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Minister Paschal Donohoe T.D.
Department of Finance
Government Buildings
Upper Merrion Street
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27 June 2022

Pre-Finance Bill 2022 Submission

Dear Minister

We set out in the body of this submission a number of legislative changes for consideration in the drafting of Finance Bill 2022. Our recommendations are broadly grouped into the following three key areas:

1. Measures to support the growth of the indigenous sector.
2. Tax technical measures required to mitigate certain 'unintended consequences' arising from existing legislative provisions.
3. Simplification measures to provide certainty to taxpayers.

Joining the OECD Inclusive Framework agreement on a Two-Pillar Solution to address the tax challenges of digitalisation (the Two-Pillar Solution) reduces Ireland's scope to compete for foreign direct investment based on its corporation tax rate. Consequently, it is now more important than ever to consider other ways to improve the Irish tax system and enhance Ireland's attractiveness as a place to do business.

The need for a territorial system of taxation

We believe that simplifying the Irish corporation tax code and making it easier to administer would enhance Ireland's competitiveness. As set out in our response to the Department's recent consultation on a territorial system of taxation, the absence of a participation exemption puts Ireland at a disadvantage when competing for foreign direct investment with other OECD and EU countries that operate exemption systems.

Moving to a territorial system of taxation would reduce the administrative burden for Irish companies with international operations and simplify how double taxation relief would be

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available in Ireland on such foreign earnings. It would also bring Ireland's corporation tax code in line with most OECD countries and EU Member States.

Companies are currently evaluating the potential impact of the Two-Pillar Solution on their business and making decisions regarding how to structure their operations going forward. The existence of a participation exemption in the Irish corporation tax code will be a key factor for such companies when determining where to locate future investment and is already impacting decisions.

In addition, a participation exemption would encourage international growth and development by Irish headquartered multinationals. Such companies have made considerable investments in Ireland, provide high quality jobs and contribute significantly to the Irish economy.

With the proposed deadline for transposing the EU Minimum Tax Directive moving to 31 December 2023, we believe that there is now an opportunity for work to progress on implementing a participation exemption and foreign branch exemption in Finance Bill 2022 to ensure Ireland remains an attractive location for investment.

We do not believe this to be an overly complex task and we would be happy to engage with your officials in this regard. The formal stakeholder engagement process which you, Minister, committed to in Ireland's Corporation Tax Roadmap January 2021 Update[1] would be an ideal forum to progress this issue with business.

The need for simplification of the interest deductibility rules

Another area where simplification of the corporation tax code is required are the rules regarding the deductibility of interest. The Anti-Tax Avoidance Directive (ATAD) Interest Limitation Rule (ILR), introduced in Finance Act 2021, was layered on top of existing comprehensive interest deductibility provisions making the operation of the rules onerous and overly complex. Taking such an approach makes it difficult for businesses to operate in Ireland and comply with their tax obligations and has resulted in Ireland having one of the most complicated interest deductibility regimes within the EU.

We would strongly urge that the interest deductibility rules be reviewed with a view to ensuring Ireland's interest deductibility regime is simplified. We have set out in the body of this submission a summary of the interest deductibility provisions which we believe, following the adoption of the ATAD ILR into Irish law, are either no longer necessary or require simplification.

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[1] https://www.gov.ie/en/publication/678e5-irelands-corporation-tax-roadmap-january-2021-update/

We would welcome the opportunity to discuss the matters raised in this submission with you or your officials.

Yours sincerely

Karen Frawley
Institute President

Institute Recommendations for Finance Bill 2022

Our recommendations for Finance Bill 2022 are grouped into three broad areas below. We have provided further detailed analysis of each technical matter in the Appendix to this submission.

1. Measures to support the growth of the indigenous sector

1.1 Allow rental costs as qualifying expenditure for the R&D Tax Credit

We believe legislative clarification is necessary to ensure rent is a qualifying cost for the purpose of the Research and Development (R&D) Tax Credit. Rental costs are a substantial cost for most small and micro sized companies. The disallowance of rent as qualifying expenditure on R&D significantly diminishes the attractiveness of the R&D Tax Credit for such companies.

1.2 Enhance the Employment and Investment Incentive Scheme (EIIS)

The EIIS continues to be a very complex and a burdensome scheme to administer despite changes introduced in recent Finance Acts. We believe further amendments are necessary to ensure the EIIS can fulfil its policy objective of supporting the growth of indigenous business, which include:

- A carve-out from the connected party rule linked with a control test
- A streamlined EIIS administrative process for small and micro companies
- Removing the exclusion of holding company structures
- Recognising additional exit strategies for EIIS investors
- Committing appropriate and adequate resourcing to the administration of EIIS applications
- Applying more proportionate monetary sanctions for administrative errors or the late filing of a return
- Providing a 4-year holding period for all EIIS investments
- Allowing the offset of capital losses
- Broadening the scope of instruments through which start-up companies can raise funds using the EIIS by amending the definition of eligible shares so that it blends the characteristics of equity and loans.

1.3 Reduce the rate of interest charged on the late payment of tax

We strongly urge that the rates of statutory interest on underpaid tax are reviewed to ensure the rate imposed is more commensurate with the cost of borrowing. We firmly believe that the reduced 3% rate that will be imposed in Period 3 of the Debt Warehousing Scheme from the beginning of 2023 represents a fair and reasonable rate of interest which should apply to all underpayments of tax.

1.4 Insert a *bona fide* test in section 135 (3A) Taxes Consolidation Act (TCA) 1997 to provide certainty for taxpayers when selling shares in closely held companies

In the absence of a statutory *bona fide* test, uncertainty remains over transactions to which section 135 (3A) TCA 1997 applies and this is hindering the scaling up and passing on of businesses in the SME sector. In many cases, the ambiguity regarding the tax consequences means a business owner is unwilling to proceed with a proposed sale of their business.

In our view, inserting an exclusion for *bona fide* commercial transactions into section 135 TCA 1997 is essential, to provide the necessary level of certainty to taxpayers and their advisers, when implementing transactions involving the disposal of shares in a company with cash on its balance sheet.

2. Tax technical measures required to mitigate certain ‘unintended consequences’ arising from existing legislative provisions

2.1 Clarification on the meaning of the term ‘money’s held’ in section 79 TCA 1997

Section 79 TCA 1997 clarifies the tax treatment for trading companies of foreign-exchange gains and losses arising in the profit and loss account on any “relevant monetary item or relevant contract” and on any “relevant tax contract”. Such exchange gains and losses typically arise when the company undertakes trading transactions in currencies other than its functional currency for accounting purposes.

A ‘relevant monetary item’ for the purposes of section 79 is defined as ‘moneys held’ or payable by the company for the purposes of a trade carried on by it. Following discussions at TALC, we understand Revenue do not consider ‘moneys held’ to include foreign currency deposited with a bank or trade debtors. In our view, a legislative amendment is required to confirm that ‘money’s held’ for the purposes of section 79 includes both foreign currency deposited with a bank and trade debtors.

In the absence of such confirmation, significant practical difficulties will arise if foreign exchange gains and losses on bank accounts are required to be separated out from other assets and liabilities.

2.2 Top up payments of preliminary tax

The introduction of ATAD ILR into Irish law in 2021 necessitated amendments to sections 959AR and 959AS TCA 1997 relating to the operation of preliminary tax top up rules for accounting periods between 1 January 2022 and 31 December 2027.

However, the Finance Act 2021 amendments removed the ability for taxpayers to make preliminary tax top up payments for the same periods in respect of chargeable gains on the disposal of assets after the date for the payment of preliminary tax and for profits, gains, or losses accrued and not realised in the accounting period on financial assets or liabilities. This would appear to be an unintended consequence of the legislation.

We believe it is critical that the ability for a taxpayer to make a top up payment of preliminary tax in respect of above items for accounting periods between 1 January 2022 and 31 December 2027 is restored in Finance Bill 2022.

