Irish Tax Institute

April 2019

Response to the Department of Finance Public Consultation on Ireland's Transfer Pricing Rules

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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 30,000-strong international CTA network and a member of *CFE Tax Advisers Europe*, 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

In October 2017, the Department of Finance launched a public consultation on the recommendations contained in the Coffey Review.[1] The Institute responded to that consultation in January 2018, setting out our views on Mr Coffey's recommendations regarding proposed changes to Ireland's transfer pricing regime.[2]

The current Consultation[3] now invites stakeholders to provide further input on the Minister for Finance's proposed implementation of Mr Coffey's recommendations regarding transfer pricing. The Irish Tax Institute welcomes this opportunity to engage with the Department on the proposed introduction of wide-ranging changes to Ireland's transfer pricing regime.

Businesses in Ireland have been applying arm's length pricing to arrangements in accordance with the 2010 OECD Transfer Pricing Guidelines since 2011. The Institute fully supports the implementation of the standards contained in the OECD BEPS Actions 8-10 and Action 13 into Irish law, through the adoption of the 2017 OECD Transfer Pricing Guidelines.

We would suggest however that the 2017 Guidelines should apply to accounting periods commencing on or after 1 July 2020, to allow Irish businesses some time to assess the impact of the updated 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.

In addition to the adoption of updated OECD Guidelines, the Consultation Paper also invites feedback on the intended direction of a number of other significant reforms to Ireland's transfer pricing regime:

- If the grandfathering provisions are removed from 1 January 2020, clear guidance must be provided by Revenue regarding the repricing of existing grandfathered transactions and recognition given for limitations on data availability in pricing pre-1 July 2010 grandfathered arrangements.

- 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 disproportionate to any tax risk arising.

- As Ireland has a separate 25% corporation tax rate for non-trading income, the proposed extension of transfer pricing rules to non-trading income could result in mismatches and consequently, increased taxation. Policymakers could consider excluding domestic non-trading transactions from the scope of transfer pricing rules in order to minimise the potential impact of the differing corporation tax

[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] http://taxinstitute.ie/Portals/0/Tax%20Policy/Institute%20Submission/2018/2017%2001%2030%20ITI%20response%20to%20consultation%20on%20coffey%20review%20Final.pdf
[3] Department of Finance, Ireland's Transfer Pricing Rules, Public Consultation, February 2019

rates applying in domestic situations. Non-application of transfer pricing rules to domestic transactions would be compliant with EU law.[4]

- A range of provisions under tax law currently exist to ensure market value applies to related-party capital transactions. Layering transfer pricing provisions on top of existing measures would place a significant burden on taxpayers in situations where any tax risk has already been addressed. Policymakers should consider introducing a hierarchy within the tax code or aligning the existing legislation that applies market value to capital transactions with transfer pricing principles, to alleviate the significant documentation burden on taxpayers.

- Ireland should adopt the OECD set of common criteria in Annex I and II of the 2017 Guidelines for Master and Local Files, as the standard for content for transfer pricing documentation. The filing of Master and Local Files should be upon written request by Revenue, as is the case in many EU and OECD member countries, rather than imposed as a mandatory filing requirement.

- In principle, we would consider it appropriate to adopt the Authorised OECD Approach (AOA) for the attribution of branch profits into Irish law. However, we believe more time is needed for further consultation with the financial services industry and other relevant sectors, to ensure that there are no unintended consequences resulting from the proposed adoption of the AOA approach.

In view of the significance of the intended changes to the existing transfer pricing regime, it is an imperative that stakeholders are given the opportunity to consult on draft legislation well in advance of the measures commencing and clear and comprehensive Revenue guidance will be published in tandem with the new legislative provisions, so that businesses can have certainty regarding the application of the new measures in practice.

In conclusion, a well-resourced Competent Authority will also be critical to deal with the probable increase in international disputes and Mutual Agreement Procedures that are likely to occur following the adoption of the OECD 2017 Guidelines into Irish law.

