disadvantages for one method of relief over the other? Are there other methods of relief that should be considered?*

As noted, Ireland should look to adopt as broad a participation exemption regime as possible. A participation exemption is an international norm, with Ireland's complicated and antiquated rules being the exception to the norm of OECD and EU Member States. Anything short of a full participation exemption will result in Ireland remaining as an international outlier that is uncompetitive and unattractive for new or continued investment.

### **Full or Partial Relief**

*9. In your view, should an Irish dividend participation exemption provide a full or partial exemption? Please provide reasons for your answer.*

Ireland is a small open economy which is reliant on Foreign Direct Investment and as such should look to introduce an internationally competitive full participation exemption for dividends. As noted by the Minister, Ireland currently raises no or negligible incremental tax from the credit system of taxation. As such, it is unclear as to what the policy objective would be of Ireland introducing a partial exemption.

### **Type of Dividend**

*10. What should the scope of a participation exemption be in terms of the type of dividend or other distributions that may qualify? What are the specific types of distributions that you envisage should or should not be eligible for exemption?*

Ireland should adopt a full exemption for all dividends and distributions, wherever they are sourced. Due to the advent of Pillar 2, the profits from which dividends are paid to Ireland should have already been subject to a minimum level of tax of 15%.

*11. Should a participation exemption apply to both income and capital distributions and, if so, how should a capital distribution be defined?*

The exemption regime should apply to both. Section 583 already provides a definition of a capital distribution. Please note that the UK government faced this issue on the introduction of the UK regime. The UK regime is applicable to all distributions, irrespective as to whether they are income or capital in nature.

*12. Is there a rationale for extending a participation exemption to other classes of shares beyond distributions in respect of ordinary share capital?*

Ireland should look to introduce as competitive regime as possible.

*13. Should a dividend exemption only apply in respect of shares which, if disposed of, would qualify for the section 626B participation exemption? Please provide details in support of your response.*

As noted, Ireland should look to bring in as broad a regime as possible and should not look to include conditionality. By applying conditionality, this would further complicate the regime and would potentially lead to similar complexities as is already the case with schedule 24 TCA 1997.

## **Minimum Shareholding Requirements**

*14. What are your views on the application of a minimum holding period in respect of participations qualifying for exemption?*

It is unclear as to the policy rationale for including a minimum holding period in order to qualify for the regime. As such, we would recommend that no minimum holding period be required.

*15. Are there circumstances in which dividends received shortly after a share acquisition should qualify (for example if the shares are subsequently held for a pre-determined length of time)?*

Again, it is unclear as to the policy rationale for including a minimum holding period in order to qualify for the regime.

*16. Should a participation be determined by reference to a percentage of ownership, voting rights and/or other criteria? What is the appropriate percentage of participation that should apply and why?*

Again, we would recommend as broad a regime as possible. We would not recommend including significant conditionality to the regime, but the minimum ownership percentage should not exceed 5% of the participation.

## **Optionality**

*17. Are you in favour of allowing businesses to choose whether to apply an exemption or to retain the current system of taxing foreign dividends and claiming a foreign tax credit? Please outline the key reasons in support of your answer.*

We recommend that the default position is that the participation exemption will apply to foreign sourced dividends. Companies should have the ability to elect for the existing tax treatment, as detailed under the provisions of Schedule 24, on a dividend-by-dividend basis. The UK rules allow for

companies to elect on a per dividend basis. This was adopted to address concerns that UK companies would not be able to claim relief from foreign withholding taxes under some UK double tax treaties where the availability of relief is dependent on the dividend being subject to tax in the UK (as opposed to a full exemption).

*18. Having regard to the above, if you are in favour, please outline your views on what basis optionality would operate.*

As noted under question 17, companies should be able to elect for schedule 24 treatment on a dividend by dividend basis.

*19. What anti-avoidance measures should apply in order to deter and prevent aggressive tax planning with regards to an optional exemption regime?*

Similarly to the UK, and as outlined in question 4, the dividend exemption regime should not apply where a deduction has been claimed for the dividend in the payor location.

*20. Should a participation exemption apply automatically once qualifying criteria is met, or should a business elect to apply the exemption?*

The participation exemption should be the default position.

*21. Should an election apply on a subsidiary by subsidiary, dividend by dividend, year to year or other basis?*

As noted in question 18, the election should be made on a dividend-by-dividend basis, in order to address the concerns that Irish companies may not be able to reclaim foreign withholding tax if the double tax agreement that Ireland has entered into with other countries requires that the specific dividend be subject to tax.