2.3 Define the term 'Member State' for the purpose of section 130 (2B) TCA 1997

Subsection 130 (2B) TCA 1997 refers to a company which is a resident of a 'Member State' or the UK. However, the term 'Member State' is not defined for the purposes of this subsection, although the term 'relevant Member State' is defined elsewhere in section 130. We believe clarification is required in legislation regarding the scope of the term Member State for the purpose of subsection 130 (2B).

2.4 Section 110 TCA 1997: restore the deduction for foreign withholding tax and provide clarity regarding *bona fide* CLO transactions

2.4.1 *Restore the deduction for foreign withholding tax*

Finance Act 2019 amended section 81 TCA 1997 to provide that in computing the amount of the profits or gains to be charged to tax under Case I or II of Schedule D, a tax deduction should not be allowed in respect of any 'taxes on income'. Clarification is required regarding the impact of this provision for section 110 companies.

As the profits or gains chargeable to tax at 25% under Case III by section 110 must be computed in accordance with Case I rules, it is unclear whether a tax

deduction is now available for foreign withholding taxes, assuming that these are taxes on income, suffered on the receipt of distributions or interest received by a section 110 company. To ensure that the policy intention of section 110 can continue to be achieved, a legislative amendment is required to confirm a section 110 company is entitled to a deduction for foreign withholding taxes.

2.4.2 *Clarity regarding bona fide CLO transactions*

Finance Act 2019 amended the definition of 'control' for the purposes of section 110 TCA 1997. An unintended consequence of the 2019 amendment to section 110(7)(b) was the extension of the test for control to include *bona fide* CLO transactions in certain circumstances. We believe legislative clarification is necessary to confirm the definition of control would not apply in circumstances where a section 110 qualifying company is set up for the purpose of executing a *bona fide* CLO, which complies with the Securitisation Regulation.[2]

2.5 Reconvene the Leasing Working Group

In early 2021, the Department of Finance established a working group to discuss long-standing tax technical issues arising in the area of leasing in order to identify matters that require legislative amendment and those which could be clarified via Revenue guidance.

Following an initial meeting of the working group, practitioners submitted a list of priority issues to the Department in April 2021 for their consideration which was supported by a number of technical papers prepared by the Institute. As it is now over a year since the initial meeting of the working group, we would urge that the working group be reconvened as a matter of urgency so that the issues raised can be progressed to provide the necessary certainty sought by taxpayers in the leasing sector.

2.6 Interaction of the close company surcharge with section 79C TCA 1997

Gains or losses arising from the disposal of foreign currency held in an Irish bank, by certain holding companies are chargeable to corporation tax as Schedule D Case IV income, rather than CGT, in accordance with section 79C TCA 1997. Such gains

[2] Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012 standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012

also fall within the scope of "investment income" for close company surcharge purposes. We believe this is an unintended consequence of the legislation.

We recommend that a new sub-section be inserted into section 79C as follows: *“Any income chargeable under Case IV of Schedule D by virtue of this section shall not be taken into account in computing ‘investment income’ for the purposes of Section 434*”.

2.7 Determination of company residence for tax purposes

Irish tax law requires consideration of whether a company is resident in a tax treaty country when determining eligibility for certain tax reliefs and exemptions. Often such provisions in TCA 1997 include conditions which require consideration of whether a company is "by virtue of the law of a relevant territory, resident for the purposes of tax in the relevant territory”. However, this condition can give rise to uncertainty as some countries, such as Hong Kong, do not have a domestic concept of tax residence.

We would suggest that wording is introduced into the TCA 1997 to clarify that a company that is resident in a territory for the purposes of a tax treaty with Ireland shall be considered to be so resident "by virtue of the law of" that territory.

2.8 Amend the tax treatment of employer contributions to a PRSA

Consideration should be given to equalising the tax treatment of employer contributions to a Personal Retirement Savings Account (PRSA), which are currently treated as a Benefit-in-Kind (BIK), with employer contributions to a group occupational pension scheme, which are exempt from a BIK charge. Such a change would make PRSAs a more viable alternative to one-member pension schemes, which have become unsustainable for many due to the increased compliance requirements imposed by the European Union (Occupational Pension Schemes) Regulations 2021, thus offering more market choice and lowered costs for employers.

3. Simplification measures to provide certainty to taxpayers

3.1 Simplify the rules regarding the deductibility of interest

The ATAD ILR[3], introduced in Finance Act 2021, was layered on top of existing comprehensive interest deductibility provisions, which has resulted in Ireland having

[3] Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

one of the most complicated interest deductibility regimes within the EU. The complexity of the rules makes it difficult and costly for businesses to comply with their tax obligations.

We would strongly urge the Department to carry out a review of the interest deductibility provisions in the Irish tax code to modernise it and reduce its complexity, so the rules can compare favourably with regimes in other jurisdictions competing with Ireland for investment.

3.2 Repeal section 757 TCA 1997: Charges on capital sums received for sale of patent rights

The differing tax treatment that applies to proceeds arising from the disposal of patents and patent rights continues to create uncertainty for business. Under existing legislation, any gain arising on the disposal of a patent is treated as a disposal of a capital asset and is subject to CGT, while any gain arising on the disposal of patent rights is treated as Case IV income under section 757 TCA 1997 and, as such, is subject to corporation tax of 25%.

As patent rights are not within the charge to CGT, this means that there is no group relief mechanism on the transfer of patent rights within a group. In our view section 757 should be repealed and patent rights should be treated akin to any other chargeable asset, subject to CGT.

3.3 Simplify the Offshore Funds Regime

Determining the correct tax treatment of income and gains arising from foreign investments can be very complex. Performing the requisite analysis to determine whether the investment is in an offshore fund and the relevant tax treatment is costly and time consuming and the analysis may often be incomplete due to the lack of full information on the investment products. Individual products are continually developed so there is no set list of products and their treatment for taxpayers to review.

Revenue has endeavoured to provide guidance and decision trees to assist taxpayers and professional advisers to determine the tax treatment based on a fund’s characteristics, but the usefulness of this approach is limited. There is no guarantee that if a taxpayer uses their best efforts to determine the correct treatment that interest and penalties will not apply if they get it wrong. We believe that the Offshore Funds Regime should be overhauled to simplify the regime and support tax compliance.

3.4 Align the basis of assessment for proprietary directors with PAYE income with employees

Finance Act 2017 amended the basis for assessing income tax on PAYE income (Schedule E income) so that such emoluments are assessed to tax on the receipts basis rather than the earnings basis. However, proprietary directors continue to be assessed to tax on the earnings basis on their PAYE income.

We believe that consideration should be given to aligning the basis of assessment for proprietary directors with employees, so that both cohorts of taxpayers are assessed to tax on Schedule E emoluments on the receipts basis.

3.5 Amend the VAT 'use and enjoyment' provisions post-Brexit

Following the UK's exit from the EU, the potential for transactions to come within the scope of both Irish and UK VAT rules has increased significantly. There are two areas where we believe that the VAT rules should be reviewed in order to minimise the risk of double taxation and reduce the administrative burden for businesses.

Firstly, we believe consideration should be given to amending section 35 (2) Value-Added Tax Consolidation Act (VATCA) 2010, so that it applies to the hiring out of movable goods in addition to means of transport.

We also consider that it would be reasonable to introduce into that subsection a *de minimis* limit of 30 days so that a taxpayer would only be required to switch VAT accounting jurisdiction after a means of transport has moved jurisdiction for a period in excess of the *de minimis*.

3.6 Streamline the tax reporting and collection process for non-resident landlords

The tax collection and reporting process of non-resident landlords needs to be modernised in line with the ongoing moves to digitalisation in tax collection and administration. Where a non-resident landlord is in receipt of Irish rental income they must appoint a "collection agent" (such as a property management company, letting agent or family friend) and the non-resident landlord is chargeable to income tax in the name of that collection agent under section 1034 TCA 1997. This presents a range of practical issues, including difficulties in completing the return by the collection agent as they do not have the necessary information on the landlord's other income, and the submission of multiple returns and duplicate claims in respect of a single taxpayer if there are multiple collection agents.