Moreover, the Directive on Double Taxation Dispute Resolution Mechanisms in the EU[5] requires tax authorities to reach agreement on mutual agreement procedures within two years, otherwise binding arbitration procedures can be initiated by taxpayers. This reinforces the need for a well-resourced Competent Authority.

[4] The Court of Justice of the European Union decision in the case of C-382/16 Hornbach-Baumarkt which determined that Germany's transfer pricing legislation that differentiates between domestic and foreign transactions was consistent with the EU freedom of establishment.
[5] Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union.

3. List of Recommendations

Incorporation of the OECD 2017 Guidelines into Irish legislation

1. We would suggest that the OECD 2017 Guidelines should apply to accounting periods commencing on or after 1 July 2020, to allow Irish businesses the 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.

2. When adopting the 2017 Guidelines, it should be made clear that they will apply prospectively. However, provision should also be made for taxpayers to elect for early adoption of the 2017 Guidelines, instead of the 2010 version for 2018 and 2019 accounting periods, to allow certain taxpayers to achieve consistency in pricing across the group, where they operate in counterparty jurisdictions that already apply the 2017 Guidelines.

3. A well-resourced Competent Authority will be critical to deal with the increase in international disputes and Mutual Agreement Procedures that are likely to occur following the adoption of the OECD 2017 Guidelines into Irish law.

Removal of grandfathering for pre-1 July 2010 arrangements

4. If the grandfathering provisions are removed from 1 January 2020, clear guidance must be provided by Revenue regarding the repricing of existing grandfathered transactions.

5. It is important to recognise the limitations on data availability in pricing previously grandfathered arrangements and therefore, a practical approach should be adopted by Revenue to the documentation requirements for such transactions.

6. The timing of the removal of the grandfathering provisions should coincide with any proposed extension of transfer pricing rules to non-trading transactions, so as to minimise any potential mismatches in tax treatment which could arise.

Extension of transfer pricing rules to SMEs

7. We strongly support the continued exemption for SMEs from the Irish transfer pricing regime.

8. If policymakers decide to remove the current general exemption for SMEs, at a minimum the extension of the transfer pricing rules should be confined to medium sized entities and *de minimis* thresholds should be introduced into both the pricing provisions and the documentation requirements to reduce the significant compliance burden.

9. Should policymakers decide to remove the current exemption for SMEs from the Irish transfer pricing regime, SMEs will need a significant lead-in time, given their limited resources, to review their existing arrangements and take the necessary steps to put

appropriate documentation in place to ensure that they are compliant with the transfer pricing rules.

Extension of transfer pricing rules to non-trading transactions

10. Careful consideration should be given to unintended mismatches and consequential double taxation that could arise for intra-group lending in domestic situations, should the transfer pricing rules be broadened to include non-trading income. These are interlinked with the reform of Ireland's interest deductibility rules that is currently under consideration by policymakers.

11. Policymakers could consider excluding domestic non-trading transactions from the scope of Irish transfer pricing rules, within the defined parameters of EU law, in order to minimise the potential impact of the differing corporation tax rates applying to parties to a domestic transaction.

12. If policymakers extend transfer pricing provisions to non-trading transactions, exemptions for loans or other forms of debt provided by an Irish company to direct or indirect subsidiaries could also be considered, which would reflect the economic reality of such funds as quasi-equity.

13. It would be important to maintain tax neutrality should the transfer pricing rules be extended to non-trading income in Ireland. Therefore, provision for corresponding adjustments should be permitted at the same tax rate and on a current year basis, rather than the following year, which is currently the case.

14. 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. Extending transfer pricing rules to capital transactions, without alleviating provisions, would place an unnecessary additional burden on taxpayers.

15. A hierarchy should be introduced within the tax provisions, to alleviate the significant compliance burden that would result from layering an additional transfer pricing documentation requirement for capital transactions, on top of the existing market value provisions.

16. Alternatively, consideration could be given to aligning the existing legislation that applies market value to capital transactions with transfer pricing legislation, such that the use of accounting valuations for capital gains tax purposes could satisfy the documentation requirements for transfer pricing purposes.