*22. Should an election be irrevocable once made? A. If not, what are the circumstances in which you would wish to opt-out of the exemption regime (and revert to the current system of taxing the income and claiming a double tax credit)? B. If an election were to be revocable or apply for a specific minimum time period, what is the appropriate minimum length of time that an election should apply for?*

As noted, the election should operate on a dividend-by-dividend basis.

*23. Are there examples of other jurisdictions, in addition to the UK, that allow optionality in relation to their participation exemption and if so, what are the key features that would or would not be suitable in Ireland?*

Most countries have historically had a participation exemption for dividends. As such, this issue would not have arisen in many instances, and thus an optional regime would not have been required.

## **Interest Limitation**

*24. Would the potential for an increased interest expense restriction as a result of the exemption of dividend income influence your view on the desirability of a participation exemption?*

The Irish interest deductibility rules are one of the most restrictive and punitive in the EU. As such, Ireland should look to simplify and improve the interest deductibility regime, and not look to impose further restrictions.

## **Subject to Tax Rule**

*25. How should a participation exemption be designed in order to prevent double nontaxation? Are there provisions of the current Irish corporation tax system, such as Controlled Foreign Company (CFC) and anti-hybrid rules, that could be enhanced in order to support this aim?*

It is unclear as to what the policy objectives of introducing the subject to tax rule would be. Given the existing CFC rules and anti-hybrid rules, in addition to the transposition of the Pillar 2 Directive, it is unclear why such increased design features would be required.

## **Substance in Ireland**

*26. What considerations are relevant to the design of substance requirements for a participation exemption that could be effective in promoting Ireland as a holding location for companies with economic substance in Ireland?*

We recommend a broad participation exemption for dividends, which would of itself be effective in promoting Ireland as a holding location for companies with economic substance in Ireland. Further as noted above, a participation exemption for dividends would support cash repatriation to Ireland from global operations which would be used to increase investment in Ireland and return value to shareholders. We believe conditionality associated with the legislation should be avoided or limited to the greatest extent possible.

## **Trading Requirement**

*27. What are your views on a potential condition of exemption whereby relief only applies to certain trading companies?*

The concept of trading is not universally applicable internationally. Including a trading requirement would complicate the regime and would also not be complementary to the mechanics of Pillar 2.

*28. Should a participation exemption align with trading criteria applicable in other foreign subsidiary related reliefs such as section 21B and 626B? Please elaborate*

As noted, Ireland should look to introduce a broad participation exemption with limited (if any) conditionality. As such, we would strenuously recommend against linking the exemption to sections 21B or 626B TCA 1997.

## **Transitional Arrangement**

*29. Should there be a lead-in period before a participation exemption regime is introduced? If so, what is an appropriate length of lead-in time that should apply?*

The participation exemption should be introduced as a matter of urgency, effective from 1 January 2025 at the latest. As noted in previous submissions, the participation exemption should have been introduced in conjunction with the introduction of Pillar 2.

*30. Would you still be in favour of introducing a participation exemption if unutilised foreign tax credits were lost?*

An exemption regime is more favourable than a credit regime.

*31. Are there other transitional arrangements that should be considered?*

We would not foresee any requirements for transitional arrangements. The UK did not include any transitional features on the adoption of the participation exemption regime.

### **Franked Investment Income**

*32. In your view, what are the main opportunities or issues in applying similar treatment to domestic and foreign dividend exemption regimes?*

A simple and uncomplicated regime would be internationally comparable. There is also a concern that the current Ireland treatment of domestic dividends compared with EU sourced dividends is not currently compatible with EU law.

*33. Would you be in favour of aligning the tax treatment of domestic and foreign dividend exemption regimes, if this meant additional qualifying conditions would apply to the treatment of exempt domestic dividends?*

Again, it is unclear as to the policy objectives or including conditionality in the participation exemption regime.

### **Portfolio Investors**

*34. What are the main advantages to the State and to businesses in the application of the portfolio exemption in its existing form under section 21B?*

n/a

*35. What are the arguments for or against retention of a portfolio exemption following the introduction of a participation exemption?*

n/a

*36. What would your views be on the introduction of a participation exemption if it required consequential amendments to, or removal of, the portfolio exemption?*

n/a

*37. What modifications or anti-avoidance provisions could be introduced to the tax treatment of portfolio investments in Ireland should a participation exemption exclude portfolio holdings?*

### **Existing Relief Alignment**

*38. To what extent should criteria for a foreign dividend exemption align with criteria for other reliefs related to foreign subsidiaries, such as section 21B and section 626B reliefs?*

As noted, Ireland should not look to include conditionality to the participation exemption regime and should introduce a broad regime with limited complexity.

