TAXE Committee : Country specific fact sheet
Ireland

Roadmap for Green delegation

Key data

- Standard corporate income tax rate is quite low (12,5%). The rate has been unchanged for 12 years now.
- double Irish scheme (company registered in Ireland but not Irish tax resident, e.g. Apple) to be phased out from 1 January 2015, but said to be replaced by IP box regime
- A very low IP box tax rate is envisaged → 5% (which would be the lowest in the EU with Netherlands)
- A 25% credit on incremental R&D spending over the base year of 2003; total effective tax deduction of 37.5%
- double taxation agreements with 68 countries, almost all treaties provide for <u>nil withholding tax neither on interest nor on dividends</u> (result: <u>double non-taxation)</u>
- Ability to carry out investment management activities for non-Irish investment funds without creating a taxable presence in Ireland for such funds.

1) Irish rulings : Rotten Apple

Apple is the world's biggest public company. Analysts say its market value is over $750 billion.
The company settled in Ireland in 1980 and has enjoyed a very low tax-rate ever since. It was evidenced by the former Apple tycoon at the time, Mr. Del Yocam who stated : "*There were tax concessions for us to go there*"
The effective tax rate that Apple has paid was well under the - already low - regular corporate income tax rate of 12,5%

How did this occur ?

Answer : Rulings.

Rulings were granted to Apple by the Irish Tax office (Revenue) in 1991 and 2007.
These rulings have been granted to Apple by the Irish Tax Authorities on an <u>individual</u> and <u>discretionary</u> basis.
They are not formally named as rulings but rather as "<u>opinions</u>" and <u>although they are not legally binding</u>, they are usually <u>not challenged by the Revenue office</u>. The procedure is therefore not formalized.
They dealt with the calculation of the taxable profit allocated to the Irish branches of Apple Sales International and of Apple Operations Europe.
By approving the calculation and scheme submitted by Apple, <u>the Irish Tax Administration reduced effective taxation to a rate well under the 12,5% normal rate</u>.

Estimates vary around a 2% effective tax rate.
Not to mention that Apple previously benefited of a tax holiday until 1990 until the European Community banned it.
The measure allowed Apple to pay $ 500,000 in income tax on profits of $317 million, a rate of 0.2 percent.

→ It is the ban of the tax holiday that motivated the 1991 ruling.

The Commission formally opened a State-Aid case in 2013. It is still investigating and analysing Ireland's replies.
However, the Commission's preliminary views in its Statement of objections released on 11 June 2014 leave no room for doubt:

> *"The Commission's preliminary view is that the tax ruling of 1990 (effectively agreed in 1991) and of 2007 in favour of the Apple group constitute State aid according to Article 107(1) TFEU. The Commission has doubts about the compatibility of such State aid with the internal market. The Commission has therefore decided to initiate the procedure laid down in Article 108(2) TFEU with respect to the measures in question."*

A 2013 US Senate Committee hearing found that the key Apple affiliate, Apple Sales International (ASI), was not a tax resident anywhere and said Apple's taxable profits in Ireland had been calculated "in such a way as to produce an effective rate in the low single digits". This assessment corroborates the 2% effective tax rate estimate.

The company itself has started to realize the seriousness of the charges against it in a recent regulatory filing to the US Securities and Exchange Commission reporting that :

> "*On June 11, 2014, the European Commission issued an opening decision initiating a formal investigation against Ireland for alleged state aid to the Company. The opening decision concerns the allocation of profits for taxation purposes of the Irish branches of two subsidiaries of the Company. The Company believes the European Commission's assertions are without merit. If the European Commission were to conclude against Ireland, the European Commission could require Ireland to recover from the Company past taxes covering a period of up to 10 years reflective of the disallowed state aid. While such amount could be material, as of March 28, 2015 the Company is unable to estimate the impact.*"

The US Senate committee went even farther in establishing Apple Sales International (ASI) precise effective tax rate based on Apple Consolidating Financial Statements and the figures are absolutely stunning going far beyond the 2% estimation :

Global Taxes Paid by ASI, 2009-2011

	2011	2010	2009	Total
Pre-Tax Earnings	$ 22 billion	$ 12 billion	$ 4 billion	$ 38 billion
Global Tax	$ 10 million	$ 7 million	$ 4 million	$ 21 million
Tax Rate	0.05%	0.06%	0.1%	0.06%

Source: Apple Consolidating Financial Statements, APL-PSI-000130-232 [Sealed Exhibit]

These figures demonstrate that Ireland has essentially functioned as a tax haven for Apple, providing it with minimal income tax rates approaching zero.