Transfer Pricing Documentation

17. Ireland should adopt the OECD set of common criteria in Annex I and II of the 2017 Guidelines for Master and Local Files, as the standard for content for transfer pricing documentation.

18. In our view, 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.

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

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

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

22. The timing for the preparation of transfer pricing documentation should remain in line with current practice; being available no later than when the Irish corporation tax return is due for the accounting period in which the transaction was reflected.

23. Penalty protection measures put forward in the OECD 2015 BEPS Action 13 Report could be considered to encourage transfer pricing documentation compliance.

Application of transfer pricing rules to branches

24. In principle, we would consider it appropriate to adopt the Authorised OECD Approach (AOA) for the attribution of branch profits into Irish law. However, we believe more time is needed for further consultation with the financial services industry and other relevant sectors to ensure that there are no unintended consequences resulting from the proposed adoption of the AOA approach.

25. Detailed Revenue guidance regarding the application of the AOA in an Irish context would be required to provide certainty for business, given the differing views that have been taken by tax authorities around the world regarding aspects of the AOA.

4. Response to Consultation Questions

4.1 Incorporation of the OECD 2017 Guidelines into Irish legislation

- *It is intended that Irish transfer pricing legislation will be amended to include a direct reference to the 2017 OECD Transfer Pricing Guidelines. Do you consider that this proposed course of action will give rise to any specific issues?*

Ireland has had transfer pricing legislation[6] since 2011. It applies arm's length pricing to arrangements agreed after 1 July 2010,[7] in accordance with the OECD Transfer Pricing Guidelines published in July 2010.[8] The 2017 OECD Transfer Pricing Guidelines incorporate the guidance set out in the OECD's Base Eroding Profit Shifting (BEPS) Actions 8, 9 and 10.[9]

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 that are more closely aligned with value creation. We believe Ireland's transfer pricing legislation should be updated to refer to the 2017 Guidelines in order to meet the internationally agreed standards in BEPS Actions 8, 9 and 10.

For many types of intercompany transactions there may be no difference to the arm's length analysis, irrespective of whether the 2010 or the 2017 OECD Guidelines are applied. 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.

Timing

To ensure effective compliance and implementation of the transfer pricing regime going forward, it is essential that careful consideration is given to the sequencing of the change to Irish law to reflect the 2017 Guidelines, including the publication of comprehensive Revenue guidance.

Mr Coffey recommended in his *Review of Ireland's Corporation Tax Code*[10], that if the Government decided to implement any or all of his recommendations on updating Ireland's transfer pricing rules, including the adoption of the 2017 Guidelines, that this should take place no later than the end of 2020.

If it is intended to adopt the 2017 Guidelines in Finance Bill 2019, we would recommend that there is short lead-in time provided to business between the enactment of the Bill and the operative date of the 2017 OECD Guidelines, given the very short timeframe between the publication of the Finance Bill in mid-October and its entry into force at the end of the year.

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[6] Part 35A 1997
[7] Section 835A (1) TCA 1997
[8] Section 835D TCA 1997
[9] OECD/G20 Base Erosion and Profit Shifting Project: Aligning Transfer Pricing Outcomes with Value Creation, Actions 8-10 - 2015 Final Reports, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris - http://dx.doi.org/10.1787/9789264241244-en
[10] Review of Ireland's Corporation Tax Code, Seamus Coffey, June 2017.

This would allow Irish businesses some time to adjust their operations and current pricing where necessary to meet the 2017 Guidelines. We would suggest that the new OECD source guidelines could apply to accounting periods commencing on or after 1 July 2020. This would afford businesses a greater opportunity to ready themselves for the impact of the new rules on their operations and provide the necessary tax certainty, which influences business investment and location decisions.[11]

When adopting the 2017 Guidelines, it should be made clear that they will apply prospectively and that the 2010 version will continue to apply to accounting periods prior to transposing the 2017 Guidelines into Irish law.

