Irish Tax Institute

January 2019

Response to the Consultation on ATAD Implementation – Hybrids and Interest Limitation

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1. About the Irish Tax Institute

The Irish Tax Institute is the leading representative and educational body for Ireland's Chartered Tax Advisers (CTA) and is the only professional body exclusively dedicated to tax.

The Chartered Tax Adviser (CTA) qualification is the gold standard in tax and the international mark of excellence in tax advice. With over 5,000 members in Ireland, along with the Chartered Institute of Taxation UK and The Tax Institute of Australia, we are part of the 30,000-strong international CTA network and a member of CFE Tax Advisers Europe, the European umbrella body for tax professionals.

Our members provide tax education and expertise to thousands of businesses, multinationals, and individuals in Ireland and internationally. In addition, many hold senior roles within professional service firms, global companies, Government, Revenue, state bodies and the European Commission.

After 50 years, the Institute remains deeply committed to the role it can play in education, tax administration and tax policy in Ireland and in building an efficient and innovative tax system that contributes to a successful economy and society. We are also committed to the future of the tax profession, our members and our role in serving Ireland's taxpayers and best interests in a new international world order. Our *Irish Tax Series* publications and online database *TaxFind* are respected and recognised as Ireland's most extensive tax information sources.

Irish Tax Institute - Leading through tax education.

2. Executive Summary

The Irish Tax Institute welcomes the opportunity to engage with the Department of Finance on two further areas of implementation of the EU Anti-Tax Avoidance Directives (ATAD and ATAD2).[1] Namely:

- Anti-Hybrid Rules; and
- Interest Limitation Rules

We have responded to the questions raised in the Consultation Paper[2] to the extent that it has been possible within the short consultation time period. We understand that this public consultation is a first step in a wider consultation process on the implementation of anti-hybrid and interest limitation rules in Ireland. Undoubtedly, further discussions with companies and other stakeholders will be essential in order to be fully informed of the impact of these rules.

Anti-Hybrid Rules

Ireland is required under ATAD[3] and ATAD2[4] to introduce anti-hybrid rules by 1 January 2020 (1 January 2022 in the case of reverse hybrid mismatches). Anti-hybrid provisions are extremely complex and require very careful consideration before implementing into Irish law.

We have set out detailed recommendations in response to the consultation questions in the body of this submission, however, it is important that policymakers take the following key matters into account when implementing rules to target hybrid mismatches in Ireland:

- Ireland should not go beyond the framework for hybrid mismatch rules in ATAD and ATAD2. Any changes to Irish tax legislation should be limited to payments that are actual hybrid payments and not for mismatches arising because of another country's tax system or from transfer pricing adjustments.

- Irish legislation should treat as "included" income payments that are taxed in another jurisdiction, even if these payments are not taxed upon the same entity, as the entity that is considered the taxable entity from an Irish perspective. For example, in an US/Ireland scenario, Ireland should not deny a tax deduction if a payment is not taxed in the immediate recipient company, based in the US, as it might ultimately be taxed in another US company, if the immediate recipient is treated as disregarded under the US check-the-box rules or under the global intangible low-taxed income (GILTI) provisions.

[1] 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 and Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries.
[2] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018.
[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.
[4] Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries.

- Using a version of the control test in section 432 Taxes Consolidated Act (TCA) 1997 would introduce concepts, such as participators and associated persons that would be inappropriate in the context of the anti-hybrid rules. It would include non-bank lenders, which would radically extend the scope of the Directive.

Interest Limitation Rules

The general implementation date for the ATAD interest limitation rules was 1 January 2019. However, the Directive permits a derogation from this implementation deadline until 1 January 2024, for EU countries that have national targeted rules, which are equally effective as the ATAD interest limitation rules.

On 22 June 2016, the Department of Finance released a statement which confirmed that, *"the provisions on interest deductions are deferred until 2024 for countries, like Ireland, that already have strong targeted rules. There are also strong grandfathering provisions to provide certainty to investors"*[5] Subsequently, the Irish Government notified the European Commission that Ireland's existing interest deductibility rules are at least equally effective to the rules contained in the Directive.

Based on the position taken by the Government in June 2016, taxpayers have entered into transactions in good faith, on the assumption that our existing interest deductibility rules would continue to apply until 1 January 2024.

In September 2018, the Government indicated for the first time that Ireland might introduce the interest limitation rules under ATAD before 2024, because it remains unclear that agreement will be reached with the Commission on the derogation, as Ireland's existing rules are structurally different to the ratio-based rules in ATAD.[6]

It is a matter for the Government to defend its stated position regarding our existing rules with the Commission. If the Government moves to introduce ATAD interest limitation rules before 2024, this should be confirmed without delay, together with a clear announcement given on grandfathering of existing loan arrangements. This is critical so that businesses can have the necessary certainty regarding the tax consequences of arrangements that they have entered on foot of these statements.

Given the Government's stated position from the outset when the Directive was agreed, that our existing interest deductibility rules are equally effective to those contained in ATAD, we believe our existing domestic legislation should be fundamentally reformed, in parallel with the implementation of the new ATAD compliant interest limitation rules in the tax code.

[5] https://merrionstreet.ie/MerrionStreet/en/News-Room/Releases/Minister_Noonan_welcomes_agreement_on_the_Anti-Tax_Avoidance_Directive.html#sthash.l3szqoph.dpuf

[6] Government of Ireland, Ireland's Corporation Tax Roadmap, Incorporating implementation of the Anti-Tax Avoidance Directives and recommendations of the Coffey Review, September 2018.[6]

In our view, the reformed corporate tax code 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 under ATAD against base erosion risks and removing the existing interest restrictions within sections 247/249 TCA 1997.

Preserving some of the targeted measures within the existing legislation, such as bond-washing or interest on capital gains, could be considered by policymakers to address any concerns they may have regarding the removal of the protections contained within the existing tax code for the deductibility on interest.

In any case, any early adoption of the interest restriction measures under ATAD should take place no earlier than 2021, because there will undoubtedly be a great deal for taxpayers to absorb and businesses will need time to put the necessary systems in place.

Conclusion

In view of the very technical nature of these provisions, it is an imperative that all stakeholders are provided with an opportunity for extensive consultation on draft legislation well in advance of the measures commencing, to ensure the new rules within the tax code do not give rise to any unintended consequences.

3. Institute Recommendations

Anti-Hybrid Rules

1. In implementing ATAD2, Ireland should apply the framework for the hybrid mismatch rules as set out in the Directive. Consequently, Irish anti-hybrid provisions should only apply to taxpayers that are subject to corporation tax in Ireland.

2. The definition of foreign taxes equivalent to Irish taxes should be as broad as possible and include all taxes on profits that a corporate taxpayer could be subjected to in a foreign jurisdiction, including CFC charges.

3. Any changes to Irish tax legislation should be limited to payments that are actual hybrid payments and not for mismatches arising because of another country's tax system or from transfer pricing adjustments. This would be in line with the recommendations made in the OECD 2015 Report on BEPS Action 2, regarding hybrid mismatch arrangements.

4. Irish legislation should treat as "included" income payments that are taxed in another jurisdiction, even if these payments are not taxed upon the same entity, as the entity that is considered the taxable entity from an Irish perspective. For example, in an US/Ireland scenario, Ireland should not deny a tax deduction if a payment is not taxed in the immediate recipient company, as it might ultimately be taxed in another entity in the US, e.g. it could be taxed under their GILTI provisions.

5. Payments which are ultimately subject to CFC charges in another jurisdiction and payments to check-the-box entities in the US should be treated as being subject to tax (and therefore included) on the basis that the payment is ultimately subject to tax (albeit not necessarily by the immediate recipient company).

6. Irish legislation should follow the guidance in ATAD2, to provide that timing differences in recognising items of income or expenditure as derived or incurred, do not generally give rise to mismatches for the purposes of the anti-hybrid provisions.

7. In respect of payments under a financial instrument, the test of whether a payment will be made within a reasonable period of time should be based on the terms that might be expected to be agreed between unrelated parties acting at arm's length. If the mismatch is simply the result of a timing difference, the taxpayer may be denied a deduction but should be allowed to take deduction at a later date when that income is taxed in the other jurisdiction.

8. As disregarded PEs would become relevant in the context of an introduction of a branch exemption, as part of a potential move to a territorial tax regime, we believe that policymakers should consider whether to introduce defensive rules on disregarded PEs, as

part of the planned consultation process on moving from a worldwide basis of taxation to a territorial tax system, due to be held in 2019.

9. Where an amount of income would become chargeable to Irish corporation tax in Ireland, because of the anti-hybrid rules, such income should be taxed as if it was earned in Ireland, under the corresponding Case in Schedule D.

10. The imported mismatch rules should not be applied where an Irish taxpayer is transacting with a taxpayer in an EU country. The onus cannot be on a taxpayer to determine if an EU Member State has implemented their obligations under ATAD2. This is a matter for the European Commission to address.

11. Irish tax legislation implementing anti-hybrids provisions for financial instruments should include the concept of dual inclusion income and confirm that a double deduction does not arise in such circumstances.

12. The financial trader exemption contained in ATAD2 should be incorporated into domestic legislation, together with the determining factors for that exemption which are set out in the Directive.

13. Using a version of the control test in section 432 TCA 1997 would introduce concepts, such as participators and associated persons that would be inappropriate in the context of the anti-hybrid rules. It would include non-bank lenders, which would radically extend the scope of the Directive.