On a three-year period, the maximum effective tax rate for ASI was 0,1% paid on its earnings.
Worse : As ASI's earnings increased almost sixfold between 2009 and 2011 shifting from $ 4 billion to $ 22 billion, its effective corporate tax rate halved !

The corporation pretends it is unable to reckon the figure of the sweetheart tax deal it enjoyed, yet, Apple consolidating financial statements evidenced the effective tax rate paid by its subsidiaries !
They consider the Commission's assertions are "without merit" but they do not provide any factual nor legal evidence that they are untrue.

Still, the odds are growing that Apple's rulings might be found unlawful. Not only according to NGO's or the Commission but even the American Bank, JP Morgan, which maintains strong business ties with Apple.
The Hi-tech company is an investment banking client of the bank, JP Morgan trades Apple's stocks and manages the Californian firm's public offerings of equity or debt securities.

JP Morgan has reckoned that a negative decision from the EU Commission is "more likely than not".
(“*Based on our work so far we do believe that a negative European Commission ruling is more likely than not*")
The Bank also confessed that its client pays "negligible tax" on only "59 percent of its global income". It accounted for these stunning revelations on the fact that US and Irish tax laws are different and Apple concluded successful negotiations with Ireland.
→ Even Apple's business partner made admissions on Apple's role in avoiding taxation. This is to be interpreted as strong evidence that Apple used Ireland as its main hub in order to avoid taxation and shift as much taxable profit as possible.