However, some Irish businesses may already operate in a setting where the 2017 OECD Guidelines are applied in counterparty jurisdictions and have elected for early adoption of the 2017 OECD Guidelines to achieve greater consistency in pricing across the group. It is important therefore that provision is made for such taxpayers, to permit early adoption of the 2017 OECD Guidelines for 2018 or 2019 accounting periods.

In addition, consideration will need to be given to how impending OECD guidance on financial transactions will be reflected in Irish law once issued.

Revenue Guidance

Irish taxpayers will need clear and comprehensive guidance from the Revenue Commissioners on how the 2017 OECD Guidelines will be implemented in practice to reduce tax uncertainty and this should be available when the new framework becomes law.

It is critical that the scope and application of the 2017 Guidelines is clarified for existing transactions, matters under audit and matters with the Competent Authority.

Further guidance and examples from Revenue on what would be regarded as control over the Development, Enhancement, Maintenance, Protection and Exploitation (DEMPE) functions relating to intangible assets from an Irish perspective would be helpful. In framing that guidance, it would also be useful to explore examples of what the difference in application in practice would be between the 2017 Guidelines and the 2010 version.

Competent Authority

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.

In order to deal with the inevitable increase in international disputes and Mutual Agreement Procedures that are likely to occur, it is vital that there is a well-resourced Competent Authority in place, which has the capacity to address and conclude issues on a timely basis. Furthermore, the Directive on Double Taxation Dispute Resolution

[11] Update on Tax Certainty, IMF/OECD report for G20 Finance Ministers and Central Bank Governors, July 2018.

Mechanisms in the EU[12] requires tax authorities to reach agreement on mutual agreement procedures within two years, otherwise binding arbitration procedures can be initiated by taxpayers. This reinforces the need for a well-resourced Competent Authority.

Institute Recommendations:

We would suggest that the OECD 2017 Guidelines should apply to accounting periods commencing on or after 1 July 2020, to allow Irish businesses some 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.

When adopting the 2017 Guidelines, it should be made clear that they will apply prospectively. However, provision should also be made for taxpayers to elect for early adoption of the 2017 Guidelines, instead of the 2010 version for 2018 and 2019 accounting periods, to allow certain taxpayers to achieve consistency in pricing across the group, where they operate in counterparty jurisdictions that already apply the 2017 Guidelines.

A well-resourced Competent Authority will be critical to deal with the increase in international disputes and Mutual Agreement Procedures that are likely to occur following the adoption of the OECD 2017 Guidelines.

[12] Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union.

4.2 Removal of grandfathering for pre-1 July 2010 arrangements

- *It is intended to extend the transfer pricing legislation to arrangements the terms of which were agreed before 1 July 2010, commencing from 1 January 2020. Do you consider that this proposed course of action will give rise to any specific issues?*

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 that were in place before 1 July 2010 would be excluded from the regime.[13]

There was no indication at the time that the grandfathering provisions would expire in the future, but rather the arrangements would gradually become un-grandfathered, as and when the terms of the arrangements were altered.

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 Irish transfer pricing rules, provided the terms of the arrangement remained unchanged.

If the grandfathering provisions are to be removed from 1 January 2020, clear guidance must be provided by Revenue regarding the repricing of existing arrangements. To the extent that some businesses have pre-1 July 2010 intercompany agreements that remain in place, for example, a long-term 30-year loan with 15 years left to run, what factors must be considered when repricing the loan?

The level of detail that you would generally expect in circumstances where documentation is prepared contemporaneously is unlikely to be available where the documentation would be prepared a decade or more after a transaction was contemplated.

The limitations on data availability in pricing previously grandfathered transactions should be recognised and therefore, a practical approach should be adopted by Revenue to the documentation requirements for such transactions.

Furthermore, the timing of the removal of the grandfathering provisions should coincide with any proposed extension of transfer pricing rules to non-trading transactions, so as to minimise any potential mismatches in tax treatment which could arise.

Institute Recommendations:
If the grandfathering provisions are removed from 1 January 2020, clear guidance must be provided by Revenue regarding the repricing of existing grandfathered transactions.

It is important to recognise the limitations on data availability in pricing previously grandfathered transactions and therefore, a practical approach should be adopted by Revenue to the documentation requirements for such transactions.