14. Associated enterprises could be defined by reference to section 7, Companies Act 2014, which refers to control of the composition of the board of the directors and dominant influence and would be in line with the policy objective of ATAD2.

15. In order to apply anti-hybrid rules, taxpayers should have certainty regarding the tax treatment of entities. This could be achieved by putting existing case law principles on a legislative footing.

16. To ensure that codification of existing principles regarding the tax status of an entity will operate effectively in practice, a consultation should take place on draft legislation in advance of enacting the rules. In the interim, Revenue could adopt a practice similar to that in the UK, where they could issue a non-exhaustive list of opaque and transparent entities.

17. For ease of administration, a single concept to encompass both investor and payee when determining if a payment has been deducted and included as income would be preferable. However, in defining an investor or payee, the key factor to be considered is whether a payment has been included or not, as it will not necessarily be the entity who receives the payment that includes the payment as income for tax purposes.

18. We would recommend that the definition of financial instrument for the purpose of the anti-hybrid rules is aligned to TCA 1997.

19. The test for borrower knowledge in the context of structured arrangements and capital market transactions must be a high bar. It should not impose an obligation on a taxpayer to undertake additional due diligence on a commercial transaction over and above what would be expected of a reasonable and prudent person.

20. In defining the test for borrower knowledge in the context of structured arrangements, safe harbour provisions should be considered for securitisation transactions where funding is provided through notes of listed stock exchange entities.

21. For there to be certainty regarding the application of the anti-hybrid rules, consideration should be given to the laws of the jurisdiction in which the payee/investor is resident or subject to tax. The rules should only apply to the extent that a payee/investor is actually entitled to a deduction for a payment under local law.

22. It is critical that all stakeholders are given the opportunity to consult well in advance on draft legislation to ensure the technical operation of the anti-hybrid rules in practice do not create any unintended consequences, when interacting with existing domestic provisions.

23. Any adjustments made by an Irish taxpayer because of the application of the anti-hybrid rules should be treated as non-deductible expenses for Irish tax purposes.

24. We recommend that Ireland follows the order of application outlined in BEPS Action 2 when implementing the anti-hybrid rules in ATAD and ATAD2.

25. Irish tax legislation could be amended to reflect the existing tax treatment of stock lending and repo transactions that is currently set out in Revenue guidance. However, it would be important to consider legislating for all types of stock lending and repo transactions and not just those transactions where the transfer is for periods of less than 12 months, which are referred to in the guidance, as these would be a relatively small portion of such transactions.

26. In our view, sharia compliant transactions should be treated as “financial instruments” for the purposes of the anti-hybrid provisions in Ireland. However, such transactions should not require adjustments to be made under the rules, given the hybridity of the transaction would be directly related to timing differences, which are not considered a mismatch in a tax outcome under ATAD2.

27. The rationale for the proposed use of a separate “subject to tax” rule for reverse hybrids is unclear. We would suggest that this matter be considered as part of a public consultation on reverse hybrids, before the implementation of those rules before 2022.

28. Ireland should not apply the reverse hybrid rule to collective investment vehicles as permitted under ATAD2.

Interest Limitation Rules

29. Irish tax legislation should allow taxpayers the flexibility to decide whether to apply the interest limitation ratio rule at an individual or at a group level. Once the deductible interest for a group is calculated, a local group should have full discretion as to how the interest amount is allocated between the various members of the group.

30. Ireland should include the *de minimis* threshold of €3 million for exceeding borrowing costs permitted under ATAD, when implementing the ATAD interest limitation rule in Ireland.

31. The definition of 'standalone entity' must be implemented in a manner that will work in practice and should include entities that are legally remote (i.e. orphan entities).

32. All existing loans entered before 17 June 2016 should be excluded from the ATAD interest limitation rules adopted by Ireland, as permitted under the Directive.

33. Irish legislation should clarify that the 'grandfathering' provisions will not be lost because of a technical amendment to a pre-existing loan, which does not alter the commercial features of it.

34. If the Government plans to introduce ATAD interest limitation rules before 2024, this should be confirmed without delay, together with a clear announcement given on grandfathering. This is critical so that businesses have the necessary certainty regarding the tax consequences of arrangements that they have entered into and are contemplating now.

35. The definition of long-term infrastructure should not be confined to public private partnership projects. Projects should be considered for the general public interest irrespective of whether they are privately owned or whether a fee is charged to the public for their use.

36. In addition, the long-term infrastructure project may be located in any EU Member State and should not be confined to Ireland.

37. If it is not possible to implement both tests for the consolidated group ratio rule into Irish law, then Ireland should adopt option (b), the consolidated group's external borrowings to EBITDA ratio rule.

38. Groups containing financial undertakings should be exempt from the interest limitation restrictions. If it is not possible to extend the exemption for financial undertakings to the entire group, then a financial undertaking should have an option to avail of the exemption. Failure to provide an opt-in clause could result in groups containing financial undertakings being adversely impacted by an automatic exclusion of the financial undertaking from the interest limitation rules.

39. Non-regulated undertakings providing the same services as regulated financial undertakings should be able to avail of the financial undertaking exemption, if available.

40. Option C should be implemented into Irish legislation, i.e. to carry forward, without time limitation, exceeding borrowing costs and, for a maximum of five years, unused interest capacity, which cannot be deducted in the current tax period.

41. Consideration could be given in cases of cessation, to allow unutilised interest relief to form part of a claim for terminal loss relief under section 397 TCA 1997.

42. Given the broad range of the type of income/expenses that could potentially be treated as economically equivalent to interest and the different circumstances of the taxpayer, it may be preferable to transpose the definition set out in ATAD into Irish law. The definition contained in the legislation could be supported by Revenue guidance regarding the scope of the term.

43. All income of a section 110 company should be considered economically equivalent to interest for the purposes of the ATAD interest limitation rule.

44. To the extent lessors are not treated as an exempt "financial institution", leasing income should be considered economically equivalent to interest for the purposes of the new provisions.

45. In our view, Ireland could follow the OECD approach to define EBITDA, as taxable income, with net interest expense and capital allowances added back. If a company within a group has a negative EBITDA, this should be treated as zero for the purposes of calculating the overall group EBITDA or alternatively, it should be excluded from the EBITDA calculation entirely and be dealt with on a solo basis.

46. In view of the broad range of potential reliefs that can apply to a foreign dividend, which vary between taxpayers in Ireland, it would be challenging to devise a general rule that might operate to exclude a foreign dividend. Therefore, foreign dividends that remain subject to corporation tax in Ireland should be included in EBITDA.

47. If Ireland moves to a territorial tax system in the future, which includes a foreign dividend exemption regime, it would be appropriate then for such tax-exempt dividends to be excluded from the measure of EBITDA.

48. We believe that there should be a reconstruction of Ireland's existing rules on interest deductibility in parallel with the implementation of new ATAD compliant interest limitation rules in the tax code.

49. In our view, the reformed corporate tax code 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 247/249 TCA 1997.

50. However, any early adoption of the interest restrictions under ATAD should take place no earlier than 2021 because there will be a great deal for taxpayers to absorb and undoubtedly, businesses will need time to put the necessary systems in place to capture the data and carry out the required calculations.

4. Response to Consultation Questions

4.1 Anti-Hybrid Rules

Ireland is required under ATAD[7] and ATAD2[8] to introduce anti-hybrid rules by 1 January 2020 (1 January 2022 in the case of reverse hybrid mismatches). Anti-hybrid provisions are extremely complex and require very careful consideration before implementing into domestic law.

4.1.1 Scope of anti-hybrid rules

What entities should be within the scope of the new rules?
Article 1 of ATAD2 clearly states that the rules to address hybrid mismatches *apply to "all taxpayers that are subject to corporate tax in one or more Member States, including permanent establishments in one or more Member States of entities resident for tax purposes in a third country."* In implementing ATAD2, Ireland should not go beyond the framework for hybrid mismatch rules as set out in the Directive.

Consequently, Irish anti-hybrid provisions should only apply to taxpayers that are subject to corporation tax in Ireland. To the extent that Ireland imposes income tax on non-resident companies for certain sources of income, such entities should not fall within the scope of the new provisions, on the basis that they are not taxpayers subject to corporation tax. Similarly, regulated funds and collective investment vehicles, which are not subject to corporation tax, should be outside the scope of Ireland's anti-hybrid regime.

What foreign taxes should be considered?
The definition of foreign taxes that should be considered equivalent to Irish taxes for the purposes of establishing whether a mismatch outcome occurs should be as broad as possible, to ensure any potential for double taxation is eliminated. It should include all taxes on profits that a corporate taxpayer could be subjected to in a foreign jurisdiction, including CFC charges.

Institute recommendations:
In implementing ATAD2, Ireland should apply the framework for the hybrid mismatch rules as set out in the Directive. Consequently, Irish anti-hybrid provisions should only apply to taxpayers that are subject to corporation tax in Ireland.

The definition of foreign taxes equivalent to Irish taxes should be as broad as possible and include all taxes on profits that a corporate taxpayer could be subjected to in a foreign jurisdiction, including CFC charges.

[7] 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.
[8] Council Directive (EU) 2017/952 of 29 May 2017 amending Directive (EU) 2016/1164 as regards hybrid mismatches with third countries.

4.1.2 Subject to tax

The purpose of the anti-hybrid rules are to prevent mismatches that can arise due to differences in the legal characterisation of a financial instrument or entity.[9] Mismatch outcomes occur when there is a deduction of an expense (or double deductions of the same expense) without the corresponding receipt being fully taxed (i.e. included as ordinary income for tax purposes).