We believe that the current process, underpinned by the legislation, is cumbersome and adds cost and unnecessary complexity to the tax compliance process. In our view, a more streamlined approach to collecting information and tax relating to non-resident landlords should be adopted.

APPENDIX I

1. Measures to support the growth of the indigenous sector

1.1 Allow rental costs as qualifying expenditure for the R&D Tax Credit

The disallowance of rent as qualifying expenditure on R&D substantially reduces the attractiveness of the R&D Tax Credit for SMEs. In July 2020, Revenue updated their guidance on section 766(1) TCA 1997 on the circumstances in which rental costs can be considered qualifying expenditure for the purpose of the R&D Tax Credit.

Notwithstanding representations from practitioners via TALC[4], Revenue confirmed their view in guidance[5] that in most cases rent does not qualify as R&D expenditure but there may be scenarios where rent can qualify where the expenditure is incurred wholly and exclusively in the carrying on of the R&D activities.

Revenue's guidance provides examples of rent incurred on a specialised laboratory or a clean room in order to advance R&D activities which it states may be qualifying expenditure but the rent of an office space in which R&D activities are carried on is not qualifying expenditure as the office is "*the setting in which R&D happens and does not itself perform a key function in relation to the R&D process".* We believe Revenue's guidance significantly narrows the circumstances where rent may be included as qualifying expenditure on R&D and in our view is contrary to the policy intention of the R&D Tax Credit.

We consider Revenue's interpretation also creates a clear inequity in favour of companies that have the available resources to incur expenditure on the construction or refurbishment of a building or structure for R&D purposes rather than incur a rental cost. Section 766A TCA 1997 provides that where a company acquires a building and incurs expenditure on the refurbishment of the building for R&D purposes, these costs, subject to meeting specific conditions, qualify for the R&D Tax Credit. However, based on Revenue's updated guidance, renting the same refurbished R&D building may not qualify for the R&D Tax Credit even if the same R&D activity is being undertaken in the building.

As rental costs are a substantial cost for most small and micro sized companies, the disallowance of rent as qualifying expenditure on R&D significantly diminishes the attractiveness of the R&D Tax Credit for such companies. In our view, legislative

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[4] https://taxinstitute.ie/wp-content/uploads/2021/06/2020-11-16-ITI-Submission-to-Revenue-on-treatment-of-rent-in-Research-and-Development-TDM.pdf

[5] Research and Development (R&D) Tax Credit, Part 29-02-03,Tax and Duty Manual, April 2021

clarification is now necessary to ensure rent is a qualifying cost for the purpose of the R&D Tax Credit so the credit can continue to encourage investment in innovation by Irish business.

1.2 Enhance the Employment and Investment Incentive Scheme (EIIS)

The EIIS is a vital source of funding for early stage and small businesses that often have limited financing options available to them. However, in many cases the rules of the EIIS do not reflect commercial investment norms. Our members continue to report of instances where the scheme has hampered a company's ability to grow and expand, or accelerate their ability to do so, which is contrary to the objective of the scheme.

The Institute has responded to various public consultations carried out by the Department of Finance on the EIIS, most recently in February 2021[6], and several of the recommendations made in those submissions for the improvement of the scheme remain valid. Whilst the changes introduced in Finance Acts 2018, 2019 and 2021 have, for the most part, enhanced the scheme, the EIIS continues to be very complex and burdensome to administer. Further amendments are necessary to ensure the EIIS can fulfil its policy objective of supporting the growth of indigenous business. These include:

- A carve-out from the connected party rule linked with a control test
- A streamlined EIIS administrative process for small and micro companies
- Remove the exclusion of holding company structures
- Recognise additional exit strategies for EIIS investors
- Commit appropriate and adequate resourcing to the administration of EIIS applications
- Apply more proportionate monetary sanctions for administrative errors or the late filing of a return
- Provide a 4-year holding period for all EIIS investments
- Allow the offset of capital losses.

One of the most frequent issues which is raised by our members regarding the EIIS is the restrictive nature of the connected party rules. Indeed, the feedback we have received is that the 'connected party rule' coupled with the narrow scope of the definition of 'eligible shares' for the purposes of EIIS relief is significantly hampering the effectiveness of the EIIS as a source of finance for early stage and small businesses.

[6] https://taxinstitute.ie/wp-content/uploads/2021/02/2021-02-12-ITI-Response-to-the-Public-Concultation-on-EII.pdf

The connected party rule was initially introduced into EIIS legislation in November 2017 in response to concerns raised by the European Commission regarding founders availing of the relief. The EIIS does not permit the investor or their associate (including a relative) to hold any shares in the company before making the EIIS investment. An individual is connected with a company if they or an associate is a partner, director or employee of the company or any company in the RICT Group.[7]

We have previously highlighted that the connected party rule presumes that the potential pool of investor money for high-risk early-stage companies in Ireland is so considerable that a company can raise funds from an entirely different cohort of investors on each round. This is not the case in the Irish market. It also does not recognise the commercial reality that a company will seek a second round and future funding from existing investors. Investors are more likely to follow their money, which reduces the time and cost of raising capital.

Finance Act 2021 extended the EIIS to a wider range of funds, including an Investment Limited Partnership (ILP). While we welcomed this move, the operation of the connected party rule is significantly hindering the raising of EIIS funds through an ILP.

This is because all of the investors in the ILP are considered partners and consequently are viewed as connected with each other. Therefore, an investment in the eligible shares of a qualifying company by the ILP on behalf of the partners may fall foul of the connected party rules (resulting in the investment being ineligible for EIIS relief for all of the partners) simply by reason of one of those partners having an earlier non-EIIS investment in the company.

The operation of the connected party rules is also restricting the fundraising options available to companies. A company, which previously raised funds through the EIIS scheme, may choose for commercial reasons to raise funds using equity type instruments which do not come within the definition of ‘eligible shares’ for the purposes of EIIS. However, the connected party rules mean that the original EIIS investors in those circumstances are faced with the option of either following their money (but losing EIIS relief) or opting out of the investment round in order to preserve their EIIS relief.

The use of equity type instruments such as Convertible Loan Notes (CLN), Warrants, Advance Investment Agreements and Simple Agreement for Future Equity (SAFE) is common in the funding of start-ups and early-stage companies. These instruments each involve an upfront investment, giving an entitlement to acquire equity at a

[7] Sections 500 and 501 TCA 1997 set out the connected party rules.

discounted price based on a future valuation of the company. The use of such instruments is primarily driven by uncertainty in relation to the valuation of a company at the time of the investment, recognition of the risks being undertaken by the investor, and the desire to ensure there is no dilution of that investor when subsequent investments are made.

The characteristics of the various equity type instruments can vary. For instance, with a SAFE instrument the investor gives the money in exchange for future equity at a certain date. The idea for the founders is that the valuation of the business grows and when the equity is provided they are not diluted as much. The investor gets a discount on the future valuation at the point the equity is issued.

Example: *Mary invests €100k in X Ltd. X Ltd issues a SAFE for equity to be issued in 18 months. After the 18 months the business has grown from €2m to €10m because X Ltd used the funds to finalise software and land some big sales contracts. Mary has a 30% discount as part of her SAFE agreement, so her equity is provided on a €7m valuation (as opposed to €10m). There is a €5m benefit in valuation for the founders for dilution purposes.*

In our view, consideration should be given to amending the definition of eligible shares so that it blends some of the characteristics of equity and loans. This would widen the scope of instruments through which start-up companies can raise funds using the EIIS. It would also mean that existing EIIS investors would have the option to follow their money where a start-up company chooses to use equity-type instruments, such as CLN, when raising funds.

