TAXAND

Transfer Pricing Rules – Public Consultation,
Tax Division,
Department of Finance,
Government Buildings,
Upper Merrion Street,
Dublin 2,
D02 R583

Submitted by email: tpreview@finance.gov.ie

02 April 2019

Comments on the Public Consultation Document " Ireland's Transfer Pricing Rules Public Consultation".

Dear Sir / Madam,

Taxand Ireland (William Fry Tax Advisors) welcomes the opportunity to provide comments on the Public Consultation Document " Ireland's Transfer Pricing Rules Public Consultation" published on 18 February 2019.

We would like to share our thoughts on the proposals based on our experience of advising multinational enterprises, large domestic Irish headquartered enterprises and small and medium enterprises.

1) Incorporation of the OECD 2017 Guidelines into Irish legislation

We are of the view that it is important that the OECD 2017 Guidelines should be directly incorporated into Irish transfer pricing legislation with effect from 1 January 2020. It is important that taxpayers have certainty regarding their tax affairs and many of our EU and tax treaty partners have already implemented the OECD 2017 Guidelines. This of course gives rise to problems in practice in relation to transfer pricing cross border transactions, transfer pricing audits, mutual assistance procedures and advance pricing arrangements. Therefore, the alignment of our transfer pricing rules with our international trading partners is a welcome development.

However, we would submit that some level of leniency should be afforded to companies concerning the implementation of the OECD 2017 Guidelines from a practical perspective having regard to the increased costs and administrative burden placed on companies in updating their transfer pricing policies and implementing the new expanded documentation requirements. Particularly where companies have recently undertaken an exercise to update their transfer pricing policies based on OECD 2010 Guidelines, consideration should be given to a period of grace as to when they would be required to undertake such an exercise again.

Furthermore, in any proposed legislative changes introducing the OECD 2017 Guidelines, it should be clear that the OECD Guidelines will only have prospective application and will not have any bearing on prior periods, particularly with respect to Revenue audits.

The impact of the OECD Public Consultation "Addressing the Tax Challenges of the digitalisation of the Economy" published on 13 February 2019 should be considered further. While we do not think this should delay the introduction of the OECD 2017 Guidelines, regard should be had to the increasing burdensome complexities that are being discussed for multinational companies at OECD level.

An unintended consequence of the introduction of the OECD 2017 Guidelines could be an accelerated impact on the "Double Irish" structure. As you are aware, historic "Double Irish" structures must be unwound with the new residency rules enacted in Finance Act 2014, applying to all companies from 1 January 2021. The introduction of the OECD 2017 Guidelines, and in particular the application of DEMPE, could result in royalties paid in the course of 2020 under the "Double Irish" structure by Irish resident companies being considered non-deductible. We would welcome some guidance on how the interaction of the OECD 2017 Guidelines and the final year of the "Double Irish" will operate in practice.

2) Removal of the exemption for arrangements in place since pre-July 2010

This is likely to impact certain domestic arrangements more so than international arrangements. Please see comments below at Question 4 regarding whether there is a requirement to extend transfer pricing legislation to domestic transactions or whether transfer pricing legislation should be limited to cross-border transaction, focussed on base erosion and profit shifting structures.

In general, the majority of arrangements covered by this exemption should have been phased out and the impact of removing this grandfathering exemption should not be unfair on taxpayers. Given the focus on international tax arrangements more generally, it is hard to support the retention of such an exemption and we do not see sufficient tax or economic rationale to justify maintaining the exemption.

We are of the view that a 10-year grandfathering period has been generous and has afforded sufficient time for taxpayers to consider the potential impact of transfer pricing legislation on their structures and to plan accordingly.

3) Extension of transfer pricing rules to SMEs

Whilst we note the Coffey report recommended extending transfer pricing legislation to govern small and medium enterprises, we would note that the SME exemption is provided for by the EU and therefore we would query whether extending the rules to SME's is 1) strictly required and 2) would yield sufficient economic gains to the exchequer to justify their inclusion within the remits of the transfer pricing legislation.

There is very little evidence to suggest that SME's are implementing tax practices contrary to policy objectives and we would consider that the introduction of transfer pricing rules, and the additional costs and compliance burden it brings, would only act to discourage entrepreneurship and the development of indigenous business. The compliance burden on the SME sector is significant enough.

In addition, we would question whether the current competent authority / transfer pricing function within Revenue would have adequate resources to cope with an extension of the rules to SME's and the additional workload that would come with enforcing those rules

To the extent it is felt that the rules should be extended to cover transactions involving SMEs we would recommend that the following points are considered:

- Introduction of reduced and simplified documentation requirements for SME;
- Incorporation of de minimus rules for transaction between SMEs. This could take the form of different mechanics and could be based on a % of transactions conducted with third parties versus related parties or indeed a % of the euro value of transactions conducted with third parties versus related parties for example; and/or
- Potential introduction of safe harbour rules for SME which could set acceptable ranges of prices which could be followed by SMEs based on sectors or the type of transactions.

4) Extending Transfer Pricing Rules to non-Trading Income and Capital Transactions

a) Non-trading transactions

There is a significant concern amongst our clients that the extension of transfer pricing rules to non-trading transactions will have severe negative tax implications for Irish tax payers and will likely penalise domestic companies more than multinational companies.

