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Mr Eugene Creighton
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Double Taxation Conventions on CAT

Dear Eugene

We are writing to you to highlight our members ongoing concerns with the lack of double taxation conventions that have been concluded between Ireland and other jurisdictions in respect of capital acquisitions tax (CAT).

Currently, Ireland has only two double taxation conventions in respect of CAT in operation, one with the UK, which was negotiated in 1977 and the other with the USA, which was negotiated in 1950. These two agreements recognise the historic links between the countries involved and Ireland's diaspora. However, migration and international investment trends have changed significantly since these two double tax conventions were concluded.

With the increased globalisation of the economy, the prevalence of Irish taxpayers holding assets outside of Ireland has increased significantly in recent decades. We believe it is timely and appropriate for Ireland to seek to conclude new double taxation conventions in respect of CAT, particularly with other EU Member States. In addition, we consider the terms of the existing Ireland/ USA double taxation convention in respect of taxes on the estates of deceased persons, should be reviewed and updated.

Negotiate new double taxation conventions in respect of CAT

The investment market has expanded exponentially over recent years with a wide array of international investment products and platforms now available to investors. This means that overseas investment by Irish individuals has become more the norm rather than the exception. In addition, many individuals choose to move to work abroad for a number of

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years following completion of their education or later in life to pursue career opportunities before returning to Ireland. As a result of these changes, Irish individuals bequeathing assets from more than one country on their death is a common occurrence.

The absence of double tax conventions on CAT means that where an Irish resident or ordinarily resident taxpayer dies leaving assets in a foreign jurisdiction, double taxation can arise in respect of the passing on of those assets. This is because in many cases, both Ireland, as the country of residence of the taxpayer and the other country where the foreign asset is located, have taxing rights on the death of the taxpayer.

Most EU Member States levy taxes on the death of a person. Some Member States apply a tax on the heirs, while other Member States apply a tax on the basis of the estate. In both cases, the tax liability is determined on the basis of a variety of factors such as the residence, habitual residence, domicile or nationality of the deceased and/ or of the beneficiary and/ or, the location of property.

This means that double or even multiple taxation of the same inheritance may arise in different Member States. The European Commission has acknowledged that while Member States levying inheritance or estate taxes may have adopted mechanisms to avoid the double taxation of inheritances in a cross-border context, in most cases, relief from double taxation is incomplete.¹ In addition, the taxation of trusts on the death of a disponent can be problematic as many EU Member States do not recognise trusts.

As you will be aware, in an Irish context, where there is no double tax convention in place, unilateral relief may be available under section 107 Capital Acquisitions Tax Consolidation Act (CATCA) 2003. Relief under this section is granted where a gift or an inheritance of foreign property to or from an Irish resident or ordinarily resident beneficiary or disponent is reduced by the payment of a foreign tax which is similar in nature to estate duty, gift tax or inheritance tax.

However, there are limitations to the relief available under section 107. For example, if a benefit contains both Irish and foreign property, the credit for foreign tax is available against the tax applicable on the foreign property only. In other words, the Irish tax must be apportioned between the Irish and foreign property and credit is only given for the foreign tax against the Irish tax on the foreign property. This may lead to scenarios where no relief for foreign tax is given where the Irish tax referable to the foreign property/ asset is less than the foreign tax.

In addition, where the foreign tax is not payable by the beneficiary of the foreign benefit, then no credit is allowed even if the foreign tax is payable by the estate or another beneficiary. In cases where the foreign tax is to be paid by the estate or is treated as a testamentary expense, then such tax would be payable out of the residue of the estate.

Another example of the limitations to the relief available under section 107 CATCA 2003 is the requirement that the foreign tax be *“of a character similar to estate duty, gift tax or inheritance tax.”* This can give rise to uncertainty in some cases. For instance, in Australia,

¹ https://taxation-customs.ec.europa.eu/paying-inheritance-tax-twice_en

while there is no inheritance or estate taxes, in certain circumstances capital gains tax may apply to the deceased's estate at the time of their death on the passing of an asset to a foreign resident.