*39. Should a participation exemption for dividends align with the qualifying conditions for the participation exemption on gains under section 626B? If not, what are your views on a scenario where a participation in a subsidiary qualifies for one relief but not the other?*

As noted, Ireland should not look to include conditionality to the participation exemption regime and should introduce a broad regime with limited complexity.



*40. What are the features in other jurisdictions that operate participation exemptions for both dividends and gains that would or would not work well in Ireland?*

As noted, Ireland should not look to include conditionality to the participation exemption regime and should introduce a broad regime with limited complexity.

### **Deductibility of Expenses**

*41. What are the considerations in support of or against allowing a deduction for expenses related to exempt foreign dividend income?*

It is unclear as to what the policy rationale for limiting the deductibility of expenses of management. The purposes of the deduction for expenses of management, under the provisions of section 83 TCA 1997, is to put on a similar footing trading companies and investment companies. These expenses are currently deductible against profits which are subject to Irish corporation tax. It would be discriminate to disallow a deduction for expenses of investment companies.

### **Close Company Surcharge**

*42. What are the considerations in relation to applying a close company surcharge in a regime incorporating a participation exemption for foreign dividend income?*

n/a

### **Specific Tax Regimes**

*43. Please identify any corporation tax legislative provisions that could be affected by a change in how foreign dividends are taxed, along with consideration of the potential implications.*

n/a

*44. What amendments, if any, would be required to those provisions in order to ensure their continued operation in conjunction with a participation exemption?*

n/a

### **Anti-Avoidance Rules**

*45. What type of anti-avoidance provisions should be incorporated into a participation exemption in order to eliminate opportunities for tax avoidance?*

As noted previously, the exemption should not apply to dividends where a deduction has been claimed in the paying jurisdiction. Further, as noted above, any potential risk for aggressive tax planning will be greatly reduced or eliminated for companies that will also be subject to the Pillar 2 rules and thus should be considered in the design of any anti-avoidance provisions.

*46. Are there features of existing anti-avoidance provisions that could be enhanced in order to support this aim?*

Nothing that we are aware of.

## **Controlled Foreign Companies**

*47. Are there other legislative amendments required to CFC rules in order to ensure they are robust enough in the context of a participation exemption?*

The Irish CFC rules are already compliant with ATAD CFC rules, which are aligned with the existence of a participation exemption. As such, we would expect that minimum amendments would be required to the CFC rules. The obvious amendment would be to apply a CFC charge where profits are distributed by a CFC in the form of a dividend which is exempt from tax under the Irish participation exemption regime.

## **Anti-Hybrids**

*48. What modification, if any, would be required to anti-hybrid provisions in order for Irish tax rules to remain ATAD compliant in conjunction with a participation exemption?*

As noted, the exemption should be disappplied where a deduction has been claimed for the dividend in the payor location. However, this should already be encapsulated under the provisions of section 835AJ(2)(b) TCA 1997 so that no further anti-hybrid legislation should be required.

*49. Are there specific features of anti-hybrid regimes in other jurisdictions that have a participation exemption that Ireland should adopt in addition to our existing anti-hybrid regime?*

The UK regime disapplies the participation exemption where a deduction has been claimed in the payor jurisdiction.

## **Interaction with Pillar II**

*50. Are there features of the Pillar II regime that should be considered and taken into account when designing a dividend participation exemption?*

A participation exemption is complementary to Pillar 2, as Pillar 2 was designed on the basis of a participation exemption already existing in jurisdictions. Additionally, for companies already subject to Pillar 2, there should be unrestricted eligibility as global earnings will already be subject to the global minimum tax rate of 15%.

## **Transfer Pricing**

*51. Do you foresee potential impacts arising from moving to a participation exemption for Ireland's transfer pricing regime?*

Nothing that we are aware of.

## **Multilateral Instrument Provisions**

*52. Do you foresee a need to adopt any provisions of the Multilateral Instrument in conjunction with a participation exemption?*

Nothing that we are aware of.

**Any Other Issues**

*53. In your view, are there any other relevant considerations that should be taken into account in the design of a participation exemption for foreign dividends, or the integration of the exemption into the existing corporation tax regime?*

Nothing that we are aware of.