1.3 Reduce the rate of interest charged on the late payment of tax

The Debt Warehousing Scheme has proven to be a critical support for businesses struggling to meet their tax payment obligations because of the impact of COVID-19 public health restrictions. Now that the Debt Warehousing Scheme will soon move into its last stage, Period 3 from 1 January next year, it is timely to consider the fairness of the higher interest rates imposed on the late payment of tax.

In the UK, the interest rate for late payment of tax will soon increase to 3.75%[8] (from 3.5%), tracked at 2.5% above the current Bank of England base rate. The current European Central Bank (ECB) rates are minus 0.50% for deposits and 0.25% for marginal lending. It is our view that statutory interest rates of between 8% and 10% per annum cannot be justified by reference to the time value of money.

[8] From 5 July 2022.

It is noteworthy that in a recent case in Germany, the Federal Constitutional Court (Bundesverfassungsgericht) ruled that Germany's annual statutory rate of interest of 6% on late payment of taxes, which had been in force for about 50 years, was unconstitutional given the long-established prevailing low rate of interest.[9] In its decision, the Court stipulated that the German legislature must make new rules by 31 July 2022. As a result, the German Federal Ministry of Finance has now published draft legislation to lower the interest rate on underpaid tax from 6% to 1.8% per annum (0.15% per month). The new interest rate is based on the Deutsche Bundesbank's current base rate (minus 0.88% per annum) with a mark-up of approximately 2.7 percentage points. The interest rate is subject to review every three years.

We strongly urge that the rates of statutory interest on underpaid tax are reviewed to ensure the rate imposed is more commensurate with the cost of borrowing. We firmly believe that the reduced 3% rate that will be imposed in Period 3 of the Debt Warehousing Scheme from the beginning of 2023 represents a fair and reasonable rate of interest which should apply to all underpayments of tax.

Of course, any reduced rate of interest must recompense the Exchequer and act as a disincentive to late payment. With the recent announcement that interest rates on lending will increase in the near future, tracking the interest rate which applies to the late payment of tax to prevailing ECB market rates, with an opportunity for the rate to be adjusted on a periodic basis, would ensure that it reflects the actual cost to the Exchequer.

1.4 Insert a bona fide test in section 135 (3A) TCA 1997 to provide certainty for taxpayers when selling shares in closely held companies

In the absence of a statutory *bona fide* test, uncertainty remains over transactions to which section 135 (3A) TCA 1997 applies, which continues to hinder the scaling up and passing on of businesses in the SME sector.

The effect of subsection (3A) is that if Revenue take the view that a company has retained profits in excess of the company's commercial needs, income tax treatment rather than CGT treatment will apply to the selling shareholders. This is notwithstanding that there are two specific provisions, the close company surcharge and the professional services company surcharge, which are intended to counteract

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[9] BVerfG, decision of the First Senate of July 8, 2021, - 1 BvR 2237/14 -, paras. 1-264, http://www.bverfg.de/e/rs20210708_1bvr223714.html

the retention of profits in excess of a company's commercial needs in a close company.

Unlike other anti-avoidance provisions in Irish tax legislation, section 135 TCA 1997 does not include a *bona fide* test. Although Revenue guidance states that the provision does not apply to *bona fide* financing arrangements entered into by a purchaser relating to the acquisition of shares, this is not expressed in legislation. Therefore, a taxpayer cannot rely on this guidance in the event of the matter being disputed and subject to an appeal. Furthermore, as it is an anti-avoidance section, Revenue will not provide an advance opinion as to the application or otherwise of section 135(3A) to any given transaction.

Certainty regarding the net proceeds after tax available following any sale is a key deciding factor for business owners on whether they can afford to exit their business. In our view, inserting an exclusion for *bona fide* commercial transactions into section 135 TCA 1997 is essential, to provide the necessary level of certainty to taxpayers and their advisers, when implementing transactions involving the disposal of shares in a company with cash on its balance sheet.

2. Tax technical measures required to mitigate certain 'unintended consequences' arising from existing legislative provisions

2.1 Clarification on the meaning of the term 'money's held' in section 79 TCA 1997

Section 79 TCA 1997 clarifies the tax treatment for trading companies of foreign-exchange gains and losses arising in the profit and loss account on any "relevant monetary item or relevant contract" and on any "relevant tax contract". Such exchange gains and losses typically arise when the company undertakes trading transactions in currencies other than its functional currency for accounting purposes. Under section 79, such exchange gains and losses are brought into the computation of the company's Case I trading income for corporation tax purposes, and hence taxed or allowed at the rate of 12.5%, as and when they are properly credited or debited to the profit and loss account of the company.

A 'relevant monetary item' for the purposes of section 79 is defined as 'moneys held' or payable by the company for the purposes of a trade carried on by it. Revenue recently confirmed at TALC that they do not consider the term 'moneys held' to include foreign currency deposited with a bank or trade debtors. It is our firm view that such an interpretation of 'money's held' is contrary to settled case law in this area.

In the event that foreign currency bank accounts are not regarded as being captured by section 79 TCA 1997, this would lead to significant practical difficulties which would

require foreign exchange gains and losses on bank accounts to be separated out from other assets and liabilities. It would be extremely difficult for businesses to track the position on a yearly basis. In our view, legislative confirmation is required that 'money's held' for the purposes of section 79 includes both foreign currency deposited in a bank account and trade debtors.

2.2 Top up payments of preliminary tax

The operation of the preliminary tax top up rules for accounting periods between 1 January 2022 and 31 December 2027 were amended by Finance Act 2021 to allow for a top up payment to be made within a period of 6 months after year end to cater for the application of the ATAD ILR.

However, the Finance Act 2021 amendments to section 959AR and section 959AS TCA 1997 also simultaneously removed the ability for taxpayers to make a top up payment of preliminary tax for accounting periods between 1 January 2022 and 31 December 2027 in respect of:

a) chargeable gains on the disposal of assets after the date for the payment of preliminary tax; or
b) profits, gains, or losses accrued and not realised in the accounting period on financial assets or liabilities.

This would appear to be an unintended consequence. It is an imperative for taxpayers that the ability to make a top up payment of preliminary tax in respect of items (a) and (b) for accounting periods between 1 January 2022 and 31 December 2027 is restored.

2.3 Definition of 'Member State' for the purpose of section 130 (2B) TCA 1997

Subsection 130 (2B) TCA 1997 refers to a company which is a resident of a 'Member State' or the UK. The term 'Member State' is not defined for the purposes of this subsection although the term 'relevant Member State' is defined elsewhere in section 130.

Notably, prior to the introduction of the Withdrawal of the United Kingdom from the European Union (Consequential Provisions) Act 2019, the subsection referred to a 'Member State of the European Communities'. We believe clarification is required in legislation regarding the scope of the term Member State for the purpose of subsection 130(2B) TCA 1997.

2.4 Section 110 TCA 1997: restore the deduction for foreign withholding tax and provide clarity regarding bona fide CLO transactions

Restore the deduction for foreign withholding tax

The policy intention for the introduction of section 110 TCA 1997 was to promote securitisation for the financial sector operating in Ireland. It was designed as a tax neutral regime for securitisation transactions. Where a section 110 company suffers foreign tax on their income, this can impact on their tax neutrality if double tax relief is not available.

Finance Act 2019 amended section 81 TCA 1997 to provide that in computing the amount of the profits or gains to be charged to tax under Case I or II of Schedule D, a tax deduction should not be allowed in respect of any 'taxes on income'. Whilst we understand the policy intention of this amendment for companies which are carrying on a Case I trade in Ireland, this provision gives rise to unintended consequences for section 110 companies.

As the profits or gains chargeable to tax at 25% under Case III by section 110 are computed in accordance with Case I rules, it is unclear whether a tax deduction is now available for foreign taxes, assuming that these are taxes on income, suffered on the receipt of distributions or interest received by a section 110 company.

