Feeback on the draft Pillar Two guidance circulated to the TALC BEPS Sub-committee

10 July 2024

General comments on the draft guidance

The Institute welcomes the opportunity to provide feedback on the draft Pillar Two guidance prepared by Revenue. As it currently stands, we consider the draft Tax and Duty Manual (TDM) on Part 4A provides a very high level summary of the Irish implementation of the Pillar Two Rules. While we recognise Revenue has noted at TALC that the TDM will be a living document with many iterations given the evolving nature of the administrative guidance issuing from the OECD, it must be acknowledged that many significant points of uncertainty remain for taxpayers.

It is helpful to have sight of a list of "*Items not currently addressed in TDM"* which have either been referred to the OECD for consideration (or may be referred in the future) and we welcome an update at the next meeting on how these items are progressing.

However, there is no doubt given the inherent complexity of the legislation that taxpayers will continue to identify matters that are unclear, as they apply the rules to their groups. The OECD has indicated that the rate and degree of administrative guidance is likely to substantially decrease going forward meaning it can no longer be reasonably assumed that the OECD will issue timely guidance on all of these matters.

Therefore, in the absence of a clear indication from the OECD that a matter is a priority for consideration by the Secretariat and the Inclusive Framework delegates, Revenue should strive to provide clarity on these fundamental issues for Irish taxpayers in its own guidance.

Specific comments on the draft guidance

Part 04A-01-03 – Draft Guidance on Administration

- **Registration/ deregistration:** We request that the guidance on "relevant parent entity", "relevant UTPR entity", and Section 111AAH TCA 1997 should be expanded to give taxpayers clarity regarding their registration and deregistration obligations for the IIR and UTPR top-up taxes.

  Section 111AAH(1) defines a relevant parent entity and relevant UTPR entity as an entity that is subject to the IIR or UTPR top-up taxes, respectively. Taxpayers should be provided specific guidance on the meaning of "subject to tax" in this context, particularly

in circumstances where the entity is potentially subject to top-up tax in Ireland, but no liability actually arises for a particular fiscal year.

We would also request that the guidance clarifies the deregistration obligations on taxpayers where they have registered for a top-up tax but a nil liability arises for a particular fiscal year. At a minimum, we would ask that Revenue's comments at the TALC BEPS Sub-committee meeting on 24 October 2023 in relation to the above matter, are reflected in the published TDM.

- **Section 111AAO – QDTT Group:** We request that specific guidance should be provided on scenarios where the composition of an MNE Group changes and the impact of such changes on existing Irish QDTT Groups (e.g., Irish entities are acquired, disposed, incorporated, liquidated, etc. during a fiscal year).

- Members are seeking guidance on how to register entities for Pillar Two on ROS. We welcome an update from Revenue on its plans to provide published guidance including screen-shots etc to be included in the TDM in due course. Members have queried whether a registration can be amended after the fact (for instance, if an entity registered but did not elect into a QDTT group on Day 1 but then wants to elect in at a later date).

Part 04A-01-01 – Draft Guidance on Part 4A TCA 1997

- **Section 2 – OECD/G20 Guidance on the GloBE rules:** We request that this section be updated to reflect:

  - The release of the consolidated version of the OECD's Commentary on the GloBE Rules and Safe Harbour and Penalty Relief Guidance on 25 April 2024. At present, the draft TDM only refers to the updates to the illustrative examples document.
  - The release of the latest OECD Administrative Guidance in June 2024.

- **Section 8.7 – Section 111Z:** We request that further clarification is given in section 8.7 to note that guidance included therein on section 111Z are for IIR/UTPR purposes. Readers should be referred to Revenue's guidance on the QDTT, noting that differences may arise with respect to the cross-border allocation of taxes under Ireland's QDTT rules.

- **Section 9.3 – Section 111AE:** We request that the guidance on eligible payroll costs is updated to specify that benefits such as health insurance, pension contributions and stock-based compensation should be included in this figure.

