On a Page - Coffey Report - Review of Ireland's Corporation Tax Code

Background

The Government released on 12 September 2017 the Review of Ireland's Corporation Tax Code, prepared by independent expert Seamus Coffey (the Report).

The Report was prepared in response to September 2016 terms of reference which recognised the context for Ireland's tax code in a changing international landscape for corporate income tax regimes, including:

- Achieving the highest international standards in tax transparency, taking into account the impact of transparency on developing countries,
- Implementing Ireland's commitments under the OECD's Base Erosion and Profit Shifting (BEPS) Project,
- Delivering certainty for business, maintaining the regime's competitiveness - whilst not affording preferential treatment to any taxpayer,
- The pattern and sustainability of Ireland's corporation tax receipts, and
- **Maintaining the 12.5% rate of corporation tax.**

Review of the 12.5% rate was not in scope - nor were indirect taxes or Ireland's personal tax regime.

This is a summary of the Report findings and recommendations. The findings are broadly positive on the medium term sustainability of Ireland's corporation tax receipts and Ireland's low rate corporation tax regime.

The Report's recommendations will be subject to a public consultation to launch on 10 October 2017 Budget Day seeking feedback on enacting recommendations.

Some expected changes, if adopted, could have a significant impact on business. Timing of adoption is uncertain.

Matters of potential relevance to your business and what you should do next are explored overleaf.

Transfer Pricing

The Report recommends consideration of:

- Timing of adoption of changes to the transfer pricing regime. This is to be included in the public consultation with agreed changes recommended to be implemented no later than the end of 2020.
- Extending the scope of Ireland's transfer pricing regime to non-trading transactions – domestic and cross border. There is a strong rationale if it reduces risk of aggressive tax planning and, in the case of capital transactions, improves existing provisions.

  Market value is imposed for tax purposes in a number of non-trading scenarios but arm's length pricing requirements do not apply to impute arm's length income to transactions conducted outside the course of a trade. This can lead to benefits arising from cross border mismatches where the counterparty jurisdiction applies a one-sided transfer pricing adjustment for an expense currently not taxed in Ireland.

  For domestic intra group transactions, applying an arm's length price to non-trading transactions could result in a domestic tax rate mismatch between non-trading income currently taxed at 25% and trading expense deductible at 12.5%.
- Applying transfer pricing provisions to all corporate taxpayers, irrespective of size - options presented for review consider whether the compliance burden for SMEs, currently excluded, is proportionate to the mispricing risk.
- Specific obligation for taxpayers in scope of transfer pricing rules to adopt OECD compliant standards for transfer pricing documentation.
- Ending the exclusion from transfer pricing of arrangements in place prior to 1 July 2010 under existing grandfathering provisions – having consideration to the commencement date.
- Formal adoption of 2017 OECD transfer pricing guidelines - timing of adoption uncertain.
- Preserve Ireland's existing one-way transfer pricing adjustment approach.

Taxation of intangible assets

The Report recommends:

- Reintroducing a cap on the deductibility of capital allowances and interest expense on expenditure incurred on intangible assets under section 291A, TCA 1997.
  - The measures already restrict relief for current period allowances to profits deemed to arise from the intangibles, net of financing expense. The recommendation is to restore a previous cap on current period capital allowance deductions to 80% of these separate profits (net of financing expense).
  - Timing of implementation uncertain.
  - If enacted, depending on the profitability of the claimant, this could slow down the use of the allowances. However, it is not suggested to restrict the use in future periods of excess current period allowances, which should carry forward indefinitely.
- No recommendation to change the scope of eligible asset expenditure or the rate of claim of allowances on intangibles.
- No changes to Ireland's R&D tax credit regime or to the Knowledge Development Box.
- Updating Ireland's use of OECD transfer pricing guidelines to the 2017 guidelines will focus pricing of intangibles on attributing profits to the value added by functions related to the Development, Enhancement, Management, Protection and Exploitation (DEMPE) of the intangibles.

  Timing of adoption is uncertain but recommended to be implemented no later than the end of 2020.

BEPS, transparency and other matters

- Ireland has already committed to adopt minimum standard measures to counteract Base Erosion and Profit Shifting (anti-BEPS) recommended by the OECD and those set out under European Union (EU) Anti-Tax Avoidance Directives (ATAD). The Report recommends implementation should take account of consultation feedback and remain aligned with OECD recommendations. Measures include:
  - Adoption of a controlled foreign company (CFC) regime from 1 January 2019 with possibility of exemption for foreign branch income and foreign connected company dividends or simplification of current credit relief measures.
  - Anti-hybrid mismatch measures from 1 January 2020.
  - Revised exit tax regime from 1 January 2020.
  - Ireland's existing general anti-avoidance rule (GAAR) may meet ATAD standards.
  - Ireland intends to defer implementation of the ATAD Interest Limitation Rule based on its assessment of the equivalent protection afforded under existing anti-abuse measures targeted at excessive deductions for financing expense.
- Having achieved the highest rating on transparency from the Global Forum on Transparency and Exchange of Information for Tax Purposes, Ireland should continue to take account of peer review recommendations, continue to support EU proposals for Mandatory Disclosure of certain tax planning in alignment with OECD BEPS Action 12 recommendations and pass the Taxation and Certain Other Matters (International Mutual Assistance) Bill to enhance Ireland's capacity related to mutual assistance and cooperation on tax matters.
- Ensure Ireland adequately resources its Competent Authority to reduce uncertainty in implementation of changes to the international tax framework including support for enhanced dispute resolution mechanisms for taxpayers.