The scope of hybrid mismatch outcomes are widely cast in the Directive, which mirror the broad scope of recommendations in the OECD's 2015 BEPS Action 2 Report.[10] Ireland should not go beyond the framework for hybrid mismatch rules in the Directive. Differences in tax outcomes that arise from differing valuations resulting from the application of transfer pricing rules, should not be regarded as a hybrid mismatch.[11] In addition, a payment should not give rise to a hybrid mismatch because of the tax-exempt status of the payee under the laws of the payee jurisdiction.[12]

In implementing ATAD2, Members States can use the explanations and examples in the BEPS Action 2 Report[13] as a source of illustration and interpretation, to the extent that they are consistent with the Directive.[14] Examples in the 2015 Report[15] confirm that payments to a person established in a no-tax jurisdiction or to a taxpayer resident in a territorial tax regime (that exempts foreign source income), do not give rise to hybrid mismatches, because the resulting mismatch outcomes are not attributable to the terms of a financial instrument but rather the country's tax system.

Therefore, any changes to Irish tax legislation should be limited to payments that are actual hybrid payments and not for mismatches arising because of another country's tax system or from transfer pricing adjustments.

In practice, Ireland does not have many hybrid mismatches with EU jurisdictions, in which Ireland adopts a different view of the characterisation of an entity in another Member State, unless the Member State treats a partnership as a corporation for tax purposes. This is an issue that arises much more often in an US context.

The most common potential hybrid entities involving Ireland are entities which are subject to a US 'check-the-box' election, which potentially creates a hybrid mismatch between Ireland's treatment of the entity and the entity's treatment for US tax purposes.

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[9] Recital 13 of ATAD

[10] OECD (2015), Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 – 2015 Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

[11] Recital 22 of ATAD2

[12] Recital 18 of ATAD2

[13] OECD (2015), Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 – 2015 Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.

[14] Recital 28 of ATAD2.

[15] OECD (2015), Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 – 2015 Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, Example 1.6 and Example 1.7.

For example, a US LLC is treated as a company for Irish corporation tax purposes but can be treated as a disregarded entity for US tax purposes (i.e. either as a branch of its single member company or as a transparent partnership.)

Irish tax legislation should treat as 'included' income payments that are taxed in another jurisdiction, even if these payments are not taxed upon the same entity, as the entity that is considered the taxable entity from an Irish perspective. Ireland should not deny a deduction if a payment is not taxed in the immediate recipient company, as it may ultimately be taxed in the US for example, under the GILTI provisions. This approach would be in keeping with the guidance provided in BEPS Action 2.[16]

In determining whether a payment has been subject to tax, it is critical that any definition of foreign taxes is as broad as is possible and should include all charges on profits, to ensure any potential for double taxation is eliminated. For example, payments which are ultimately subject to CFC charges in another jurisdiction and payments to check-the-box entities in the US should be treated as being subject to tax (and therefore included) on the basis that the payment is ultimately subject to tax (albeit not necessarily by the immediate recipient company).

The Consultation Paper[17] outlines that the concept of 'inclusion' is often framed in Irish law as 'subject to tax'. ATAD2 does not refer to being subject to tax when considering whether a payment has been included as income.

However, Irish tax law contains a 'subject to tax' test in section 110(4A)(b)(I) TCA 1997, which could be adapted for the purpose of framing the new anti-hybrid provisions under the Directive into domestic law;

> *"….under the laws of a relevant territory, is subject, without any reduction computed by reference to the amount of such interest or other distribution, to a tax which generally applies to profits, income or gains received in that territory, by persons, from sources outside that territory."*

However, it may be preferable in the interest of providing clarity to Irish business and international companies looking to invest in Ireland, to have anti-hybrid provisions that apply to all types of companies that are subject to corporation tax in Ireland and remove the existing anti-hybrid provisions[18] contained within section 110 TCA 1997. This is considered further at section 4.1.4 in the context of the interaction with domestic provisions.

Adapting the 'subject to tax' concept in section 110 (4A)(b)(I) for anti-hybrid rules could also take account of potential issues arising from the use of the accruals basis when preparing a

[16] OECD (2015), Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 – 2015 Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, Paragraph 86.
[17] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 11.
[18] Section 110(4A)(b)(I) &(II) TCA 1997 and section 110(5A)(d)(iii) TCA 1997.

company's accounts and address deemed payments between a Permanent Establishment (PE) and Head Office.

Institute recommendations:
Any changes to Irish tax legislation should be limited to payments that are actual hybrid payments and not for mismatches arising because of another country's tax system or from transfer pricing adjustments.

Irish legislation should treat as "included" income payments that are taxed in another jurisdiction, even if these payments are not taxed upon the same entity, as the entity that is considered the taxable entity from an Irish perspective. Ireland should not deny a tax deduction if a payment is not taxed in the immediate recipient company.

Payments which are ultimately subject to CFC charges in another jurisdiction and payments to check-the-box entities in the US should be treated as being subject to tax (and therefore included) on the basis that the payment is ultimately subject to tax (albeit not necessarily by the immediate recipient company).

Timing differences

ATAD2 provides that timing differences for recognising when items of income or expenditure have been derived or incurred, should not generally be treated as giving rise to a tax outcome mismatch.[19] We believe that this should be reflected in domestic legislation, as it is necessary to allow for countries to have different rules for recognising income and expenditure. The Irish tax legislation should only target indefinite deferrals.

ATAD2 goes on to state that a payment under a financial instrument, which cannot reasonably be expected to be included in income within a reasonable period of time, should be treated as a hybrid mismatch, if that deduction without inclusion outcome is attributable to differences in the characterisation of the financial instrument or payments made under it. ATAD2 provides that for the purposes of payments under a financial instrument, a reasonable period of time may be considered to be either an accounting period which commences within 12 months of the end of the payer's accounting **or** if it is reasonable to expect that the payment will be included in the jurisdiction of the payee in a future period (and the terms of the payment reflect the arm's length principle).

We believe that the arm's length principle should be sufficient to ensure the inclusion of the income within a reasonable period. The test of whether a payment will be made within a reasonable period of time should be based on the terms that might be expected to be agreed between unrelated parties acting at arm's length. Such an approach is recommended in BEPS Action 2[20], taking account of the terms of the instruments and other commercial factors affecting the payment. The provision of a fixed period is likely to give rise to commercial issues

[19] Recital 22 of ATAD2
[20] OECD (2015), Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 – 2015 Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, Paragraph 58.

and could create an increased compliance burden for companies. If the mismatch is simply the result of a timing difference, the taxpayer may be denied a deduction but should be allowed to take deduction at a later date when that income is taxed in the other jurisdiction.

A similar mechanism currently exists in the operation of Section 817C TCA 1997, which could be adapted for the anti-hybrid rules. Section 817C denies a tax deduction for interest accrued on a liability between an Irish person and a connected person until such time as the interest is actually paid to the connected person.

Institute recommendations:
Irish legislation should follow the guidance in ATAD2, to provide that timing differences in recognising items of income or expenditure as derived or incurred, do not generally give rise to mismatches for the purposes of the anti-hybrid provisions.

In respect of payments under a financial instrument, the test of whether a payment will be made within a reasonable period of time should be based on the terms that might be expected to be agreed between unrelated parties acting at arm's length. If the mismatch is simply the result of a timing difference, the taxpayer may be denied a deduction but should be allowed to take deduction at a later date, when that income is taxed in the other jurisdiction.

Disregarded PEs

As Ireland currently has a worldwide basis of taxation, an Irish company cannot have a disregarded PE elsewhere in the world. The concept of a disregarded PE is not addressed in BEPS Action 2 and so, there is a risk that countries may address the issue in different ways, which could give rise to double taxation.

Ireland's Corporation Tax Roadmap[21] provides that a public consultation will be held on moving to a territorial system of taxation in early 2019. As disregarded PEs would become relevant in the context of an introduction of a branch exemption as part of a potential move to a territorial tax regime, we believe that policymakers should consider whether to introduce defensive rules on disregarded PEs as part of that consultation process.

Institute recommendation:
As disregarded PEs would become relevant in the context of an introduction of a branch exemption as part of a potential move to a territorial tax regime, we believe that policymakers should consider whether to introduce defensive rules on disregarded PEs, as part of the planned consultation process on moving from a worldwide basis of taxation to a territorial tax system, due to be held in 2019.

[21] Government of Ireland, Ireland's Corporation Tax Roadmap, Incorporating implementation of the Anti-Tax Avoidance Directives and recommendations of the Coffey Review, September 2018.

Charge to tax

Where an amount of income would become chargeable to corporation tax in Ireland, because of the application of Irish anti-hybrid rules, such income should be taxed as if that income was earned in Ireland, under the corresponding Case in Schedule D and not solely under Case IV. This option would be consistent with the approach that was recently adopted for charges arising on controlled foreign companies under section 835R (6) TCA 1997.

Institute recommendation:
Where an amount of income would become chargeable to Irish corporation tax in Ireland, because of the anti-hybrid rules, such income should be taxed as if it was earned in Ireland, under the corresponding Case in Schedule D.

Imported mismatches

The imported mismatch rule[22] applies to prevent mismatches between parties in third countries being imported into the EU, using a non-hybrid instrument. The Consultation Paper[23] asks what factors should be considered in relation to the application of the rules to prevent imported mismatches, where an Irish taxpayer is transacting with a person in an EU Member State which has implemented ATAD2.