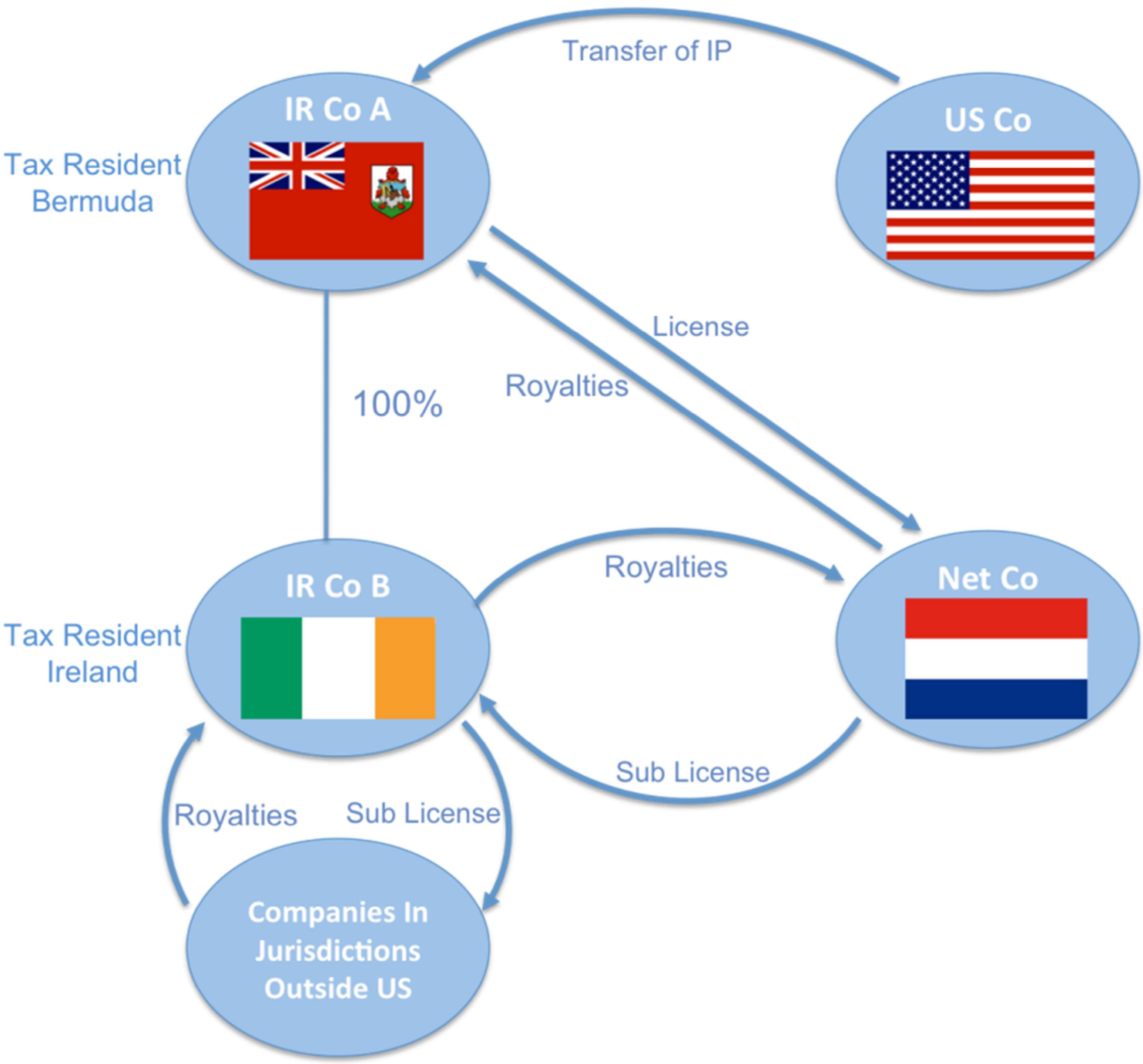
2) Double Irish

The Double-Irish is a scheme that allows companies to be registered in Ireland but without being tax resident.

This enables them to <u>hold their intellectual property in Irish companies that are tax-resident in another country which has a zero rate of corporate tax, such as Bermuda or the Caymans</u>. Netherlands is also included in the Double-Irish scheme because there is no withholding tax on royalties paid by the Dutch company to the Irish company tax resident in a tax haven. The companies said to be using this structure include Apple, Facebook, Google, Microsoft, Oracle Corp and Pfizer Inc.

The structure utilizes advantageous taxation rules in Ireland and the Netherlands to limit the taxation payable on flows of royalty income generated from IP, and is also tax efficient from a US perspective.

<u>How the Structure Works</u>



Based on the content of various reports in the media, the structure is used by US companies which hold IP.
This accounts for the numerous US biggest technological firm using this tax planning method.

- The US parent company (USCo) transfers the IP to an Irish incorporated company, tax resident in an offshore country e.g. Bermuda (IRCoA). (This is made possible because there is no need for an Irish incorporated company to be resident in Ireland).

- IRCoA sublicenses the IP to a company tax resident in the Netherlands (NETCo). NETCo sublicenses the IP to a company tax resident in Ireland (IRCoB). IRCoB is a wholly owned subsidiary of IRCoA.

- IRCoB sub licences the IP to companies located in various jurisdictions outside the US.

<u>How the Royalty Flows ?</u>

IRCoB receives royalties from the various companies in the non-US jurisdictions to which it has granted sub licences. IRCoB retains a small margin of these royalties (usually 5-10%) and passes the remainder to NETCo. NETCo retains a small margin of the royalties it receives from IRCoB and passes the remainder to IRCoA. The royalty margins retained by IRCoB and NETCo are presumed to be compliant with the minimum required for transfer pricing rules.

<u>The Taxation planning process under the Double-Irish</u>

- IRCoB is liable to Irish taxation on <u>only the portion of the royalties which it retains</u>. For Irish taxation purposes, <u>the royalties paid to NETCo are allowed as a deduction against the royalty income received</u>.
- <u>No Irish Withholding Tax</u> (“WHT”) arises on the royalties paid from IRCoB to NETCo.
- <u>No Dutch WHT</u> arises on the royalties paid by NETCo to IRCoA.
- The royalties received by IRCoA suffer a low or nil rate of taxation in Bermuda.
- It may be worthwhile for USCo to transfer the IP to IRCoA early (i.e. when the IP has a low value) in order to limit the amount of US tax payable.
- The structure is also advantageous from a US CFC perspective.

The “Double Irish Dutch Sandwich” tax structure has become increasingly popular with many US companies holding IP.
The structure (in which the two Irish companies are referred to as the “bread” and the Netherlands company as the “cheese”) is designed to help many US multinationals reduce their global taxation liabilities through the use of the favourable taxation regimes in both Ireland and the Netherlands. The structure is also designed to comply with the US CFC tax legislation.

NOTICE on the phasing-out of the "Double-Irish scheme" : The Finance Act 2014 enacted in December 2014 amends the corporate residence rules in order to put an end to the Double-Irish system.
The amendments provide that a company incorporated in Ireland will be regarded as tax resident in Ireland as the default position, with a single exception for companies which are regarded as tax-resident in another country under the terms of a double taxation agreement with Ireland.

→ Basically, any Irish-incorporated business entity would also and without exception be an Irish tax resident liable for tax on its worldwide income.

From now on, an Irish incorporated company will be regarded as Irish tax resident.
The law applies to companies incorporated in Ireland on or from 1 January, 2015. A transitional period applies until 2021 to company incorporated before the 2014 amendment was passed.

The "Double Irish" has been severely criticized by Irish officials themselves through the Tax Strategy Group that comprises top Irish officials from the Ministry of Finance or Tax administration.
Even US President, Mr. Barack Obama pointed out the scheme.
This has questioned Ireland's international credibility and there is no doubt that the growing pressure from official organizations such as the OECD and the EU as well as various stakeholders has forced the Irish government to withdraw the "Double Irish" scheme.