Recommended for implementation/remain unchanged

Implementation subject to consultation and ongoing scrutiny that measures to not afford preferential treatment to any taxpayer

Preparing for implementation of Report recommendations

What will expanding the scope of transfer pricing mean?

Applying transfer pricing requirements to trading and non-trading transactions would require a change of mindset for Irish based business – greater rigour and formality when transacting intra group transactions, as well as streamlining intra group processes.

Report recommendations of interest:
Applying arm's length pricing to trading and non-trading transactions – both domestic and cross border.

Adoption of current OECD guidelines on transfer pricing. This could affect your group's approach to transfer pricing intangible assets, the split of profits in a global supply chain and the allocation of profits to branches.

What should you do?

- Review and identify group arrangements whether domestic or cross border where transfer pricing adjustments are not made because the transaction is non-trading.

  Common arrangements include the advance of intra group loans at below market rates (both domestic and cross border) or intra group informal property letting arrangements (domestic).

  Review the impact on cash tax and the group's effective tax rate of adjusting these flows to an arm's length basis.

  Review current interest free loan arrangements to consider if they meet the medium/longer term requirements of your business.
- Alternatives to existing intra group arrangements might include centralising and supporting intra group arrangements with additional infrastructure and carrying on intra group lending, treasury and other support activities as a trade taxed at 12.5%
- Up to now, growing businesses did not have to address formal Irish transfer pricing requirements until they exceeded the size thresholds applicable to SMEs. If transfer pricing requirements are extended to smaller entities, they may need to put in place transfer pricing procedures that can be flexed as they grow.

Are group profits underpinned by intangible assets?

Understanding the location of both the operational and strategic management of the risks, functions and related profits from the development and exploitation of intangibles will be important to identifying the future measure and timing of Irish taxable profits.

Report recommendations of interest:
Capping current period capital allowances claims on expenditure on intangible assets at 80% of taxable profits (net of financing costs) from the development and exploitation of intangible assets.

Adoption of current OECD guidelines on transfer pricing of intangible assets.

What should you do?

- If you are claiming allowances on intangible asset expenditure, review the cash tax and accounting income tax effect of capping each current period allowances claims at 80% of relevant profits. This review should take into account the potential increased capacity to absorb credit relief for foreign taxes borne on royalty income together with the possibility of claiming relief under the Knowledge Development Box 6.25% tax regime.
- If planning future expenditure on intangibles, consider the impact of cap recommendations on the timing of relief claims.
- The current OECD guidelines on transfer pricing for intangibles focus on attributing profits to the value added by key decision makers.

  Understanding where decision makers are located and how key decisions are made at various levels is an important step in understanding if your transfer pricing approach to the recognition of Irish profits from intangible assets is aligned with current OECD guidelines.

Are you ready for the impact of anti-BEPS measures?

Are you ready to have your voice heard? Insights and feedback drawn from real life businesses have the greatest effect when legislators draft measures – so that – when adopted, they can preserve the attractions of Ireland's regime.

Report recommendations of interest:
Public consultation on ATAD measures including a CFC regime from 1 January 2019 together with measures to counteract hybrid mismatches and a revised exit tax regime by 1 January 2020.

Adoption of current OECD guidelines on transfer pricing of intangible assets amongst other matters.

What should you do?

- Review current Irish group holding arrangements to understand the tax profile and nature of activities conducted by foreign subsidiaries and branches.

  Does your review suggest that adoption of a dividend/branch profit exemption in tandem with a CFC regime would make a good fit for your group?

  Which of the two forms of CFC regime permitted under ATAD would be the best fit for your business?

  These are matters likely to be under debate in a consultation process.
- Existing intra group arrangements (whether related to interest, royalties or other business transactions) that result in taxation mismatches due to hybrid arrangements will no longer be effective from 1 January 2020.

  Have you considered the impact on group payment flows and effective tax rate of adopting arrangements not in scope?
- Life happens – and business must respond. Have you considered the impact of a revised exit tax regime from 1 January 2020 if future business plans require a transfer of assets/business from Ireland?

Contact us:
For more information and to have your voice heard in the consultation process, please contact your usual KPMG client service team or:

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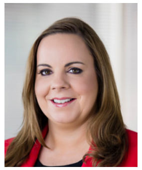

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