An anomaly could potentially arise if both a deduction was not allowed for foreign taxes suffered and where the tax credit available under Schedule 24 was computed in line with that of a trading company such that the income which was not received by a section 110 company (i.e., the foreign withholding tax) would be subject to tax at a rate of 25%.

In addition, because of the corporate tax liability in the first year of the foreign tax being suffered, the amount of the liability cannot be paid out as interest on the profit participating note (PPN) in the second year. Therefore, a tax deduction cannot be claimed for this amount of interest on the PPN in the second year, resulting in a corporation tax liability in year 2 that is based on the corporation tax charge in year 1.

This issue will be compounded on a yearly basis, with a resulting tax liability yearly based on the corporation tax charge in the year before. Such an outcome would likely place Ireland at a disadvantage relative to competitor jurisdictions. It would also appear to be at odds with the intended policy objective of section 110.

To ensure that the policy objective of section 110 can continue to be achieved, legislative clarification is required to ensure a section 110 company is entitled to a deduction for foreign withholding taxes.

Provide clarity regarding bona fide CLO transactions

Finance Act 2019 amended the definition of 'control' for the purposes of section 110 TCA 1997. A consequence of the amendment to section 110 (7) (b) was the extension of the test for control to include *bona fide* CLO transactions in certain circumstances. We understand from discussions with Revenue at TALC that this was not the policy objective.

Legislative clarification is now required to confirm that the Finance Act 2019 amendments to the definition of control would not apply in circumstances where a section 110 company is set up for the purpose of executing a *bona fide* CLO which complies with the Securitisation Regulation.[10]

2.5 Reconvene the Leasing Working Group

A working group was formed by the Department of Finance in early 2021 to discuss technical issues arising in the area of leasing in order to identify matters that require legislative amendment and those which could be clarified via Revenue guidance.

Following the initial meeting of the working group, a list of priority issues was submitted by practitioners to the Department in April 2021, together with technical papers prepared by the Institute on three priority issues, which were submitted in May 2021.

As it is now over a year since the initial meeting of the working group, we would urge that the working group be reconvened as a matter of urgency so that the issues raised can be progressed to provide the necessary certainty sought by taxpayers in the leasing sector.

2.6 Interaction of the close company surcharge with section 79C TCA 1997

Gains or losses arising from the disposal of foreign currency held in an Irish bank, by certain holding companies, are chargeable to corporation tax as Schedule D Case IV income, rather than CGT, in accordance with section 79C TCA 1997. However, section 79C provides that the amount of any currency gain brought into the charge to

[10] Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012

corporation tax is increased, so that the tax payable equates to the tax that would have been payable if CGT had applied. This is to ensure that there is no loss to the Exchequer.

Foreign exchange gains taxable under section 79C fall within the scope of "investment income" for close company surcharge purposes. We believe that was an unintended consequence of the legislation.

To address this unintended consequence, we recommend that a new subsection be inserted into section 79C as follows: *“Any income chargeable under Case IV of Schedule D by virtue of this section shall not be taken into account in computing ‘investment income’ for the purposes of Section 434”*

2.7 Determination of company residence for tax purposes

When determining eligibility for certain tax reliefs and exemptions, Irish tax law requires consideration of whether a company is resident in a tax treaty country. For example, section 626B TCA 1997 provides for an exemption from tax on certain capital gains from the disposal of holdings in subsidiaries.

One of the conditions of section 626B requires consideration of whether a company is "by virtue of the law of a relevant territory, resident for the purposes of tax in the relevant territory”.

However, this condition can give rise to uncertainty as some countries, such as Hong Kong, do not have a domestic concept of tax residence. There is a well-reasoned view that the provisions of a double taxation agreement (DTA) form part of the law of the contracting states, with the result that a company that is resident in a territory under the terms of a DTA shall be considered resident "by virtue of the law of" that territory.

This approach would appear to be accepted by Revenue in principle. For example, Revenue’s guidance on Controlled Foreign Company (CFC) rules[11] clarifies that for the purposes of the rules if a company is regarded as resident in a territory under the terms of a double tax treaty, in accordance with section 826(1) TCA 1997 then, the company will be regarded as resident in that territory.

We would recommend wording could be introduced into the TCA 1997 to clarify that a company that is resident in a territory for the purposes of a DTA with Ireland shall be considered to be so resident "by virtue of the law of" that territory.

[11] Tax and Duty Manual 36b-01-01

2.8 Amend the tax treatment of employer contributions to a PRSA

The European Union (Occupational Pension Schemes) Regulations 2021 were signed into law on 22 April 2021. The Regulations transpose the requirements of the EU IORP II Directive into Irish law. Although one-member occupational pension arrangements and employer schemes have received some derogations under the Regulations until April 2026, there is a significant increase in governance and compliance requirements and increased restrictions from an investment perspective, making the use of one-member schemes expensive and unsustainable for many.

A potential alternative to a one-member scheme is a Personal Retirement Savings Account (PRSA). However, the tax treatment of employer contributions to a PRSA is preventing PRSAs from being a viable option in many cases.

Employer contributions to a PRSA are regarded as a Benefit in Kind (BIK) and therefore are taken into account when calculating the maximum pension contributions that can be made to a PRSA in a tax year as set out in the table below.

Age	Age related %	Earnings Limit	Maximum Contributions
Under 30	15%	€115,000	€17,250
Age 30 – 39	20%	€115,000	€23,000
Age 40 - 49	25%	€115,000	€28,750
Age 50 - 54	30%	€115,000	€34,500
Age 55 - 59	35%	€115,000	€40,250
Age 60 or over	40%	€115,000	€46,000

As the employer contribution is aggregated with the employee contributions to the PRSA to determine the total amount of the contributions to a PRSA, this reduces the scope for contributions by an employee. In contrast, the employer contribution to an occupational pension scheme is not treated as a BIK and is ignored when calculating what contributions can be made by an employee.

In our view, employer contributions to a PRSA should not be regarded as a BIK as this creates an inequity between the treatment of employer contributions to an occupational pension scheme and a PRSA and reduces the scope for contributions to be made by an employee.

Another related issue is the difference in the tax treatment for the employer of the employer contributions to an occupational pension scheme and PRSA. Ordinary contributions to an occupational pension scheme are deductible on a paid basis

against Case I/II profits for the employer and special contributions by the employer are deductible against Case I/II profits, but are spread over a number of years, subject to a maximum of five years.

In contrast, the maximum employer contributions to a PRSA for which a deduction is available against Case I/II profits is subject to the age related limit as outlined in the above table. However, as this limit includes both employer and employee contributions/additional voluntary contributions (AVCs), the potential for tax relief on employer contributions to a PRSA is very limited making a PRSA a less attractive option.

We consider that the same tax treatment for employer contributions to an occupational pension scheme should equally apply to a PRSA. Such an approach would mean that a PRSA would be a viable alternative to a group occupational pension scheme, thus providing increased market choice and significantly lower costs for employers.

3. Simplification measures to provide certainty to taxpayers

3.1 Simplify the rules regarding the deductibility of interest

The ATAD Interest Limitation Rule (ILR) introduced in Finance Act 2021 was layered on top of existing comprehensive interest deductibility provisions making the operation of the rules onerous and overly complex. This makes it difficult and costly for businesses to operate in Ireland and comply with their tax obligations and has resulted in Ireland having one of the most complicated interest deductibility regimes within the EU.

We would strongly urge the Department to carry out a review of the interest deductibility rules with a view to ensuring that Ireland's interest deductibility regime is modernised and less complex and can compare favourably with competitor jurisdictions. We recommend that the reformed interest deductibility rules should reflect a broad base for interest deduction against both trading and non-trading income, using the protection of the new 30% EBITDA ratio rule against base erosion risks and removing the existing interest restrictions within sections 247 and 249 TCA 1997.