The timing of the removal of the grandfathering provisions should coincide with any proposed extension of transfer pricing rules to non-trading transactions, so as to minimise any potential mismatches in tax treatment which could arise.

[13] Part 35A TCA 1997

4.3 Extension of transfer pricing rules to SMEs

- *Do you consider that transfer pricing legislation should be extended to small and medium enterprises?*
- *What level of documentation do you feel would be appropriate to require SMEs to maintain, to demonstrate compliance with transfer pricing rules?*
- *If transfer pricing rules are extended to SMEs, what other measures might be considered to mitigate the compliance burden for SMEs?*
- *What particular issues do you consider might arise from the application of transfer pricing rules to SME transactions with effect from 1 January 2020?*

The Institute supports the continued exemption[14] 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[15] in Irish legislation refers to the European Commission Recommendation that was adopted on 6 May 2003, which replaced the previous definition agreed in 1996.

It is worth noting that an exemption for SMEs is a feature of transfer pricing legislation in many other EU jurisdictions. Countries such as the UK, the Netherlands and Germany all have exemptions based on the EU SME definition, however, there can be conditions attached to the exemption.

For example, in the UK, the exemption does not apply to transactions between related parties where the other party is in a territory where the UK does not have a double tax agreement with an appropriate non-discrimination article. However, it is open to HMRC to notify a medium sized entity that it must apply transfer pricing for a particular period.

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. Indeed, stated Government policy[16] encourages SMEs to pursue diversification of export markets. Imposing additional costs and administrative burdens on those firms that enter new export markets could act as a barrier to achieving those policy goals.

Due to the relatively small size of the Irish economy, Irish SMEs tend to engage in cross border transactions at a much earlier stage in their growth, than is the case for many SMEs operating in larger economies. This might be considered to create a risk of loss of tax revenues for the Exchequer from SMEs mispricing cross border transactions. However, given our 12.5% corporation tax rate and the fact that SME operations

[14] Section 835E Taxes Consolidation Act 1997
[15] Commission Recommendation 2003/361/EC of 6 May 2003
[16] Enterprise 2025 Renewed, March 2018 and Global Ireland: Ireland's Global Footprint to 2025, June 2018.

generally do not have high-value transactions, the risk they pose from a transfer pricing perspective is low.

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"*[17] 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 policymakers wish to remove the current general exemption for SMEs, at a minimum, the extension of the transfer pricing rules should be confined to medium-sized entities. In addition, we would strongly recommend introducing *de minimis* thresholds into both the pricing provisions[18] and the documentation requirements[19]. 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.

If the basic transfer pricing rules[20] 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. Paragraphs 33 of Action 13[21] recommends that SMEs should not be required to produce documentation that might be expected from larger enterprises. Simplified documentation requirements for SMEs forms part of the transfer pricing rules in jurisdictions such as France and Australia.

De minimis 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.

[17] Section 81(2)(a) Taxes Consolidation Act 1997
[18] Section 835C Taxes Consolidation Act 1997
[19] Section 835D Taxes Consolidation Act 1997
[20] Section 835C Taxes Consolidation Act 1997
[21] OECD (2015), Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. http://dx.doi.org/10.1787/9789264241480-en

- 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.

Should policymakers decide to remove the current exemption for SMEs from the Irish transfer pricing regime, such businesses will require a significant lead-in time, given their limited resources, to review their existing arrangements and take such steps that are necessary to put appropriate documentation in place to ensure that they are compliant with the transfer pricing rules.

Institute Recommendations:

We strongly support the continued exemption for SMEs from the Irish transfer pricing regime.

If policymakers decide to remove the current general exemption for SMEs, at a minimum, the extension of the transfer pricing rules should be confined to medium sized entities and *de minimis* thresholds should be introduced into both the pricing provisions and the documentation requirements to reduce the significant compliance burden.

Should policymakers decide to remove the current exemption for SMEs from the Irish transfer pricing regime, SMEs will need a significant lead-in time, given their limited resources, to review their existing arrangements and take the necessary steps to put appropriate documentation in place to ensure that they are compliant with the transfer pricing rules.