The imported mismatch rules should not be applied where an Irish taxpayer is transacting with a taxpayer in an EU country. An Irish taxpayer should be entitled to assume that the Member State has implemented ATAD2 properly. The onus cannot be on a taxpayer to determine if a Member State has implemented their obligations under ATAD2. This is a matter which rests solely with the European Commission to undertake infringement proceedings against the relevant Member State.

Applying and monitoring an Irish rule that denied deductions for imported mismatches on payments made to EU recipients would be extremely difficult. ATAD provides that no adjustment is needed if another country adjusts for the mismatch. It is unclear where the adjustment should be made, where there is more than one EU payer in a series of transactions. The preferable approach would be to only apply the provision to payments made to non-EU recipients in order to avoid the risk of double taxation.

Careful consideration should also be given to the meaning of funding (direct and indirect) expenditure involving a hybrid mismatch under the imported mismatch rules. The definition of funding in this context should be narrow to ensure greater certainty in the application of the imported mismatch rules and to prevent any unintended outcomes and double taxation.

[22] Recital 25 of ATAD2

[23] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 13.

Institute recommendation:
The imported mismatch rules should not be applied where an Irish taxpayer is transacting with a taxpayer in an EU country. The onus cannot be on a taxpayer to determine if an EU Member State has implemented their obligations under ATAD2. This is a matter for the European Commission to address.

Dual inclusion income and financial instruments

The purpose of ATAD2 is to neutralise hybrid mismatches as comprehensively as possible.[24] The Directive provides that a double deduction outcome will not arise where there is dual inclusion income.[25] However, ATAD2 does not directly address the concept of dual inclusion income in the context of financial instruments.

We believe that it would be appropriate for the concept of dual inclusion income to be incorporated into the anti-hybrid rules relating to financial instruments in Ireland and that the legislation should confirm that a double deduction would not arise in such circumstances. We believe that such an approach would be in keeping with the stated objective of ATAD2 to neutralise hybrid mismatches, while ensuring proportionality and limiting risk of double taxation. We understand that this approach has been adopted in Belgium.

Institute recommendation:
Irish tax legislation implementing anti-hybrids provisions for financial instruments should include the concept of dual inclusion income and confirm that a double deduction does not arise in such circumstances.

Financial trader exemption

Payments under financial instruments do not give rise to a deduction without inclusion outcome, where the payment is made by a financial trader under an on-market hybrid transfer, provided certain conditions are met.[26] The Consultation Paper[27] asks what factors Ireland should consider when determining whether to apply the deduction without inclusion rules to such trades by financial traders.

We believe that the financial trader exemption should be adopted into Irish tax legislation. The criteria set out in ATAD2, regarding the determination of whether to apply the deduction without inclusion rules to trades by financial traders should be incorporated into the domestic rules (i.e. there must be an on-market hybrid transfer and the payer jurisdiction should require the financial trader to include as income all amounts received relating to the transferred financial instrument.[28])

[24] Recital 5 of ATAD2
[25] Article 9(1) ATAD as amended by ATAD2
[26] Dept. of Finance, ATAD Implementation, Hybrids and Interest Limitation, Public Consultation, November 2018, para. 4.3.8
[27] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 14.
[28] Article 2(9) ATAD as amended by ATAD2

In addition, if it would be appropriate for the results of the trades by a financial trader to be taxed under Schedule D, Case I, this would also be a factor that could determine the application of the exemption for Irish tax purposes.

Institute recommendation:
The financial trader exemption contained in ATAD2 should be incorporated into domestic legislation, together with the determining factors for that exemption which are set out in the Directive.

4.1.3 Definitions

Associated enterprises

The Consultation Paper[29] asks whether the existing control test in section 432 TCA 1997 should be used to determine associated enterprises for the purposes of Irish anti-hybrid rules or whether the concepts of a group under accounting principles in section 7, Companies Act 2014 would be a more appropriate test.

ATAD2 defines an associated enterprise for the purposes of anti-hybrid rules, in addition to the requisite shareholding relationship between the companies, to include entities that are part of the same consolidated group under accounting principles and an enterprise in which a taxpayer has significant influence in the management or vice versa.[30]

It is essential that any proposed definition of associated enterprises to be included in domestic legislation for the purposes of the anti-hybrid rules is workable from a commercial perspective and does not give rise to unintended consequences.

Using a version of section 432 TCA 1997 would introduce concepts, such as participators and associated persons (which can include relatives), that would be inappropriate in the context of the anti-hybrid rules. It would include non-bank lenders and thus would radically extend the scope of the Directive.

Section 432 was specifically drafted for close companies and its purpose is to identify where there are five or fewer "participators" in a company. The definition considers a person to be a participator, even where a person cannot direct how the affairs of a company is carried on. Control for the purposes of the anti-hybrid rules should seek to determine where the ability (directly or indirectly) to control a company lies.

The inclusion of the term participator in the definition of control would mean that loan creditors would be taken into account when considering control. Although there is an exclusion in section 433(6)(b), where a loan is provided by a person carrying on the business of banking, no such exclusion exists for non-bank lenders. Consequently, non-bank lenders would come within the

[29] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 15.
[30] Article 2(4) ATAD as amended by ATAD2

scope of the definition of control, even in circumstances where the finance being provided is on commercial terms.

The purpose of ATAD2 is to neutralise hybrid mismatches, while ensuring proportionality. Restricting the scope of the rules to associated enterprises and structured arrangements reflects efforts made to ensure proportionately. If the section 432 definition is imported into the concept of associated enterprises, it would significantly extend that concept and would most notably include non-bank lenders. This would mean that a loan from a non-bank lender of itself could bring the loan within the scope of ATAD2. Such an outcome would arguably be a disproportionate extension of the scope of the Directive and not intended by ATAD2.

Associated enterprises could be defined by reference to Section 7, Companies Act 2014, which refers to control of the composition of the board of the directors and dominant influence. The definition in Section 7 would be easily understood by companies and would be in line with the guidance provided in ATAD2 regarding the requirement for Member States to have a sufficiently comprehensive definition of an associated enterprise.[31]

Alternatively, it may be preferable to draft a control test based on the wording contained in ATAD2 to define associated enterprises for Irish anti-hybrid provisions.

Institute recommendations:
Using a version of the control test in section 432 TCA 1997 would introduce concepts, such as participators and associated persons that would be inappropriate in the context of the anti-hybrid rules. It would include non-bank lenders, which would radically extend the scope of the Directive.

Associated enterprises could be defined by reference to section 7, Companies Act 2014, which refers to control of the composition of the board of the directors and dominant influence and would be in line with the policy objective of ATAD2.

Clarification on the tax treatment of entities

The Consultation Paper[32] states that in order to apply anti-hybrid rules, taxpayers must have certainty regarding the tax treatment of certain entities. Currently, principles set out in case law are used to determine whether an entity is transparent for tax purposes in Ireland, which can create some uncertainty for taxpayers.

Whilst codification of existing principles may simplify matters, in order to ensure that codification would operate effectively in practice, a meaningful consultation on draft legislation should be undertaken. Such an approach would provide the desired clarity in determining the tax status of entities going forward. However, this approach would undoubtedly present some

[31] Recital 14 of ATAD 2

[32] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 15.

difficulties regarding the potential application of the new rules to existing entities that have been assessed based on principles outlined in case law.

The process of codification of the existing case law principles would take some time to allow for consultation in advance of the enactment of the rules. As an interim measure, we believe that certainty regarding the tax status of an entity could be achieved if the Revenue Commissioners issue a non-exhaustive list of opaque and transparent entities. If an entity is not on the list, then a taxpayer could opt to write to the Revenue to request for the entity to be added to the list or alternatively, a taxpayer could determine the tax status of an entity based on existing principles outlined in case law. This would be similar to the approach adopted by HMRC in the UK.

Institute recommendations:
In order to apply anti-hybrid rules, taxpayers should have certainty regarding the tax treatment of entities. This could be achieved by putting existing case law principles on a legislative footing.

To ensure that codification of existing principles regarding the tax status of an entity will operate effectively in practice, a consultation should take place on draft legislation in advance of enacting the rules. In the interim, Revenue could adopt a practice similar to that in the UK, where they could issue a non-exhaustive list of opaque and transparent entities.

Concept of investor/payee jurisdiction

ATAD2 refers to double deductions as deductions that are available in both the investor jurisdiction and the payer jurisdiction.[33] Deduction without inclusion is defined in the Directive as a deduction in the payer jurisdiction without inclusion in the payee jurisdiction.[34] The Consultation Paper[35] asks whether it would be preferable to have a single concept to encompass both investor and payee when determining if a payment has been deducted and included in income.

For ease of administration, a single concept to determine if a payment has been deducted and included as income would be preferable. However, the key factor that should be considered is whether a payment has been included or not. It may not necessarily be the entity immediately receiving the payment that includes the payment for tax purposes and this should be reflected in the Irish rules. For example, a payment to an US check-the-box entity could be included in the US, rather than in the jurisdiction in which the entity is tax resident, even though it was not the entity that received the payment. This approach would be in keeping with the guidance provided in BEPS Action 2.[36]

[33] Article 2(9) and Articles 9, 9a and 9b ATAD as amended by ATAD2
[34] Article 2(9) and Articles 9, 9a and 9b ATAD as amended by ATAD2
[35] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 15.
[36] OECD (2015), Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 – 2015 Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, Paragraph 86.

As the concepts of investor and payee jurisdiction are very difficult to comprehend, it would be worthwhile to consider these concepts in draft legislation and to 'test' them in practice against various real-life holding structures to ensure no unintended consequences.