In our view, retaining two separate interest limitation regimes on a permanent basis is likely to increase the cost of borrowing for Irish businesses. By comparison, both Germany and the UK operate straightforward EBITDA-based interest limitation regimes.

As Ireland has different rules for trading and non-trading activities, a legislative basis for claiming a tax deduction for interest arising in a non-trading context would need to be established within the Irish corporation tax code, in conjunction with a full removal of section 247 TCA 1997, by incorporating a general test for permitting a deduction for interest expense that is incurred for a business or commercial purpose, similar to the German regime.

In our response to the Department of Finance's consultations on the implementation of the ATAD ILR in 2021, we identified the interest deductibility provisions which we believe, following the adoption of the ATAD ILR into Irish law, are either no longer required or should be amended. We have summarised these suggested legislative amendments in Appendix II of this submission.

3.2 Repeal of section 757 TCA 1997: Charges on capital sums received for sale of patent rights

The differing tax treatment that applies to proceeds arising from the disposal of patents and patent rights continues to create uncertainty for business.

Any gain arising on the disposal of a patent is treated as a disposal of a capital asset and is subject to CGT. However, any gain arising on the disposal of patent rights is treated as Case IV income under section 757 TCA 1997 and, as such, is subject to corporation tax of 25%. As patent rights are not within the charge to CGT, this means that there is no group relief mechanism on the transfer of patent rights within a group.

Section 757 was introduced in 1967 to ensure that receipts arising on the disposal of certain patent rights could be earned tax-free. CGT legislation was introduced in 1975, thus eliminating the necessity for the standalone provisions in section 757. In our view, section 757 should be repealed and patent rights should be treated similar to any other chargeable asset, subject to CGT.

3.3 Simplify the Offshore Funds Regime

The investment market has expanded exponentially over recent years with a wide array of investment products and platforms now available to investors. Diverse and international investment portfolios, once the preserve of high earners engaging professional brokers, are now accessible to a much broader cohort of taxpayers.

However, determining the correct tax treatment of income and gains arising from foreign investments can be very complex. Investors must consider whether the investment falls within Ireland's Offshore Funds regime (outlined in Chapters 2, 3 and 4 of Part 27 TCA 1997). Performing the requisite analysis to determine whether the

investment is in an offshore fund and the relevant tax treatment is costly and time consuming and the analysis may often be incomplete due to the lack of full information on the investment products. Most private investors do not have the skillset or access to the tools required to ascertain the correct tax treatment.

Individual products are continually developed so there is no set list of products and their treatment for taxpayers to review. Revenue has endeavoured to provide guidance and decision trees to assist taxpayers and professional advisers to determine the tax treatment based on a fund's characteristics, but the usefulness of this approach is limited. There is no guarantee that if a taxpayer uses their best efforts to determine the correct treatment that interest and penalties will not apply if they get it wrong.

Equally, Revenue can change its views on the tax treatment of certain types of investment. For example, in September 2021 updated Revenue guidance was published on the tax treatment of Exchange Traded Funds (ETFs), requiring taxpayers to consider whether such investments could come within the Offshore Funds Regime which up to now was not required. Previous guidance from Revenue had confirmed that investments in ETFs domiciled in the USA, the EEA or in an OECD Member State with which Ireland has a double taxation treaty, follows the treatment that would apply to share investments generally.

We believe that the Offshore Funds Regime should be overhauled to simplify the regime and support tax compliance.

3.4 Align the basis of assessment for proprietary directors with PAYE income with employees

Finance Act 2017 amended the basis for assessing income tax on PAYE income (Schedule E income) so that such emoluments are assessed to tax by reference to the year in which they are paid by an employer to the employee ("the receipts basis")

Previously the statutory basis for taxing emoluments was by reference to the year in which the emoluments were earned by the employee ("the earnings basis"). This amendment was made in preparation for the introduction of PAYE modernisation from 1 January 2019 to align the practical operation of PAYE with the statutory basis for taxing employees. However, the basis of assessment for proprietary directors' emoluments was not altered even though proprietary directors are liable to PAYE on their emoluments.

Proprietary directors continue to be assessed to tax on the earnings basis on their PAYE income and this adds complexity in completing their income tax returns where

income is received in a different year to which it is earned. For example, directors' fees or a bonus may be paid to a director after the financial year end of their employer company but paid in respect of that financial year. Such payments are liable to PAYE through the payroll and included on a payroll submission to Revenue when they are paid to the director but are assessable to income tax for the year in which the fees or bonus was earned.

Prior to the introduction of PAYE modernisation, a Supplementary P35 (PAYE End of Year Return) was typically filed that would include details of the income and related tax deducted which was earned for a prior year but paid out in a subsequent tax year to proprietary directors, so the pay and tax could be allocated to the correct year in assessing the director to income tax.

However, PAYE modernisation removed the P35 process. Revenue cannot identify from payroll submissions the amount of pay and tax deducted in one year that relates to a prior year to be included in a proprietary director's prior year income tax return. Therefore, a proprietary director's income tax return on ROS cannot be accurately pre-populated by Revenue with their Schedule E income. Instead, the director must provide a detailed breakdown of pay and a "true estimate" of the tax and USC deducted through the payroll which relates to the income assessed under the earnings basis.

The rationale for maintaining a distinction between the treatment of proprietary directors and employees is unclear. Proprietary directors' emoluments are subject to PAYE in the same manner as emoluments paid to employees. In the vast majority of cases, PAYE will have been withheld and paid on proprietary directors' emoluments, prior to the filing of their income tax returns. So, in general, the information provided on their emoluments in the tax return is included to meet a reporting requirement.

Revenue will already have received details of the emoluments and tax deducted through the payroll submissions, as the employer company must account for the payroll taxes to Revenue within six months of the company's year-end and the director will not obtain credit for tax deducted from their emoluments unless it has been paid to Revenue (sections 996 and 997A TCA 1997).

The company's corporation tax return, filed within nine months of accounting period end, will also include information on directors' emoluments which can be used as a cross checking mechanism by Revenue on directors' emoluments, if considered necessary.

We believe that the distinction between proprietary directors and employees should be removed to simplify tax compliance. Consideration should be given to aligning the

basis of assessment for proprietary directors with employees so that both cohorts of taxpayers are assessed to tax on Schedule E emoluments on the receipts basis.

3.5 Amend the VAT ‘use and enjoyment’ provisions post-Brexit

Following the UK’s exit from the EU, the potential for transactions to come within the scope of both Irish and UK VAT rules has increased significantly. There are two areas where we believe that the VAT rules should be reviewed to minimise the risk of double taxation and reduce the administrative burden for businesses.

Hiring out of movable goods

If an Irish lessor leases movable goods to an Irish VAT registered and Irish established lessee, Irish VAT applies as the lessee is established in Ireland. If the lessee moves the leased assets to the UK during the period of the lease, as the UK is no longer a member of the EU, UK VAT also arises on the lease rentals. UK VAT rules require the Irish lessor to account for VAT on the portion of the lease used and enjoyed in the UK. For lessees with full VAT recovery entitlement, the Irish and UK VAT should typically be recoverable, however the process is administratively burdensome.

In contrast, to the position for movable goods, section 35(2) VATCA 2010 provides that where a supply of services consists of the hiring out of a means of transport and those services are used and enjoyed outside of the Community, the place of supply of those services is treated as outside of the Community.

In an effort to avoid the risk of double taxation and reduce the administrative burden for businesses, we believe that consideration should be given to amending section 35(2) VATCA 2010 so that it applies to the hiring out of movable goods in addition to means of transport.

Means of Transport

Where a service consists of the hiring out of a means of transport it may be challenging to correctly determine where the assets are used and enjoyed if they are regularly moved across the border to Northern Ireland. Under the legislation, the lease rentals must be apportioned between effective use and enjoyment in the State (subject to Irish VAT) and effective use and enjoyment in the UK (subject to UK VAT). In addition to the high administrative burden, this approach can present difficulties for taxpayers in accurately determining the correct apportionment.