4.4 Extension of transfer pricing rules to non-trading transactions

- *It is intended to extend the transfer pricing rules to non-trading income chargeable to tax under Case III, Case IV and Case V of Schedule D where such an extension would reduce the risk of aggressive tax planning as recommended by the Coffey Review. Are there issues which may arise through the extension of transfer pricing rules to non-trading income and how may any such issues be resolved?*
- *Do you believe that the current market value rules are sufficient so that capital transactions do not need to be subject to separate transfer pricing rules? Could these rules be supplemented by additional documentation requirements?*

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.

In general, there is no net transfer pricing exposure where both parties to a transaction are located within the same jurisdiction, as any understated profits of one party will be matched by overstated profits of the other entity. 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 increased taxation.

The impact of the two rates is particularly relevant in the context of Ireland's interest deductibility rules. If the scope of transfer pricing legislation is broadened to include non-trading income, interest income could be taxed in a non-trading entity at 25% with either no deduction or only a deduction at 12.5%, 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 and provision for corresponding adjustments should be permitted at the same tax rate and on a current year basis, rather than the following year, which is currently the case.

Policymakers could consider excluding domestic non-trading transactions from the scope of transfer pricing rules, in order to minimise the potential impact of differing corporation tax rates applying to parties to a domestic transaction. For example, an exclusion for domestic transactions has been adopted in Germany, France and Finland and in some countries, such as the Netherlands, transactions between members of a tax group are entirely ignored for tax purposes. Indeed, the Court of Justice of the European Union recently determined that the non-application of German transfer pricing rules to domestic transactions to be complaint with EU law.[22]

[22] The Court of Justice of the European Union in the case of C-382/16 Hornbach-Baumarkt (relying on the judgement in Société de Gestion Industrielle SA (SGI) v État belge (Case C-311/08)) ruled that Germany's transfer pricing legislation, which differentiates between domestic and foreign transactions was consistent with the EU concept of freedom of establishment.

We believe that extending transfer pricing rules to non-trading cross-border transactions, whilst exempting domestic transactions, could address the BEPS concerns associated with the provision of cross border interest-free loans.

If policymakers extend transfer pricing provisions to non-trading transactions, exemptions for loans or other forms of debt provided by an Irish company to direct or indirect subsidiaries could also be considered. For example, there are provisions in the Canadian tax code which effectively recognise that loans by a shareholder to a direct or indirect subsidiary is a substitute for capital.[23] Such an exemption would reflect the economic reality of such funds as quasi-equity.

Careful consideration should also be given to unintended consequences that could arise, given the test for applying Irish transfer pricing rules would no longer be whether the transaction is a trading or non-trading transaction. For example, the potential impact such a change in Ireland's transfer pricing rules could have on group loss relief claims or indeed, guarantees by parent companies to their subsidiaries under section 357 Companies Act 2014.

Institute Recommendations:

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

Policymakers could consider excluding domestic non-trading transactions from the scope of Irish transfer pricing rules, in order to minimise the potential impact of the differing corporation tax rates applying to parties to a domestic transaction.

If policymakers extend transfer pricing provisions to non-trading transactions, exemptions for loans or other forms of debt provided by an Irish company to direct or indirect subsidiaries could also be considered, which would reflect the economic reality of such funds as quasi-equity.

It would be important to maintain tax neutrality should the transfer pricing rules be extended to non-trading income in Ireland. Therefore, provision for corresponding adjustments should be permitted at the same tax rate and on a current year basis, rather than the following year, which is currently the case.