Institute recommendation:
For ease of administration, a single concept to encompass both investor and payee when determining if a payment has been deducted and included as income would be preferable. However, in defining an investor or payee, the key factor to be considered is whether a payment has been included or not, as it will not necessarily be the entity who receives the payment that includes the payment as income for tax purposes.

Definition of financial instrument

ATAD2 defines a financial instrument as any instrument that gives rise to a financing or equity return that is taxed under the rules for taxing debt, equity or derivatives under the laws of the payee or payer jurisdiction.[37]

The Consultation Paper[38] asks what rules could be described as Ireland's rules for taxing debt, equity or derivatives and whether existing definitions of "financial assets" within TCA 1997 should be used.

A key requirement for section 110 companies in Ireland is that they can only invest in "qualifying assets", which includes a "financial asset". The definition for "financial asset" in the same section refers to many items including, shares, bonds and other securities, futures, options, swaps, derivatives and similar instruments, etc. Given it is a statutory requirement for section 110 companies to hold or manage qualifying assets, we would recommend that the definition of financial instrument is aligned with the definition of financial asset within the TCA 1997.

Institute recommendation:
We would recommend that the definition of financial instrument for the purpose of the anti-hybrid rules is aligned to TCA 1997.

4.1.4 Transactional knowledge

Structured arrangements and capital market transactions

A structured arrangement will not result in an adjustment under the anti-hybrid rules in circumstances where the taxpayer or an associated enterprise:

(a) could not reasonably have been expected to be aware of the hybrid mismatch; **and**
(b) did not share in the value of the tax benefit resulting from the hybrid mismatch.[39]

[37] Article 2(9) ATAD as amended by ATAD2
[38] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 16.
[39] Article 2(11) ATAD as amended by ATAD2

An Irish taxpayer may inadvertently enter into a structured arrangement. For example, the taxpayer may not know that the value of the hybrid mismatch was priced into the arrangement. Therefore, it is critical that any awareness test should not impose an obligation on a taxpayer to undertake additional due diligence on a commercial transaction over and above what would be expected of a reasonable and prudent person.[40]

Where the interest paid under a loan is significantly below the market rate it may be reasonable to impute awareness. However, where normal commercial market interest is paid under a loan (or indeed interest which is only marginally under normal commercial market interest), it should be reasonable to suppose that the taxpayer was not aware of any hybrid mismatch.

In securitisation transactions, funding is often provided through notes of listed stock exchange entities. A taxpayer may not know the identity of the holder of the debt or their tax profile and therefore, they would not be aware that they are entering into a hybrid transaction. Safe harbour provisions must be included in Irish legislation in order to protect such taxpayers.

We would suggest that an awareness test, similar to that contained in s110(4A)(c) TCA 1997, which applies where the interest or other distribution is paid in respect of a quoted Eurobond or wholesale debt instrument may be appropriate;

> *"at the time the instrument was issued, the qualifying company was in possession, or aware, of information, including information about any arrangement or understanding in relation to ownership of the instrument after that time, which could reasonably be taken to indicate that interest or other distributions which would be payable in respect of that instrument would not be subject, without any reduction computed by reference to the amount of such interest or other distribution, to a tax in a relevant territory which generally applies to profits, income or gains received in that territory, by persons, from sources outside that territory."*

HMRC has also provided useful guidance regarding whether it is 'reasonable to suppose' something regarding the application of the anti-hybrid rules in the UK:

> *"In general terms the test does not require knowledge of the actual outcome or position, but a rational, justifiable and credible view of the likely outcome or position. Whilst it will depend on context, this supposition should be based on facts and circumstances that are either already established, or which might reasonably be expected to be ascertained in considering the application."*[41]

[40] OECD (2015), Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 – 2015 Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, Paragraph 343.
[41] http://www.hmrc.gov.uk/gds/intm/images/INTM850000_hybrids.pdf, pg. 40

Institute recommendations:
The test for borrower knowledge in the context of structured arrangements and capital market transactions must be a high bar. It should not impose an obligation on a taxpayer to undertake additional due diligence on a commercial transaction over and above what would be expected of a reasonable and prudent person.

Safe harbour provisions should be considered for securitisation transactions where funding is provided through notes of listed stock exchange entities.

Test for hybridity
The Consultation Paper[42] asks whether regard should be had to the transaction; the actual circumstances of the taxpayer or the laws of the foreign jurisdiction when assessing hybridity.

In order for there to be certainty regarding the application of the rules, consideration should be given to the laws of the jurisdiction in which the payee/investor is resident or subject to tax. The rules should only apply to the extent that a payee/investor is actually entitled to a deduction for a payment under local law.

This is in keeping with BEPS Action 2[43] , which provides that the rule will not apply to the extent the taxpayer is subject to transaction specific or entity specific rules that prevent the payment from being deducted. This approach should be adopted for both hybrid financial instruments and disregarded hybrid payments.

Institute recommendation:
For there to be certainty regarding the application of the anti-hybrid rules, consideration should be given to the laws of the jurisdiction in which the payee/investor is resident or subject to tax. The rules should only apply to the extent that a payee/investor is actually entitled to a deduction for a payment under local law.

4.1.4 Interaction with domestic provisions

Existing domestic provisions
In order to provide certainty for business and to ensure Ireland remains an attractive location for investment, it is important that our rules are clear and do not result in double taxation. The application of new anti-hybrid rules with existing anti-avoidance provisions contained within sections 110, 130 and 247 TCA 1997 could result in double taxation, if those sections are not amended, when implementing the new provisions.

[42] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 18.
[43] Paragraphs 35 and 122, Action 2, 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing Paris

Therefore, it is critical that all stakeholders are given the opportunity to consult well in advance on draft legislation to ensure the technical operation of the anti-hybrid rules in practice do not create any unintended consequences when interacting with existing domestic provisions.

Institute recommendation:
It is critical that all stakeholders are given the opportunity to consult well in advance on draft legislation to ensure the technical operation of the anti-hybrid rules in practice do not create any unintended consequences, when interacting with existing domestic provisions

Treatment of disallowed payments

The Consultation Paper[44] asks whether adjustments under anti-hybrid rules should cause payments to be treated as distributions or simply as non-deductible expenses. Any adjustments made by an Irish taxpayer because of the application of the anti-hybrid rules should be treated as non-deductible expenses.

If an anti-hybrid adjustment was treated as a distribution, it could result in additional administrative issues including for example, the application of dividend withholding tax. It would be a matter then for the foreign jurisdiction to determine whether the payment gives rise to a distribution under the laws of that territory.

Institute recommendation:
Any adjustments made by an Irish taxpayer because of the application of the anti-hybrid rules should be treated as non-deductible expenses.

Order of application of rules

The BEPS Action 2 2015 Report[45] includes a detailed outline of the order of application of the anti-hybrid rules, a copy of which is set out at Appendix 1. We would recommend that Ireland should follow the order outlined in BEPS Action 2 when implementing the anti-hybrid rules in ATAD and ATAD2.

Institute recommendation:
We recommend that Ireland follows the order of application outlined in BEPS Action 2 when implementing the anti-hybrid rules in ATAD and ATAD2.

Removing domestic hybridity

Existing domestic provisions that would need to be reviewed to ensure that they are not regarded as hybrid entities by other foreign jurisdictions, include those dealing with Approved Retirement Funds, Unit Trusts and Irish Collective Asset Management Vehicles (ICAV's).

[44] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 20.
[45] OECD (2015), Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 – 2015 Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris

Stock lending and repo transactions

It might be useful to put existing tax treatment of stock lending and repo transactions that is currently set out in Revenue guidance[46] on a legislative footing. However, it would be important to consider legislating for all types of stock lending and repo transactions and not just for those transactions where the transfer is for periods of less than 12 months, which are referred to in the guidance, as these would be a relatively small portion of such transactions.

As this may be a considerable task to undertake, the administrative guidance could note in the interim that if a taxpayer follows the guidance, the ancillary consequence could be that it would be regarded as interest for the purposes of anti-hybrids and interest limitation rules in ATAD and ATAD2.

Leases

In relation to leases, clarification will be needed for finance leases to ensure that no mismatch will arise where the financing element of a lease rental deductible by the lessee is taxed as the ordinary income of the lessor.[47]

Institute recommendation:
Irish tax legislation could be amended to reflect the existing tax treatment of stock lending and repo transactions that is currently set out in Revenue guidance. However, it would be important to consider legislating for all types of stock and repo transactions and not just those transactions where the transfer is for periods of less than 12 months, which are referred to in the guidance, as these would be a relatively small portion of such transactions.

Islamic Financing

The provisions in Part 8A TCA 1997 treat the return arising on a specified financial transaction (i.e. Islamic financing/Sharia compliant transactions) as interest for tax purposes and applies all relevant tax legislation regarding interest to that return. The legislation does not change the nature of the financial arrangements.

However, the application of anti-hybrid rules to Islamic financing transactions could result in a hybrid mismatch because interest is not allowed under an Islamic GAAP system. Instead, the interest is rolled up into the loan. This would create either non-inclusion or a timing mismatch between the Irish deduction and the taxable period for the counterparty in the Islamic country.

In our view, sharia compliant transactions should be treated as "financial instruments" for the purposes of anti-hybrid provisions in Ireland. Even though such transactions would expressly come within the terms of the Directive, they should not require adjustments to be made under the rules, given the hybridity of the transaction would be directly related to timing differences (i.e. the rolling up of interest), which are not considered a mismatch in a tax outcome under ATAD2.

