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Recent Developments in International Taxation

Ireland

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Major Irish developments in 2021

The principal Irish legislative changes during 2021 were announced in Budget 2022 and enacted in Finance Act 2021. Finance Act 2021 completed the Irish implementation of some final measures of the EU Anti-Tax Avoidance Directives (‘ATAD’), including implementing interest limitation rules and anti-reverse hybrid rules into Irish law.

Finance Act 2021 also introduced some helpful reliefs from Irish capital gains tax (CGT) for merger transactions and formally implemented the authorised Organisation for Economic Co-operation and Development (OECD) approach to attributing profits to branches. Other measures contained in Finance Act 2021 included clarification regarding the exemption from Irish transfer pricing rules for certain domestic Irish transactions, the introduction of a new credit regime for digital gaming businesses and the transposition of DAC 7, a European Union reporting regime applicable to certain digital platforms.

Another recent development following the relaxation of Covid-19 restrictions has been the cessation of government support available to businesses during the Covid-19 pandemic.

New Irish interest limitation rules

Ireland implemented interest limitation rules in Finance Act 2021 in accordance with ATAD with effect for accounting periods commencing on or after 1 January 2022. These rules apply to limit tax deductions for net borrowing costs at 30 per cent of (adjusted) earnings before interest, taxes, depreciation and amortisation (EBITDA) in certain circumstances.

Helpfully, there are a number of exemptions from these interest limitation rules. The rules do not apply to net borrowing costs below the €3m de minimis threshold set out in ATAD. There are also exemptions available for standalone companies, legacy debt (the terms of which were agreed before 17 June 2016) and certain long-term infrastructure projects.

The interest limitation rules include an option for companies to operate the rule on a single entity or local group basis and for certain group reliefs to apply where the Irish taxpayer is part of a consolidated worldwide group for accounting purposes by applying an equity ratio rule or group ratio rule.

Any disallowed interest may be carried forward to a tax year in which interest capacity is available. Surplus interest capacity in an accounting period can be carried forward for up to five years.

Introduction of anti-reverse hybrid rules

Ireland had previously implemented anti-hybrid rules in line with ATAD with effect from 1 January 2020. Finance Act 2021 expanded these rules to capture reverse hybrids with effect from 1 January 2022.

The anti-reverse hybrid rules apply to treat certain entities that are normally transparent for Irish tax purposes (e.g., Irish partnerships) as taxable entities in certain circumstances. As a result, these rules will now tax certain income in Ireland that would otherwise have gone untaxed because a hybrid entity was regarded as transparent in Ireland but tax opaque in the territory of its participator.

Importantly, these anti-reverse hybrid rules do not apply where profits are attributable to a participator that is:

- exempt from tax in the territory in which it is established;
- established in a territory that does not impose a foreign tax; or
established in a territory that does not impose a tax on income or profits derived from sources abroad.

These rules also contain an exemption for collective investment schemes, including regulated Irish investment funds, provided such funds are widely held and hold a diversified portfolio of assets.

**CGT relief for merger by absorption**

Finance Act 2021 introduced a helpful new relief from CGT for domestic mergers by absorption where a subsidiary merges into its parent entity. In the case of such mergers, the Irish parent company will no longer be viewed as disposing of the shares held in the Irish subsidiary that is merging into it for Irish CGT purposes. This automatic relief removes the need to satisfy the conditions for the Irish substantial shareholder exemption (including, in particular, a trading test) to avoid a charge to CGT in the case of a domestic merger by absorption.

Finance Act 2021 also updated the equivalent rule that applied to EU cross-border mergers by absorption to ensure similar treatment applies to EU cross-border mergers. Previously, there was a technical issue with the existing CGT relief for EU cross-border mergers by absorption, but the relieving provision has now been amended to remove any doubt as to the application of the relief.

Therefore, where an Irish resident company disposes of shares in a subsidiary (whether resident in Ireland or the EU) as a result of a merger by absorption, no charge to CGT should arise for that Irish parent company.

**Formal implementation of the authorised OECD approach for profit attribution to branches of non-resident companies**

Finance Act 2021 introduced into Irish law the Authorised OECD Approach to the attribution of profits to branches of non-resident companies (the 'AOA') operating in Ireland for accounting periods commencing on or after 1 January 2022. This amendment essentially codified the requirement to comply with OECD guidance and also introduced prescribed documentation requirements for the purpose of ensuring that relevant branch income has been computed in line with such guidance.

Penalties will apply for taxpayers who fail to provide relevant branch records to the Irish Revenue Commissioners. The application of the AOA to small and medium-sized enterprises is subject to the implementation of a Ministerial Order.

**Phasing out of Covid-19 support and concessions**

Throughout the period in which Covid-19 restrictions were in place, Ireland offered a wide range of support for businesses that were required to prohibit or restrict customer access to their premises. These measures included the Covid-19 Restrictions Support Scheme, Business Resumption Support Scheme and Employment Wage Subsidy Scheme. However, these support schemes have now been wound down.

Furthermore, a number of concessions that were afforded by the Irish Revenue Commissioners to businesses in relation to the tax treatment of employees and directors who were unable to travel due to Covid-19-related travel restrictions have also been phased out.

A debt warehousing scheme introduced to assist businesses struggling to make tax payments as a result of the impact of Covid-19 is also currently being phased out. This scheme allowed unpaid VAT and payroll debts resulting from the pandemic to be 'parked' for 12 months, from January 2022 to
December 2022. After the expiration of this 12-month period, employers can repay such warehoused debts at a reduced rate of interest.

**Implementation of OECD Pillar Two proposals**

Ireland is one of the signatories to the OECD/Group of Twenty (G20) Inclusive Framework agreement to reform the international tax framework as it applies to large corporate groups. Ireland supports the proposal for the Pillar Two rules to be implemented in a consistent manner across the EU by way of an EU directive.

Subject to all EU Member States reaching unanimous agreement on the current proposed directive, this text will provide the primary basis for the transposition of Pillar Two in Ireland. The EU’s current goal is for the proposed directive to be transposed and operational in EU Member States (including Ireland) by 31 December 2023. It is intended that, once agreed, the EU directive will be transposed into Irish law via future finance acts.

In May 2022, the Irish Department of Finance opened a public consultation on Pillar Two, seeking feedback from stakeholders as to how these rules should be implemented in Ireland. In the consultation document, it was noted that, as Ireland’s 12.5 per cent trading rate of corporation tax is below the agreed minimum effective rate of 15 per cent, it is very likely that Ireland will introduce a qualified domestic minimum top-up tax.

**Update on Ireland’s double taxation agreements**

Ireland’s double tax treaty negotiating team has been active in the past year. In 2021, Ireland signed new double tax agreements with Kosovo and Kenya. Ireland also signed protocols to existing treaties with the Isle of Man and Guernsey in 2021. In addition, the protocol to the double tax agreement between Ireland and Germany and amending protocol entered into effect on 1 January 2022.