Nevertheless, the problem is similar as in the Switzerland's case : While the government committed to change its tax legislation and repeal its most harmful measure, it also deploys huge efforts to "sweeten" its tax schemes.
This is the case for the Irish Patent Box.

3) Patent box *a la mode* Irish : "Knowledge development" box

In addition to its other tax incentives - 12,5% corporate tax rate, 25% credit on incremental R&D spending - Ireland is set to provide an IP regime as planned by Finance Act 2014.
What are the specificities of the Irish IP regime ?

The regular features of an IP box regime allows companies to deduct taxable revenues generated by IP deriving income. In other words, companies can deduct tax for capital expenditure incurred on the acquisition of qualifying IP assets.
IP qualifying assets vary country by country.

Irish IP box features :

- The IP assets definition was already very encompassing before 2015. Besides traditional IP assets such as patents or trademarks, they also include know-how, domain names or goodwill and even applications for legal protection (when applying for brand, trademarks registration).

→ Thanks to the Finance Act 2014, the <u>list has been extended</u> and it now includes customer lists acquired otherwise than "directly or indirectly in connection with the transfer of a business as a going concern"

- Before the Finance Act 2014, the aggregate deduction and related interest expense which could be claimed at a given year could not exceed 80% of the related IP profits of the company.
Since 2015, this restriction is over. The IP regime has been enhanced by providing a lifting of the 80% cap on the aggregate amount of capital allowances and related interest expense and an extension of the list of qualifying assets.

→ The cap has been increased from 80% to 100%

Acquisition from related parties also qualifies for the IP box → this can lead to aggressive tax planning schemes.

- The consultation ended in April but the Minister of Finance, Michael Noonan has already considered a very low corporate tax rate for the knowledge development box. 5% would be the rate. Should the rate be settled, it would be the lowest in the EU with the Netherlands (also 5%) while Great-Britain has a rate of 10% for instance.

→ The Knowledge development box should definitely be challenged as it may be a new incentive for tax avoidance.

Whereas the EU and the OECD are calling for a nexus approach which would consist in linking the tax relief to the amount of research and development conducted in the jurisdiction, thereby aligning tax rights more closely with “substance”.
Ireland seems to be going in the opposite way of the agenda !

Of course, one should not forget that the R&D credit is also a very attractive relief as it enables companies to offset a share of any research and development investment costs against any Irish corporation tax they have to pay. It can provide an overall effective corporate tax deduction of 37,5% on certain R&D expenditure.

The regime to calculate the deduction has been softened as well by the Finance Act 2014 with the removal of the base year restriction (= Now, all current year qualify to claim the tax credit)

4) The new General Anti Abuse/Avoidance Rule (GAAR) of 2014

Ireland has had a GAAR in its national law since 1989 but never fully made use of it, to say the least. Indeed, the first GAAR case to come to the Irish Supreme Court occurred three year ago (so 22 years after the GAAR introduction in Ireland) with a case named Revenue Commissioners v O’Flynn Construction.
The majority decision of the Supreme Court held that the taxpayer’s scheme was a tax avoidance transaction which did amount to a misuse or abuse of the export sales relief scheme.

But let's not rejoice too rapidly: in spite of ruling in favour of the Revenue office, the impact of the GAAR is not increased by the decision and it reiterates the view that tax planning is a legitimate activity in the course of a commercial transaction.

With the Finance Act 2014, substantial changes are foreseen in the Irish GAAR :

- The tax authority may invoke the GAAR rule if it would be reasonable to consider that when a taxpayer enters in a transaction, it is a "tax avoidance" transaction resulting in a tax advantage that motivated it. Accordingly, any reduction in tax payable is disallowed, in addition to a 30% surcharge.

- There will be no time limit for raising a GAAR notice assessment.

- A "protective notification" procedure is provided, protecting the taxpayer from the surcharge.

- The taxpayer is obliged to provide with all documentation pertaining to the transaction along with an opinion as to <u>why they believe the transaction does not fall within the GAAR</u> provisions.

→ We may want to raise questions about the new GAAR and whether it will be effectively used as an instrument to tackle corporate tax avoidance as past record is extremely poor not to mention void.

5) Irish Double-tax treaty network

Ireland has signed double taxation agreements with 72 countries, of which 68 are in effect.
Almost all of Ireland's treaties provide for <u>nil withholding tax neither on interest nor on dividends paid to a treaty partner</u>, either unconditionally or on certain types of interest only. Therefore, Ireland can be a player in the <u>double non-taxation issue.</u>