[46] Revenue Commissioners, Tax and Duty Manual, Part 04-06-13, Tax treatment of stock lending/sale and repurchase (repo) transactions.

[47] Example 1.25, Action 2, 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing Paris. Recital 28 of ATAD 2 suggests that Member States should use the explanations and examples provided in the OECD report

Institute recommendation:
In our view, sharia compliant transactions should be treated as "financial instruments" for the purposes of anti-hybrid provisions in Ireland. However, such transactions should not require adjustments to be made under the rules, given the hybridity of the transaction would be directly related to timing differences, which are not considered a mismatch in a tax outcome under ATAD2.

4.1.5 Reverse Hybrids

The reverse hybrid rule
The Consultation Paper[48] asks whether it would it be reasonable to use the same "subject to tax" definition for reverse hybrids as for all other hybrid mismatches.

The rationale for the use of a separate "subject to tax" rule for reverse hybrids is unclear. We would suggest that this matter be considered as part of a public consultation on reverse hybrids, before the implementation of those rules by 31 December 2021.

Collective Investment Vehicles
As outlined in section 4.1.1, collective investment vehicles are not subject to corporation tax and therefore, should be outside the scope of Ireland's anti-hybrid regime. Ireland should not apply the reverse hybrid rule to these vehicles as permitted under ATAD2.[49]

Consideration should also be given to extending this exclusion to all subsidiaries of regulated entities, as these subsidiaries would be effectively subject to the same Central Bank of Ireland regulatory requirements as the regulated entity (its parent), such as having common directors and restrictions over the types of assets invested.

Institute recommendations:
The rationale for the use of a separate "subject to tax" rule for reverse hybrids is unclear. We would suggest that this matter be considered as part of a public consultation on reverse hybrids, before the implementation of those rules before 2022.

Ireland should not apply the reverse hybrid rule to collective investment vehicles as permitted under ATAD2.

[48] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 22.
[49] Paragraph (2) of Article 9, ATAD2

4.2 Interest Limitation Rules

ATAD requires EU Member States to introduce ratio-based interest limitation rules, designed to limit the ability to deduct borrowing costs when calculating taxable profits. The rules are intended to prevent the use of excessive interest payments as a means by which base erosion and profit shifting (BEPS) by multinational companies can occur.[50] The interest limitation rules in ATAD operate by limiting the allowable tax deduction for net interest costs in a tax period to 30% of Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA).

The general implementation date for the ATAD interest limitation rules was 1 January 2019. However, Article 11 of ATAD provides for a derogation from this implementation deadline until 1 January 2024, for EU countries that have national targeted rules, which are equally effective as the ATAD interest limitation rule.

On 22 June 2016, the Department of Finance released a statement which confirmed that, *"the provisions on interest deductions are deferred until 2024 for countries, like Ireland, that already have strong targeted rules. There are also strong grandfathering provisions to provide certainty to investors"*[51]

Subsequently, the Irish Government notified the European Commission that Ireland's existing interest limitation rules are at least as equally effective as the rules contained in ATAD in order to avail of the derogation.

However, in September 2018, Ireland's Corporation Tax Roadmap[52] indicated for the first time that Ireland might introduce the ATAD EBITDA ratio rule before 2024, as *"it is yet unclear that agreement will be secured in relation to the derogation."* The Roadmap also confirmed that matters relating to interest limitation would be considered as part of the public consultation on hybrid mismatches.

4.2.1 Scope of interest limitation rules

Application to groups

The Consultation Paper[53] queries whether Ireland should implement the new interest limitation ratio rules in a manner that would allow application of the rules on a local group basis. Article 4(1) of ATAD allows the interest restriction to be applied at a group level or on a company by company basis.

[50] 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.

[51] https://merrionstreet.ie/MerrionStreet/en/News-Room/Releases/Minister_Noonan_welcomes_agreement_on_the_Anti-Tax_Avoidance_Directive.html#sthash.l3szqoph.dpuf

[52] Ireland's Corporation Tax Roadmap, Incorporating implementation of the Anti-Tax Avoidance Directives and recommendations of the Coffey Review, Department of Finance, September 2018, page 21

[53] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 24.

We believe the Irish legislation should provide taxpayers with the flexibility to decide whether to apply the rules at an individual or at a group level. It will be necessary to have some flexibility for groups within Irish tax legislation to ensure that Ireland would not be less competitive than countries with fiscal consolidation.

Applying the interest restriction on a group basis would ensure the allocation of interest would not be restricted to one member of the group and could be carried forward and used by another group member if required.

The Consultation Paper also asks what practical issues might arise in applying the ATAD EBITDA ratio rules, in terms of allocating the allowable quantum of interest deductions to group members. In our view, once the deductible interest for the group is calculated, a local group should have full discretion as to how the interest amount is allocated between the various members of the group. If a company joins or if there is a potential disposal of a company, then an adjustment should be made on a time-apportioned basis.

Members of a group should be required to align their accounting periods and therefore, would have corresponding tax periods.

Institute recommendation:
Irish tax legislation should allow taxpayers the flexibility to decide whether to apply the interest limitation ratio rule at an individual or at a group level. Once the deductible interest for a group is calculated, a local group should have full discretion as to how the interest amount is allocated between the various members of the group.

Definition of 'group'

The Consultation Paper asks how a 'group' should be defined for the purposes of implementing the interest limitation ratio rules and whether a local group should include those members of a consolidated group that are within the charge to Irish corporation tax or if other criteria should apply for determining the existence of a group. We have set out our view of the relevant considerations in the context of the anti-hybrid rules at section 4.1.3 of this submission and we believe that the similar considerations apply in the context of the interest limitation rules.

De Minimis threshold

Under ATAD, Member States can allow a taxpayer to deduct their net interest costs (i.e. exceeding borrowing costs) in full, where the exceeding borrowing costs do not exceed a *de minimis* threshold of up to €3 million. Where the fixed ratio rule applies on a group basis, the *de minimis* threshold of up to €3 million applies to the entire group.

Ireland should include the *de minimis* threshold of €3 million for exceeding borrowing costs permitted under ATAD when implementing the interest limitation rules in Ireland. Not including the *de minimis* threshold would impose a significant administrative burden on entities and groups with relatively low borrowings, that provide relatively limited BEPS risks. Such an approach might be regarded as disproportionate.

Institute recommendation:
Ireland should include the *de minimis* threshold of €3 million for exceeding borrowing costs permitted under ATAD when implementing the ATAD interest limitation rule in Ireland

Standalone entities

Under ATAD, a taxpayer can fully deduct their exceeding borrowing costs where the taxpayer is a standalone entity (i.e. an entity that is not included in a group's consolidated financial accounts and has no associated enterprise or permanent establishment.)[54]

It is essential that the term 'standalone entity' is implemented in manner that will work in practice and take account of entities that are legally remote (i.e. orphan entities). It should also reflect that under Irish company law, it is not possible to establish a company with no shareholder. Consequently, the only way to establish a 'standalone entity' under Irish company law is to use a nominee shareholder who holds the shares on trust but has no beneficial ownership or economic interest in the company.

There are many valid commercial reasons for using an orphan structure in a jurisdiction. For example, where bankruptcy remoteness is a concern, such as cases where a rating agency requires it. Similarly, securitisations by banks can be orphaned for regulatory capital reasons or where there is a diverse group of investors, with no single investor being permitted to have voting control of the entity. Certain parties, such as the European Central Bank, may also require orphaning.[55]

The nominal shares in an orphan entity are often held by a company on trust. As a result, the company which holds such shares on trust might be an 'associated enterprise' of the orphan entity, even though the company may have no economic participation in the orphan entity.

It would be important that the definition of a standalone entity for the purposes of the interest limitation rules could include such orphan entities. Otherwise, the debt equity ratio of an orphan entity, whose nominal shares are held on trust, could completely distort the ratio for the consolidated group, as a result of a technical association with the nominal shareholder, which would not reflect the economic reality of the situation.

Interestingly, orphan entities are not included as part of a fiscal consolidation group in Germany and therefore, are not relevant for the purposes of their interest limitation rule; rules which formed the basis for the ATAD EBITDA ratio rule.

Institute recommendation:
The definition of 'standalone entity' must be implemented in a manner that will work in practice and should include entities that are legally remote (i.e. orphan entities).

[54] Article 4(3) ATAD

[55] Revenue Commissioners, Tax and Duty Manual, Part 04-09-01, Section 110: entitlement to treatment, para. 4.8

Pre-existing loans

ATAD provides that Member States can choose not to apply the interest restriction to loans entered before 17 June 2016.[56] All existing loans entered before 17 June 2016 should be excluded from interest limitation rules in Ireland. Grandfathering of pre-17 June 2016 loans should not be lost where there is a small technical amendment to the loan that does not alter the commercial features of the loan, such as the principal amount, interest rate or maturity. Further drawdowns of principal amounts on loans agreed before 17 June 2016 should not result in grandfathering being lost.

On 22 June 2016, the Irish Government confirmed that the provisions of the ATAD relating to interest limitation would not come into effect in Ireland until 2024 and that pre-existing loans would be grandfathered. [57] Subsequently, the Government confirmed it had notified the European Commission that Ireland's existing interest limitation rules were at least equally effective as the rules contained in ATAD.

Companies have entered into commercial agreements since 22 June 2016 in good faith on the basis that the ATAD interest limitation measures would not take effect in Ireland until 1 January 2024.