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[23] Section 17 of Income Tax Act (Canada) sets out that when a taxpayer provides a loan to a related party borrower, then subsection 17(1) requires the taxpayer to recognize in its taxable income any amount of incremental interest that would otherwise be charged to an arm's length borrower. However, subsection 17(7) provides and exemption in that *"subsection (1) does not apply in respect of an amount owing to a corporation resident in Canada by a non-resident person if a tax has been paid under Part XIII on the amount owing, except that, for the purpose of this subsection, tax under Part XIII is deemed not to have been paid on that portion of the amount owing in respect of which an amount was repaid or applied under subsection 227(6.1)."* A specific transfer pricing provision is found in Section 247(2) of Income Tax Act (Canada) – which requires taxpayers to price any transactions with related parties based on arm's length terms. However, subsection 247(7) provides an exemption where a non-resident person owes an amount to the corporation and the non-resident person is a controlled foreign affiliate of the corporation *"subsection (2) does not apply to adjust the amount of interest paid, payable or accruing in the year on the amount owing"*[23]

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. Without alleviating provisions, 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 Taxes Consolidation Act (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.

Each of the above provisions require detailed and robust written documentation to be in place to support the underlying capital transaction. Layering an additional transfer pricing documentation requirement for capital transactions, on top of the existing market value provisions, could create an unduly excessive compliance burden for taxpayers.

If it is intended to extend transfer pricing rules to capital transactions and retain existing market value provisions, then there should be a hierarchy within the tax provisions. For example, if the valuation requirements for section 291A TCA 1997 are satisfied, then section 835 TCA 1997 would not apply.

Alternatively, aligning existing legislation that applies market value to capital transactions with transfer pricing legislation could alleviate the documentation burden on taxpayers. For example, if the legislation could facilitate the use of accounting valuations undertaken for capital gains tax purposes to satisfy the documentation requirements for transfer pricing purposes.

Institute Recommendations:

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. Extending transfer pricing rules to capital transactions, without alleviating provisions, would place an unnecessary additional burden on taxpayers.

A hierarchy should be introduced within the tax provisions, to alleviate the significant compliance burden that would result from layering an additional transfer pricing documentation requirement for capital transactions, on top of the existing market value provisions.

Alternatively, consideration could be given to aligning the existing legislation that applies market value to capital transactions with transfer pricing legislation, such that the use of accounting valuations for capital gains tax purposes could satisfy the documentation requirements for transfer pricing purposes.

4.5 Transfer Pricing Documentation

- *What particular issues do you consider might arise if the enhanced documentation requirements were to apply from 1 January 2020?*
- *Are there any circumstances in which the documentation requirements should be reduced or limited in specific respects?*

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-Country Reporting[24] 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.

The following issues should be considered when determining an appropriate documentation regime.

Content for Master Files/Local Files

The OECD has developed a set of common criteria in Annex I and II of the 2017 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 businesses.

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.

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. For example, Germany has set the revenue threshold for Master File at €100m, while France has opted for €400m, Indeed, Australia has taken the approach of using the same threshold as for Country-by-Country Reporting[25] when implementing Master File/Local File requirements into Australian tax law.

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.

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

Implementation Considerations for Local File

There are two elements that should be considered when developing Local File documentation requirements.[26] Firstly, Irish taxpayers could be allowed the option 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*"[27] and "*which are material in the context of the local country's tax system."*[28]

In section 4.3, we suggested *de minimis* thresholds for determining whether a transaction should be documented, analysed and validated in the event that Irish transfer pricing rules are extended to SMEs. We believe that the same *de minimis* thresholds could equally apply to documentation requirements for the Local File.

Timing of 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 the current practice of being available when the Irish corporation tax return is due (i.e. within nine months of the accounting year-end).[29] 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[30] 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.

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[26] 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.
[27] Chapter V, Transfer Pricing Documentation, OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017.
[28] Chapter V, Transfer Pricing Documentation, OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2017.
[29] Section 959A TCA 1997.
[30] Revenue eBrief No. 62/12: Monitoring Compliance with Transfer Pricing rules contained in Part 35A TCA 1997

Four areas where guidance from Revenue would be beneficial are:

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. It would be helpful for Revenue to publish its view on this matter.

   Furthermore, 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,[31] which forms part of the three-tier documentation package for large multinational groups, is an automatic filing obligation for the group and its subsidiaries. We believe it would be appropriate for Ireland 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 the Revenue Commissioners.