The potential negative tax impact arises from two areas of Irish tax law and which will negatively impact on transactions between two Irish tax resident companies as follows:

i. Operation of two corporate income tax rates

As you aware, the taxation of non-trading income is usually at the rate of 25%. Where there is a corresponding payment (for example rent or interest) made by a trading entity a deduction may only be available at the 12.5% leading to a negative tax arbitrage and cash tax leakage of 12.5% on the gross value of the payment.

The impact of the above is further increased for Irish domestic companies who are considered close companies and are required to bring the interest or rental income into the computation of estate and investment income for the purposes of calculating a close company surcharge.

It should also be mentioned that the 25% rate of taxation should be reviewed due to global trends in corporate tax rates.

ii. Restrictions on Interest Deductibility

Furthermore, given the restrictions on the availability of interest deductions for non-trading companies, where the paying entity is not a trading entity and the paying company has not borrowed for a qualifying purpose under Section 247 Taxes Consolidation, there is a very real risk that no deduction would be available for the interest payment by the paying entity. In such circumstances a taxpayer would be looking at cash tax leakage of 25% on the gross value of the payment.

We recognise that certain interest-free structure have been considered by some jurisdictions to be aggressive tax planning structures in the context of cross border tax planning and we accept that cross border interest free loan structures should be looked at as part of this initiative in order to prevent base erosion and profits shifting from occurring, if the objective of such arrangements is to base erode profit between jurisdictions.

However, any plans to extend transfer pricing legislation to non-trading transactions need to be carefully examined and the impact of the two matters above need to be considered in full. Any changes to the transfer pricing rules need to also be cognisant of the changes to Ireland's interest deductibility which will be introduced at some point in the future under the Anti-Tax Avoidance Directive.

We would strongly encourage that consideration is given to whether a domestic exemption would be possible whereby only cross-border transactions, focussed on base erosion and profit shifting between jurisdictions, be included within the remit of any extension of transfer pricing rules to non-trading transactions. An extension of the rules to domestic transactions would arguably lead to unfair taxation on domestic companies and may lead to an element of double taxation within Irish domestic groups.

In the absence of a specific domestic exemption, consideration should be given to to equalising the negative tax arbitrage that would be suffered by Irish domestic companies should the transfer pricing legislation be extended to non-trading transactions. This could be considered in the following manners:

- Extension of 12.5% rate to transactions within the scope of Irish transfer pricing legislation such that there is a matching of the deduction and taxation of the same payment;
- Increased notional deduction where the recipient is taxed at a higher rate of tax than the payor;
- Exclusion of inter-group lending which is quasi-equity in nature; and/or
- Consideration of notional deduction for equity transactions.

In addition, we would recommend that further consideration should be given to whether any extension of our transfer pricing rules should be delayed until such time as Ireland has implemented the revised interest deductibility rules under the Anti-Tax Avoidance Directive.

Further guidance should be issued in relation to what is considered "trading" particularly in the context of financial transactions.

Finally, we would recommend the introduction of safe harbour provisions which would seek to only apply transfer pricing rules for non-trading transactions to aggregate transactions above a certain value.

b) Capital Transactions

We are of the view that our current rules regarding capital transactions are appropriate and fit for purposes. The current rules allow for the market value to be determined fairly by the taxpayer, having regard to the unique characteristics of any once-off transaction, and also provide the Revenue with sufficient scope and authority to investigate and challenge how such market values are arrived at.

We do not believe extending transfer pricing rules to capital transactions would yield additional returns for the exchequer. It is important to note that many taxpayers are already required to carry out valuation exercises in accordance with generally accepted accounting principles for the purposes of their financial reporting. Extending transfer pricing rules to capital transactions would bring an unnecessary cost to taxpayers and would increase the complexity of once-off transactions.

Again, we would question whether the current competent authority / transfer pricing function within Revenue be adequately resourced to cope with an extension of the rules to capital transactions, given the additional transfer pricing expertise that would be required to audit or investigate capital transactions if the transfer pricing rules were extended to such transactions.

5) Extending Transfer Pricing Documentation

In general, we are of the view that many multinational enterprises are already implementing the master file / local file concept as these documentation requirements are already required in most jurisdictions.

Therefore, in general, we do not believe the introduction of the new documentation requirements will give rise to many issues and we believe this has been well flagged and is an expected change to our domestic transfer pricing documentation regime.

We would recommend that Ireland maintains its approach with respect to when transfer pricing documentation is required to be made available and we would not recommend any approach which sees documentation having to be submitted either as part of the CT1 return or otherwise an election having to be made to indicate that the taxpayer has documentation in place at the time of filing of the return. We are of the view the current practice and legislation is fit for purpose in this regard.

6) Application of the Authorised OECD Approach to branch profit attribution.

In general, we are of the view that implementing the Authorised OECD Approach ("AOA") on 1 January 2020 would be too soon and further consideration should be given to the AOA and its appropriateness for the Irish tax regime before any decision is taken. Clearly changes would be required to Section 25 Taxes Consolidation Act 1997 to effect any change to how profits are attributed to a branch /permanent establishment.

We would not view the introduction of the AOA as urgent and are of the view that more time should be taken to gather views from the various stakeholders and we would note that the financial services and insurance sector would likely be most impacted by any change in this regard.

About Taxand

Taxand is the world's largest independent tax organisation with more than 400 tax partners and over 2,000 tax advisors in 48 countries. If you have comments or questions, please feel free to contact any of the following

In Ireland, Taxand is William Fry Tax Advisors Limited.

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Submitted on behalf of Taxand Ireland by email on 02 April 2019.

For any queries in relation to this submission, please do not hesitate to contact us:

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