We consider that it would be reasonable to introduce a *de minimis* limit of 30 days, so that a taxpayer would only be required to switch VAT accounting jurisdiction after the means of transport has moved jurisdiction for a period of time in excess of the *de minimis*.

3.6 Streamline the tax reporting and collection process for non-resident landlords

The Institute's Pre Finance Bill Submissions for 2020 and 2021 highlighted the need to simplify the tax collection and reporting process for non-resident landlords in line with the ongoing digitalisation of tax collection and administration. Under the current tax regime for non-resident landlords, unless a tenant is paying the rent directly to the non-resident landlord, withholding tax at 20% and paying this tax to Revenue[12], a non-resident landlord is required to appoint a "Collection Agent" and the non-resident landlord is chargeable to income tax in the name of this Collection Agent[13].

The current legislative requirements present a range of practical challenges, including difficulties in completing the return by the Collection Agent, as they do not have the necessary information on the landlord's other income, and the submission of multiple returns and duplicate claims in respect of a single taxpayer, if there are multiple Collection Agents.

The current legislative rules are cumbersome, which adds cost and unnecessary complexity to the tax compliance process. In our view, a more streamlined approach to collecting information and tax relating to non-resident landlords should be adopted. For example, we proposed in our previous submissions adapting the current Third-Party Return for letting agents/property managers (provided for under section 888 TCA 1997) to capture information relating to non-resident landlords, perhaps, through a non-resident landlord version of the form. The letting/property agent could submit a report to Revenue electronically at set intervals, providing details of the non-resident landlords for whom they have collected rents. The taxpayer should then be able to submit an income tax return after the end of each year, as part of the normal self-assessment regime.

Any concerns about non-residents not complying with their tax obligations could be addressed by withholding tax at the standard rate of 20% on the rent after expenses and paid over to Revenue with the Third-Party Return. Adopting such an approach would supply Revenue with information on the recipients of such rental income while also protecting the Exchequer through the collection of withholding tax, if necessary.

[12] Section 1041 TCA 1997
[13] Section 1034 TCA 1997

APPENDIX II

Summary of the interest deductibility provisions which, following the adoption of the ATAD ILR into Irish law, are either no longer required or should be amended		
TCA 1997	**Purpose**	**Proposed amendment**
Section 81	Section 81 sets out the general rules regarding deductions in computing the profits of a trade.	Broaden the scope of section 81 so that a taxpayer is entitled to deduct interest and 'interest equivalent' expenses that is incurred for a business or commercial purpose.
Section 97(2) (e)	Section 97 sets out the computation rules for Case V rental profits. Section 97 (2) (e) provides for a deduction for interest expense related to the purchase, repair or improvement of rental property.	In our view, section 97(2)(e) should be replaced with a broad business purpose test.
Section 130 (2) (d) (iv) (and related sections 130 (2B), 452, 452A and 845A) and section 130 (2) (d) (iii) (II))	Interest on debt without any 'equity' characteristics where it is payable to a non-resident 75% group member is automatically treated as a distribution under section 130(2)(d)(iv). This treatment is disapplied for EU and UK residents by section 130 (2B). Sections 452, 452A and 845A also provide for elections to override this distribution treatment.	In our view, the automatic treatment as a distribution for interest paid to a non-resident 75% group member which is not otherwise within the scope of section 130 measures targeted at interest on debt with equity characteristics should be removed. It would follow that sections 130(2B), 452, 452A and 845A should also be removed, as they would no longer be relevant where distribution treatment no longer applies. We believe that section 130(2)(d)(iii)(II) should also be removed as it is a measure that addresses the quantum of interest akin to thin capitalisation rules (rather than the purpose of the interest) which is now also the purpose of the 30% EBITDA cap under the ATAD ILR.

Section 247 (interest as a charge) and section 249 (recovery of capital)	Section 247 TCA 1997 provides relief under interest as a charge provisions for qualifying borrowings which are used to acquire shareholdings in trading companies. Disposals of any shareholdings or intra group debt trigger ‘recovery of capital’ measures which deny a deduction for ‘interest as a charge’ by deeming borrowings to be repaid (even if the financing is unrelated to the recovery event).	The section 247 rules (and the recovery of capital rules contained in section 249) are extremely complex. Given the protection already afforded by the introduction of the ILR, in our view, these provisions should be simplified to enable groups to restructure debt without falling within the scope of onerous recovery of capital provisions. We firmly believe that a general test for permitting a deduction for interest expense that is incurred for a business or commercial purpose should be introduced in conjunction with the removal of section 247 TCA 1997. However, if it is the intention of policymakers to retain section 247, then at a minimum, the following provisions should be modified: a. Consideration should be given to removing the requirement for a common director under section 247(3)(b) TCA 1997, given this requirement poses an administrative burden without any obvious policy rationale. b. Section 247 (4E) TCA 1997 denies interest relief as a charge in respect of interest on an intra-group loan used to finance the purchase of certain assets from another group company. Consideration should be given to simplifying or removing this measure (similar to the proposed removal of section 840A below) as the ATAD ILR applies the limitation cap the limitation

		cap to both group and third-party borrowings. c. The very broad scope of the application of the deemed recovery of capital rules in section 249 TCA 1997 can mean common steps taken by companies to tidy up balance sheets of group companies and to simplify forecasting and monitoring compliance with the ATAD ILR or similar interest limitation rules in other jurisdictions, can trigger the deemed recovery of capital provisions in circumstances which are wholly unrelated to the borrowing in question. We believe that the impact of the recovery of capital rules are disproportionate and need to be reconsidered. We have set out further analysis of these issues in **Appendix III** to this submission.
Section 291A	Section 291A caps relief for interest expense and capital allowances in a given period at 80% of the tax adjusted income from specified intangible assets.	As interest is already subject to the 30% of EBITDA limit under the ILR, in our view the 80% cap under section 291A should be disapplied.
Section 817C	Section 817C is an anti-avoidance provision which denies a deduction for interest expense accrued by a borrower until such time as it is taxed in hands of connected party lender.	In our view, in a reformed regime for interest deductibility which allows for a broad business purpose test for interest, this provision should be removed for corporation tax purposes. However, it would be important to ensure that where the section has previously resulted in an expense being denied, relief should be preserved with it being treated as an interest expense subject to ILR in the claim period.
Section 840A	Section 840A is an anti-avoidance provision that denies a trading	We consider that section 840A TCA 1997 should be removed as it can impact *bona*

	deduction for interest payable on intra-group borrowings to purchase assets from a connected company.	*fide* transactions and the ATAD ILR 30% EBITDA limit will in any event apply to both group and third-party borrowings. However, relief for unused and carried forward expense which may be offset under section 840A against profits from an acquired trade should be preserved.

APPENDIX III

Further details on the impact of the sections 247 and 249 TCA 1997

Section 247 TCA 1997 provides relief under interest as a charge provisions for qualifying borrowings which are used to acquire shareholdings in trading companies.

Several limitations apply to these measures and they are also subject to the extensive recovery of capital provisions that apply under section 249 TCA 1997 and corresponding anti-avoidance measures.

The qualifying loan conditions under section 247(3) TCA 1997 which must be satisfied, not only at the time of drawdown of the borrowing but throughout the period that interest is paid on the loan are:

a) when the interest is paid, the investing company must have a material interest in the company, or where the loan is on-lent and used by a company connected with the company, in the company and the connected company,
b) during the period taken as a whole, from applying the loan to the time when the interest was paid, at least one director of the investing company was also a director of the company or, where the loan is on-lent and used by a company connected with the other company, in the company and the connected company,
c) during that period the investing company did not recover any capital from the company or from a connected company, apart from any amount taken into account under section 249.