- **Section 9.9 – Section 111AK:** We request that the guidance in this section is updated to note that the safe harbour applies only for the purposes of collection of top-up tax under the UTPR under Section 111N.

- **Section 12.1 – Section 111AW:** While this section provides an overview of the provisions of Section 111AW, we suggest it should refer readers to further OECD

Commentary and illustrative examples that are crucial to understanding and implementing the provisions of this section.

- **Substance Based Income Exclusion (SBIE) and the definition of eligible tangible assets in Section 111AE:** A number of queries have arose in practice on what is meant by "immovable property". We would welcome some practical examples to be included in the TDM to provide clarity on this.

Other queries for clarification

- We request clarification from Revenue that taxpayers and their advisers can consider the OECD June 2024 Administrative Guidance as being applicable now in the absence of it being specifically referred to in domestic legislation.

- The OECD June 2024 Administrative Guidance provides for varying degrees of optionality. For example, the Deferred Tax Liability (DTL) recapture rule may apply using LIFO or FIFO basis, which seems to be at the choice of the taxpayer. We would welcome clarification on Revenue's approach to this guidance.

- The OECD June 2024 Administrative Guidance appears to provide for the push down of deferred taxes, while the domestic legislation currently envisages the allocation of covered taxes only (i.e. current taxes to other entities). We would welcome clarification from Revenue on this point.

- The DTL recapture rules apply (Section 111X(9) TCA 1997) where the DTL does not reverse and is not paid within 5 years. The OECD June 2024 Administrative Guidance (para 57, replacing para 89 in the overall OECD guidance) notes that *"The term 'payment' in Article 4.4.4 and Article 4.4.2(b) refers to the accounting reversal of the DTL or of the recaptured DTL."* We would welcome clarification on Revenue's position on this.

- We would welcome an update from Revenue on the considerations in relation to the effective date of the CBCR Safe Harbour anti-arbitrage provisions.

Net investment loan arrangements

- Under IFRS, certain long-term loans receivable by a parent company from a foreign subsidiary may be accounted for in the same manner as a foreign exchange hedge of that investment. For accounting purposes, in the appropriate fact pattern, the loans are regarded as an extension of the parent's net investment in that foreign subsidiary. This means that in the Group's consolidated financial statements, FX movements on such a loan are initially recognised through the OCI rather than in the income statement. On disposal of the foreign subsidiary, these exchange differences are recognised within the group's consolidated income statement as part of the profit or loss on disposal.

  An example of this treatment is set out below:

  - An MNE Group prepares Euro-denominated IFRS consolidated financial statements.

- An intermediate parent entity of the group, IrishCo, lends in USD to its direct subsidiary, US Sub.
- Under IFRS (IAS 21), the loan arrangement is treated as a part of IrishCo's net investment in US Sub and therefore, FX movements on the USD loan are booked through the OCI in the IFRS consolidated accounts (and not in the income statement).
- In Year 5, IrishCo sells its shares in US Sub and the loan is repaid. As a result, under IFRS, aggregate FX movements on the loan to US Sub are recycled to the P&L in the IFRS consolidated financial statements.

Where IrishCo is not carrying on a treasury trade and the loan is not a debt on security, no Irish corporation tax/ CGT should arise on the repayment of the loan and, as a result, no deferred tax should be recognised on the unrealised FX movements. The accounting treatment of such loans is equivalent to that applicable to effective hedges, with FX movements on both instruments being reflected in OCI while the arrangements are in place, with these amounts being recycled to the P&L on disposal of the foreign subsidiary.

Paragraphs 57.2 - 57.3 of the OECD Commentary on Article 3.2.1 states that the treatment of a net investment hedge should follow the treatment of the investment it is hedging. This guidance and related paragraphs are reflected in Section 111P(13) TCA 1997.

We would welcome confirmation from Revenue that Section 111P(13) can apply to foreign exchange gains and losses on long-terms loans that are treated as part of a parent's net investment in a foreign subsidiary under IFRS.