If the Government plans to introduce ATAD interest limitation rules before 2024, this should be confirmed as soon as possible, together with a clear announcement confirming the existing understanding on grandfathering. This is critical so that businesses have the necessary certainty regarding the tax consequences of arrangements that they have entered into and are contemplating now.

Institute recommendations:

All existing loans entered before 17 June 2016 should be excluded from interest limitation rules in Ireland, as permitted under ATAD.

Irish legislation should clarify that the 'grandfathering' provisions will not be lost because of a technical amendment to a pre-existing loan, which does not alter the commercial features of it.

If the Government plans to introduce ATAD interest limitation rules before 2024, this should be confirmed without delay, together with a clear announcement given on grandfathering. This is critical so that businesses have the necessary certainty regarding the tax consequences of arrangements that they have entered into and are contemplating now.

[56] Article 4(4) ATAD

[57] https://merrionstreet.ie/MerrionStreet/en/News-Room/Releases/Minister_Noonan_welcomes_agreement_on_the_Anti-Tax_Avoidance_Directive.html#sthash.l3szqoph.dpuf

Long-term infrastructure

EU Member States can decide not to apply the interest restriction to certain loans used to fund long-term infrastructure projects, which include projects to provide, upgrade, operate and/or maintain a large-scale asset that are considered in the general public interest.[58]

In our view, the legislation should include an exclusion from the application of interest restrictions to loans used to fund long-term infrastructure projects. Generally, long-term infrastructure investment by companies can result in increased growth and employment and the interest costs associated with that investment are often simply costs incurred for expanding a business and are not tax motivated.

There are a whole range of projects which should be considered long-term infrastructure projects for the general public interest, e.g. utilities, broadband, hospitals. Therefore, the definition should not be limited to public private partnership projects. Projects should be considered for the general public interest irrespective of whether they are privately owned or whether a fee is charged to the public for their use.

In addition, ATAD is clear that the project may be located in any EU Member State and is not confined to Ireland. This should also be reflected in the domestic provisions.

Institute recommendations:

The definition of long-term infrastructure should not be confined to public private partnership projects. Projects should be considered for the general public interest irrespective of whether they are privately owned or whether a fee is charged to the public for their use.

In addition, the infrastructure project may be located in any EU Member State and should not be confined to Ireland.

Consolidated group ratio rule

The Consultation Paper[59] queries what factors need to be considered in determining which consolidated group ratio rule should be implemented in Ireland, (i.e. the equity to assets rule or the consolidated group's external borrowings to EBITDA ratio rule). The Consultation Paper states that only one of the rules may be implemented.

It is our view that Ireland can potentially adopt both rules as ATAD gives the taxpayer (rather than the EU Member State) the option to choose between either of the two consolidated group ratio rules.[60] Companies, depending on their industry, may prefer one rule to the other. If it is not possible to implement both tests into Irish law, the second option would be preferable (i.e. the consolidated group's external borrowings to EBITDA ratio rule) based on the feedback from our members.

[58] Article 4(4) ATAD

[59] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 26.

[60] Article 4(5) ATAD

Institute recommendation:
If it is not possible to implement both tests for the consolidated group ratio rule into Irish law, then Ireland should adopt option (b), the consolidated group's external borrowings to EBITDA ratio rule.

The Consultation Paper[61] asks what factors should be considered in determining whether to apply the interest restriction to financial undertakings and whether the exemption should apply only to regulated financial undertakings.

In practice, groups that contain financial undertakings generally include both regulated and unregulated entities. Companies within such a financial services group generally provide services that are ancillary to the regulated business, including raising regulatory capital, and are overall subject to the same regulatory capital and solvency requirements that apply on a consolidated basis to the entire group. These restrictions, which apply to all members as a result of having a regulated entity in the group, mean that there is a reduced risk of base erosion arising from excessive interest deductions. Therefore, groups containing financial undertakings should be exempt from the interest limitation restrictions.

If it is not possible to extend the exemption for financial undertakings to the entire group, then a financial undertaking should have an option to avail of the exemption. Failure to provide an opt-in clause could result in groups containing financial undertakings being adversely impacted from an automatic exclusion of the financial undertaking from the interest limitation rules.

In our view, there is no basis for treating regulated and non-regulated entities differently where the services provided are similar. Therefore, we believe all non-regulated undertakings providing the same services as regulated undertakings should be able to avail of the financial undertaking exemption. Notably, Revenue's guidance on debt issuance defines 'financial institution' for the purposes of that manual as including a leasing company.[62]

Institute recommendations:
Groups containing financial undertakings should be exempt from the interest limitation restrictions. If it is not possible to extend the exemption for financial undertakings to the entire group, then a financial undertaking should have an option to avail of the exemption. Failure to provide an opt-in clause could result in groups containing financial undertakings being adversely impacted from an automatic exclusion of the financial undertaking from the interest limitation rules.

Non-regulated undertakings providing the same services as regulated financial undertakings should be able to avail of the financial undertaking exemption.

[61] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 26.
[62] Revenue Commissioners, Tax and Duty Manual, Part 04-06-21, Tax Treatment of Debt Issuance Costs, para. 3.1

Carry forward

Three policy options are set out under ATAD for the carry forward of unutilised interest relief by a taxpayer. Member States must choose which of the three options to implement.[63]

The three options are:

(a) to carry forward, without time limitation, exceeding borrowing costs which cannot be deducted in the current tax period;

(b) to carry forward, without time limitation, and back, for a maximum of three years, exceeding borrowing costs which cannot be deducted in the current tax period;

(c) to carry forward, without time limitation, exceeding borrowing costs and, for a maximum of five years, unused interest capacity, which cannot be deducted in the current tax period.

In our view, Option C should be implemented into Irish legislation.

In addition, consideration could be given in cases of cessation to allow unutilised interest relief to form part of a claim for terminal loss relief under section 397 TCA 1997. Terminal loss relief permits a loss incurred in the last 12 months of a discontinued trade, insofar as it cannot be otherwise relieved, to be carried back and set against the trading income of the same trade in the three preceding years.

Institute recommendations:

Option C should be implemented into Irish legislation, i.e. to carry forward, without time limitation, exceeding borrowing costs and, for a maximum of five years, unused interest capacity, which cannot be deducted in the current tax period.

Consideration could be given in cases of cessation, to allow unutilised interest relief to form part of a claim for terminal loss relief under section 397 TCA 1997.

4.2.2 Definitions

Borrowing costs and exceeding borrowing costs

The Consultation Paper[64] queries what factors should be considered in defining borrowing costs in Irish law and the types of income/expenses that should be treated as economically equivalent to interest for the purposes of the interest limitation rules.

[63] Article 4(6) ATAD

[64] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 28.

A detailed definition of borrowing costs is set out in ATAD, which includes costs 'economically equivalent to interest' and expenses incurred in connection with the raising of finance as defined in national law.[65]

The definition of borrowing costs is critical and should consider the specific circumstances of the taxpayer, as a borrowing cost for one taxpayer may not necessarily be a borrowing cost for all taxpayers.

Other factors that need to be considered include differences between the accounting treatment of borrowing costs and the tax treatment (e.g. the cost of borrowing could be attributable to reserves rather than treated as an expense in the profit and loss account) and the impact of exchange rate losses on interest costs.

A broad view should be taken of what types of income/expenses should be treated as 'economically equivalent to interest'. It should include interest on all acceptable debt under generally accounting principles, leasing income and items, such as interest and dividends on redeemable shares.

The impact of IFRS 16 on the accounting treatment of leases also needs to be considered. If leasing income is not treated as economically equivalent to interest, then leasing companies could be negatively impacted by the interest limitation rule. It may be preferable for the definition of interest to be linked to the type of business being carried on.

Given the broad range of the type of income/expenses that could potentially be treated as economically equivalent to interest and the different circumstances of the taxpayer, it may be preferable to transpose the definition set out in ATAD into Irish law. The definition contained in the legislation could be supported by Revenue guidance regarding the scope of the term.

Significant work has been carried out in establishing an EU Capital Markets Union, which seeks to improve the availability of and access to financing for businesses and infrastructure across the EU. Our securitisation industry has played a significant role in this work.

Section 110 TCA 1997 was initially introduced to promote securitisation for the financial sector operating within Ireland and was designed as a tax neutral regime for securitisation transactions.[66] It is vital, when applying the new interest limitation rules, to ensure that the classification of income of securitisation vehicles reflect the economic reality of the transactions undertaken. Therefore, all income of a section 110 company should be considered economically equivalent to interest for the purposes of the ATAD interest limitation rule.

In addition, aircraft lessors should not be disproportionately impacted by the new provisions. To the extent lessors are not treated as an exempt "financial institution", leasing income should be considered economically equivalent to interest for the purposes of the new provisions.

[65] Article 2(1) ATAD

[66] Revenue Commissioners, Tax and Duty Manual, Part 04-09-01, Section 110: entitlement to treatment, page 3

Revenue's guidance on the tax treatment of debt issuance costs[67] provides that leasing companies will be treated as financial institutions for the purposes of that guidance.

Institute recommendations:
Given the broad range of the type of income/expenses that could potentially be treated as economically equivalent to interest and the different circumstances of the taxpayer, it may be preferable to transpose the definition set out in ATAD into Irish law. The definition contained in the legislation could be supported by Revenue guidance regarding the scope of the term.

All income of a section 110 company should be considered economically equivalent to interest for the purposes of the ATAD interest limitation rule.

To the extent lessors are not treated as an exempt "financial institution", leasing income should be considered economically equivalent to interest for the purposes of the new provisions.