We think a mandatory formal submission procedure for Master Files or Local Files would only increase the burden for both taxpayers and the Revenue. 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.

[31] Section 891H TCA 1997

Penalty Protection

In order to encourage compliance with transfer pricing documentation requirements, policymakers could consider introducing penalty protection provisions which operate to exempt a taxpayer from penalties or apply a lower penalty rate if a transfer pricing adjustment is made and sustained, notwithstanding the provision of documentation.

This would be in keeping with the approach put forward in the Action 13 Report, which suggests that the burden of proof can shift to the tax administration in circumstances where adequate documentation is provided on a timely basis. Taking this measure could act as incentive for transfer pricing documentation compliance.[32]

Institute Recommendations:

Ireland should adopt the OECD set of common criteria in Annex I and II of the 2017 Guidelines for Master and Local Files, as the standard for content for transfer pricing documentation.

In our view, the Master File requirement should not apply to multinational groups of a medium or smaller scale, as the Local File should contain sufficient information to evaluate the reasonableness of their transfer pricing policies

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

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

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

The timing for the preparation of transfer pricing documentation should remain in line with current practice; being available no later than when the Irish corporation tax return is due for the accounting period in which the transaction was reflected.

Penalty protection measures put forward in the OECD 2015 BEPS Action 13 Report could be considered to encourage transfer pricing documentation compliance.

[32] OECD (2015), Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris - http://dx.doi.org/10.1787/9789264241480-en, para. 43.

4.6 Application of transfer pricing rules to branches

- *Do you consider that the Authorised OECD Approach to attribution of branch profits would be an appropriate approach to adopt into Irish law?*
- *If the Authorised OECD Approach is adopted in Irish law, what documentation requirements should apply? Is there an alternative approach that should be considered in this context?*
- *Are there any industry or sector-specific considerations that should be borne in mind, particularly in relation to financial and insurance companies, in relation to branch profit attribution?*
- *Are there any special considerations required in respect of SMEs?*

The Authorised OECD Approach (AOA)[33] is a mechanism which has been developed by the OECD to apply the OECD Transfer Pricing Guidelines to determine the profits attributable to a branch. Section 25 TCA 1997 sets out the domestic rules for the taxation of branches in Ireland, however, the AOA is often followed in practice to attribute profits to branches in a tax treaty context.

In principle, we would consider it appropriate to adopt the AOA for the attribution of profits to branches into Irish law. Indeed, the new Controlled Foreign Company (CFC) rules introduced in Finance Act 2018 specifically define 'significant people functions'[34] by reference to the OECD 2010 Report. Applying OECD Guidelines to allocate profits to branches would provide Ireland with an internationally recognised framework for determining the amount of Irish profits attributable to a branch. It would enable Ireland to assert its taxing rights where the significant people functions relating to the branch's activities are located in Ireland.

However, the OECD has recognised that there are specific considerations for banking, global trading and insurance sectors in the context of attributing profits to branches. Accordingly, we believe further consultation with the financial services industry and other relevant sectors is necessary to ensure that there are no unintended consequences resulting from the proposed adoption of the AOA approach.

Furthermore, detailed Revenue guidance regarding the application of the AOA in an Irish context would be necessary to provide certainty for business, given the differing views that have been taken by tax authorities around the world regarding aspects of the AOA.

[33] OECD, 2010 Report on the Attribution of Profits to Permanent Establishments, 22 July 2010.
[34] Significant people functions is defined in section 835I TCA 1997 by reference to the 2010 OECD Report on the Attribution of Profits to Permanent Establishments.

Institute Recommendations:

In principle, we would consider it appropriate to adopt the Authorised OECD Approach (AOA) for the attribution of branch profits into Irish law. However, we believe more time is needed for further consultation with the financial services industry and other relevant sectors, to ensure that there are no unintended consequences resulting from the proposed adoption of the AOA approach.

Detailed Revenue guidance regarding the application of the AOA in an Irish context would be required to provide certainty for business, given the differing views that have been taken by tax authorities around the world regarding aspects of the AOA.