Further complications in the application of unilateral relief under section 107 can arise where more than two countries have taxing rights over the assets in the estate. For example, an estate could have an Irish resident disponent, a German resident beneficiary and UK situate assets. In those circumstances, each jurisdiction is likely to have taxing rights over the estate. However, the application of unilateral relief in such a scenario can be very complex and in many cases double taxation will ultimately arise.

Given the varying types of inheritance and estate taxes levied in the EU alone, and the limitations which exist in respect of unilateral relief under CATCA 2003 for foreign tax paid, we firmly believe that consideration should be given to commencing the process to negotiate new double tax conventions in respect of CAT, with priority given to negotiations with other EU Member States and other countries where there is a strong Irish presence such as Australia or Canada.

Update the existing Ireland/USA double taxation convention in respect of CAT

We believe the existing Ireland/USA double taxation convention in respect of taxes on the estates of deceased persons should be reviewed as it needs to be modernised. Our members have noted that the Ireland/USA double tax convention does not compare favourably with either of the double taxation conventions the United States has concluded with Germany and the UK.

The Ireland/ USA double taxation convention was given legal effect under Finance Act 1950 meaning it predates the Capital Acquisitions Tax Act 1976 (which was consolidated into the CATCA 2003). The convention applies to inheritance tax in Ireland and federal estate tax in the USA.

The United States imposes federal estate tax on worldwide assets if the disponent was an American citizen or was domiciled in one of the states of the USA. Otherwise, generally only property situated in the United States is liable to federal estate tax.

The incidence of Irish resident or ordinarily resident individuals who hold American assets at death has increased significantly in recent times due to a number of factors. As outlined above, overseas investment by individuals is becoming increasingly common. Most investment portfolios include American situs assets such as shares in US companies or US Exchange Traded Funds (ETFs) and potentially US investments held in an Approved Retirement Fund. In addition, many US multinationals operating in Ireland incentivise their employees using share-based remuneration. Shares received by Irish based employees under such arrangements are often in the US parent company rather than the local Irish subsidiary.

Our members have raised concerns that the limited scope of the Ireland/USA double taxation convention means that US federal estate tax applies in estates even if the level of

US assets held is relatively modest. While American citizens and individuals domiciled in the USA are entitled to a US\$13,610,000 exemption amount for combined lifetime gifts and transfers at death, for non-US domiciled individuals, federal estate tax applies where the US situs assets exceed an exemption amount of US\$60,000.

This means that if an individual dies resident or ordinarily resident in Ireland and they are not an American citizen or domiciled in the USA, their estate will be subject to US federal estate tax in respect of any US situs assets held at the date of death, if the value of those assets exceed the exemption threshold of US\$60,000. This is a low threshold and where it is exceeded, the liability to US federal estate tax, which applies at rates of up to 40%, can be significant.

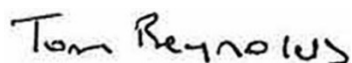
The position is further compounded by the fact that the US marital deduction (spousal relief) which exempts transfers between spouses does not apply where the spouse is not an American citizen. In circumstances where the US assets pass to a spouse who is not an American citizen, no relief is available under the Ireland/USA double tax convention as double taxation does not arise. This is an issue which is arising frequently in practice and is causing immense concern for surviving spouses and their families. As a full spousal exemption applies in Ireland, most taxpayers do not expect an inheritance tax liability to arise in circumstances where an estate passes to the spouse.

While investment in American assets by Irish resident taxpayers may have been relatively rare when the Ireland/USA double taxation convention was concluded in 1950, it is now an increasingly common occurrence. In light of this change, we would urge that consideration is given to renegotiating the terms of the Ireland/ USA double taxation convention.

Conclusion

Bilateral tax treaties are an essential part of any tax framework, particularly for small open economies, such as Ireland. We urge policymakers to address the significant gap in Ireland's tax treaty network in the area of CAT given the increased level of overseas investments made by Irish individuals. An expanded network of double taxation conventions related to CAT, particularly with our EU counterparts, would help to alleviate the incidence of double taxation and provide much needed certainty to Irish taxpayers inheriting foreign property/ assets. The Institute would welcome the opportunity to discuss the matters raised in this letter with Revenue's International Tax Division.

Yours sincerely



Tom Reynolds
Institute President

cc. Gary Hynds, Principal Officer, Tax Division, Department of Finance