The section 249 measures are essentially anti-avoidance measures which disallow or restrict interest relief available to a borrower company under section 247 where the borrower company has, or is deemed to have, recovered capital from the company in which the borrowings are invested or a connected company, without using the capital recovered to reduce the loan in respect of which relief is claimed.

If the borrower company recovers or is deemed to recover an amount of capital which is not used to repay the qualifying 247 borrowing, the borrower company is deemed to have repaid an amount of the qualifying borrowing which is equivalent to the recovered capital amount. This means that a corresponding amount of otherwise deductible interest expense paid is restricted on the borrowing and a deduction is denied for the restricted interest paid.

The measures apply not just to actual recoveries of capital by the borrower company from the investee company but also to several deemed recovery of capital events which can include:

- The assignment of connected party debt (even if the debt is wholly unrelated to the qualifying borrowing of the borrowing company or the investment made because of the deployment of the proceeds of the qualifying loan).
- The settlement of debt amounts.
- Recovery of capital arising to subsidiaries in an underlying holding chain of companies, apart from certain circumstances where permitted exclusions are available for capital recoveries resulting from the liquidation or unwinding of intermediate companies in the holding chain which have been undertaken for *bona fide* commercial purposes.

In general, the way corporate groups comply with earnings stripping measures in other countries is to ensure that the largest borrowers in their group manage their debt levels and forecasted interest costs during the taxable period so as not to exceed 30% of EBITDA. It is normal for groups to endeavour to reduce the risk of exceeding the 30% of EBITDA ceiling where the group overall has debt levels and interest expense within that ceiling. It is typical for these groups to attempt to mitigate any excess interest limitation amount in the period in order to minimise the uncertainties arising from potential reliance on reliefs.

The ATAD ILR permits the carry forward of interest spare capacity which is similar to the design of measures enacted in other EU Member States and internationally which include provisions to carry forward excess disallowed expenses in one period to future periods. However, as there is always uncertainty surrounding the capacity of the group to use these reliefs in the future, failure to deduct the disallowed expense can mean an unexpected increase in the effective tax rate of the group for the period. This effect could be immediate on the key performance metrics of a company if there is sufficient uncertainty over the probable use of the interest credit thus preventing the recording of a deferred tax asset. A deviation from expected results for the period can affect the perceived performance of the company from the perspective of its shareholders, debt investors and the markets.

In practice, and for bona fide commercial reasons, groups will focus on minimising the risks arising from unforeseen excess interest amounts by restructuring existing debt flows. To do this, the debt is consolidated into and may need to be centred on companies which have the highest capacity to absorb the expense. The group ratio rule is of course helpful here.

Irish groups are impacted by the broad scope of the deemed recovery of capital rules in section 249 where they take common steps (which are taken by companies subject to equivalent measures in other jurisdictions) to tidy up balance sheets of group companies and to simplify forecasting and monitoring compliance with ILR.

To illustrate this, we have outlined a couple of scenarios below whereby a group which wishes to take steps to simplify forecasting and monitoring compliance with ILR will be penalised by triggering the disallowance of an existing relief.

Impact for Irish groups that centralise cash and intra group debtor holdings

In this example, a company ("TopCo") has borrowed from a third-party bank and used the proceeds for a qualifying purpose under section 247, such as lending to a group member that is engaged in carrying on a trade ("TradeCo") who in turn uses the loan proceeds for a qualifying purpose. Separately, TopCo has advanced loans funded from its equity capital in the past to TradeCo who in turn used these loans to fund general working capital requirements as part of its trade.

The group decides it will focus its efforts to centralise cash balances and to monitor net borrowing costs in compliance with ILR in TopCo (which has significant third-party expense) and TradeCo (which is one of the biggest trading companies in the group). The group forecasts that its net borrowing costs will fall below the 30% of EBITDA ILR.

TradeCo holds balances of trade debtors owed by another group member, SubsidiaryCo, which does not have the liquidity to repay the sums due and TradeCo decides to assign these debtors to TopCo in settlement of the prior working capital borrowings. No part of the section 247 loan advance is repaid by TradeCo and TopCo has not realised any cash from the assigned debtor amounts owed by SubsidiaryCo. This assignment of intragroup balances relates to a completely separate loan advanced by TopCo to TradeCo but gives rise to a deemed recovery of capital by the borrower, TopCo, equal to the amount of the debtors assigned/loan repaid by TradeCo. This results in a restriction of TopCo's deductible interest expense.

The effect of these assignments is to deem TopCo to have repaid an amount of its debt to the third-party bank. There is no difference in the amount of interest expense borne by the group. This straightforward tidy up exercise has triggered a disallowance of expense.

It may be technically possible to avoid triggering a deemed recovery of capital in the above scenario, however, to do this it would involve entering into transactions which are not required from a commercial perspective and which potentially give rise to significant additional costs for the group. Therefore, careful consideration needs to be given to simply our existing legislation to remove the barrier/penalties for groups that need to take certain steps to comply with the new ILR regime.

Impact for Irish Outbound Companies

Where an Irish parent company ("Irish TopCo") uses funds borrowed from a third party bank for a qualifying purpose to invest in the share capital of its direct subsidiary, which is a holding company ("Irish HoldCo"), then the debt borrowed by Irish TopCo may be deductible as interest as a charge under section 247.

In this scenario, Irish Holdco is indirectly holding shares in trading companies through Irish and foreign subsidiary holding companies and uses the funds borrowed to finance the investment in a new foreign group. The deemed recovery of capital provisions may apply in this group structure to Irish HoldCo as it is a holding company which holds other holding companies (section 249 (2)(ac) TCA 1997). The repayments of loans, share capital sales and loan assignments between the subsidiary holding companies and trading companies in the group must be monitored, as well as any capital recovered (or deemed to be recovered) by Irish HoldCo or by Irish TopCo.

Following the implementation of the ILR into Irish law, the above group may wish to tidy up some of its intra-group debt but this may trigger the recovery of capital rules. For example, where any subsidiary holding companies in the group decides to repay any loans in existence between them and yet there is no actual or commercial changes or impact on the bank borrowings the interest on which is being tested for ILR.

Even though the business intention would be to restructure the level of interest bearing debt and related net borrowing costs of the Irish group members to be better aligned with EBITDA, the repayments of loans between the subsidiary holding companies may trigger a deemed recovery of capital by Irish HoldCo. This is notwithstanding there is no actual capital recovered from the group's investments and there are no funds received by Irish HoldCo.

The recovery of capital provisions would deem Irish TopCo, the borrower and investing company, to have recovered any capital recovered by "an intermediate holding company" from another company where the company concerned owns directly or indirectly 50% of the share capital of the intermediate holding company or both companies are under the control of the same person. The result of the application of the deemed recovery of capital provisions is that the receipt of the loan repayment proceeds by a subsidiary holding company triggers a deemed recovery of capital by TopCo such that it is treated as though it had repaid the corresponding amount of its qualifying borrowing to the bank when in fact this did not happen nor would it be possible for this to happen in a commercial environment.

This results in a disallowance of a portion of the interest expense deduction otherwise available to Irish TopCo. The outcome applies notwithstanding that the investment in the Irish and foreign operating groups is held through a parallel ownership chain and is in no way linked to the original borrowing used to finance the investment in the foreign group. International groups will continually refinance debt to fund growth rather than repay because it is the cheaper and more flexible component of its weighted average cost of capital or there are significant breakage costs. The ability for a group to actually repay debt when there is a deemed or actual recovery (in tax terms) is quite limited in reality.

We believe it is now appropriate to modify the provisions in sections 247 and 249 TCA 1997. It is clear that the deemed recovery provisions in particular can have unintended consequences of impacting wholly commercial financing transactions in an international group that are unrelated to the original debt and not connected with any base erosion, profit shifting or avoidance motivations.