EBITDA

The Consultation Paper[68] asks what should be considered when defining EBITDA in Irish tax legislation, particularly in relation to the application of the interest restriction on a group basis.

In our view, Ireland could follow the OECD approach to define EBITDA as taxable income, with net interest expense and capital allowances added back. BEPS Action 4 provides that "*as a starting point group EBITDA should be profit before tax plus net third party interest expense, depreciation and amortisation (including impairment charges).*" [69] Interestingly, the starting point to arrive at EBITDA under the interest limitation rules in both France and the US, is taxable income, as this approach takes account of most of the necessary adjustments and other timing differences.

If a company within a group has a negative EBITDA, this should be treated as zero for the purposes of calculating the overall group EBITDA or alternatively, it should be excluded from the EBITDA calculation entirely and be dealt with on a solo basis.

Institute recommendations:
In our view, Ireland could follow the OECD approach to define EBITDA, as taxable income, with net interest expense and capital allowances added back.

If a company within a group has a negative EBITDA, this should be treated as zero for the purposes of calculating the overall group EBITDA or alternatively, it should be excluded from the EBITDA calculation entirely and be dealt with on a solo basis.

[67] Revenue Commissioners Tax and Duty Manual, Tax Treatment of Debt Issuance Costs, Part 04-06-21.
[68] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 28.
[69] OECD (2017), Limiting Base Erosion Involving Interest Deductions and Other Financial Payments, Action 4 - 2016 Update: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, page 63, paragraph 141.

Exempt income

The Consultation Paper[70] asks whether foreign dividends that are fully sheltered from Irish corporation tax by double tax relief should also be treated as 'exempt' and therefore, excluded from EBITDA.

Foreign dividends are generally taxable in Ireland except for certain foreign dividends set out in section 21B TCA 1997. Under section 21B, the rate of corporation tax applicable to the dividend may also be subject to an election.

Several factors influence the final taxable income and corporation tax due on a foreign dividend, such as the rate of tax and available reliefs (e.g. expenses of management, interest as a charge). Such reliefs apply to foreign dividends in a similar way to income that is not trading income. Relief may also be available for withholding taxes and taxes equivalent to corporation tax on the underlying profits from which the dividend is paid.

In view of the broad range of potential reliefs that can apply to a foreign dividend, which vary between taxpayers, it would be challenging to devise a general rule that might operate to exclude a foreign dividend. Therefore, foreign dividends that remain subject to corporation tax in Ireland should be included in EBITDA.

If Ireland moves to a territorial tax system, which includes a foreign dividend exemption regime, it would be appropriate then for such tax-exempt dividends to be excluded from the measure of EBITDA.

Institute recommendations:

In view of the broad range of potential reliefs that can apply to a foreign dividend in Ireland, which vary between taxpayers, it would be challenging to devise a general rule that might operate to exclude a foreign dividend. Therefore, foreign dividends that remain subject to corporation tax in Ireland should be included in EBITDA.

If Ireland moves to a territorial tax system in the future, which includes a foreign dividend exemption regime, it would be appropriate then for such tax-exempt dividends to be excluded from the measure of EBITDA.

4.2.3 Interaction with domestic provisions

Scheme of relief for interest

The Consultation Paper[71] asks how the interest limitation provisions in ATAD should interact with existing interest deductibility provisions in Irish tax legislation.

[70] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 28.

[71] Department of Finance, ATAD Implementation – Hybrids and Interest Limitation, Consultation Paper, November 2018, Page 29.

We believe that there should be a reconstruction of Ireland's existing rules on interest deductibility in parallel with the implementation of new ATAD compliant interest limitation rules in the tax code, together with any other potential policy changes on transfer pricing. The implementation of the ATAD EBITDA ratio rule cannot be considered in isolation. If the new provisions are layered onto the existing interest deductibility and anti-avoidance provisions contained in sections 130, 247 and 249 TCA 1997, it would render our tax code unworkable and overly complex.

In our view, the updated provisions in the corporate tax code 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 247/249 TCA 1997.

Retaining two separate interest limitation regimes would make Ireland very uncompetitive for inward investment, compared with other jurisdictions and would likely increase the cost of borrowing for Irish businesses. By comparison, both Germany and the UK operate straightforward EBITDA based interest limitation regimes.

However, as Ireland has differing rules for trading and non-trading activities, a legislative basis for claiming a tax deduction for interest arising in a non-trading context will need to be established within the Irish tax code, in conjunction with the removal of section 247 TCA 1997.

Preserving some of the targeted measures within the existing legislation, such as bond-washing or interest on capital gains, could be considered by policymakers to address any concerns they may have regarding the removal of the protections contained within the existing tax code for the deductibility of interest.

The interest limitation rules in the UK include a proviso that the interest must not arise from a loan relationship which has an 'unallowable purpose'. An 'unallowable purpose' is defined to include a purpose which is not amongst the business or other commercial purposes of the company.[72]

In addition, consideration should be given to removing the existing provisions that impose withholding tax on interest, as they are rarely applied in practice and many Members States, including Germany and France, do not impose withholding tax on interest.

Given the Government's stated position from the outset when the Directive was agreed, that our existing interest deductibility rules are equally effective to those contained in ATAD, our existing domestic legislation needs to be fundamentally reformed.

However, any early adoption of the interest restrictions under ATAD should take place no earlier than 2021 because there will be a great deal for taxpayers to absorb and undoubtedly,

[72] Section 442 Corporation Tax Act 2009

businesses will need time to put the necessary systems in place to carry out the required calculations.

Institute recommendations:
We believe that there should be a reconstruction of Ireland's existing rules on interest deductibility in parallel with the implementation of new ATAD compliant interest limitation rules in the tax code.

In our view, the reformed corporate tax code 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 247/249 TCA 1997.

However, any early adoption of the interest restrictions under ATAD should take place no earlier than 2021 because there will be a great deal for taxpayers to absorb and undoubtedly, businesses will need time to put the necessary systems in place to carry out the required calculations.

Appendix 1

Table 1: OECD Action 2 Recommendations

Recommendations	Mismatch Type	Recommended Order
1. Hybrid Financial Instrument	D/NI	Recommendation 1
3. Disregarded hybrid payments	D/NI	Recommendation 4 and 3
4. Reverse Hybrid	D/NI	Recommendation 8
6. Deductible hybrid payments	DD	Recommendation 6 and 7
7. Dual Resident payer	DD	
8. Imported mismatch rule	Indirect D/NI	

Table 2: Outlines the ATAD rules and their closest BEPS Action 2 equivalent

ATAD Rules	Mismatch Type	OECD Equivalent
Article 9(1) DD Rule	DD	No. 6
Article 9(2) D/NI Rule	D/NI	No. 1, 3 and 4
Article 9(3) Imported Mismatch Rule	Indirect D/NI	No. 8
Article 9(5) Disregarded PE Rule	D/NI	N/A (No. 4. Reverse Hybrid rule is the closest in principle)
Article 9(6) Proportional WHT Credits	D/NI	No. 1
Article 9a Reverse Hybrid	D/NI	No. 4
Article 9b Tax residency mismatch	DD	No. 7

Table 3: Recommended order

Recommended order	OECD Equivalent	Comments
Article 9(6) Proportional WHT Credits	1. Hybrid Financial Instrument	Art 9 (6) is comparable to parts of Recommendation 1. Applying Art 9(6) is consistent with the OECD order. We do not anticipate any issues from applying this rule first.
Article 9a Reverse Hybrid	4. Reverse Hybrid	As stated above the OECD would recommend that the Hybrid Financial Instrument Rule apply prior to a Reverse Hybrid Rule. However, ATAD2 suggest it should be applied first, and if the reverse hybrid rule is applied no further adjustments should be applied. BEPS Action 2 suggests that a reverse hybrid mismatch is unlikely to occur if a hybrid financial instrument is used. As such, Recommendation 1 and Recommendation 4 likely to operate separately and the relevant order of applying the two rules is not important. Further, should the hybrid entity receive payment from a hybrid financial instrument, it is unlikely to have received income from the instrument. Consequently, the arrangement would not be subject to an adjustment under Article 9a. The arrangement could then still be subject to and adjustment under the other rules.
Article 9(5) Disregarded PE Rule	N/A	The principles of applying Article 9(5) are sufficiently similar to Article 9a. Therefore, the rule can be applied in the same order as Article 9a.
Article 9 (2) D/NI Rule	1. Hybrid Financial Instrument 3. Disregarded hybrid payments	Applying Article 9(2) next would be consistent with the OECD guidance. However, OECD Recommendation 1 (hybrid financial instrument) is suggested to apply prior to Recommendation 3 (disregarded hybrid payment). Article 9(2) effectively combines the two recommendations. To the extent an arrangement is both a hybrid financial instrument (i.e. Article 2(9)(a)) and a disregarded hybrid payment (i.e. Art 2(9)(f)) it is unclear in ATAD how Article 9(2) should apply. This is relevant as under a disregarded hybrid payment (i.e. Article 2(9)(f)), the hybrid mismatch is limited to the

		extent that the payer jurisdiction allows the deduction to be set off against an amount that is not- dual-inclusion income.
Article 9(3) Imported Mismatch Rule	8. Imported mismatch rule	Consistent with OECD guidance.
Article 9(1) DD Rule	6. Deductible hybrid payments	Consistent with OECD guidance.
Article 9b Tax residency mismatch	7. Dual Resident payer	Consistent with OECD guidance.