

**Irish Tax
Institute**

International Tax and Transfer Pricing for Corporate Treasurers

Tuesday 3 March 2020



**Irish Association of
Corporate Treasurers**

Chairperson – Pieter Berger, *Deloitte*

Please switch off/silence your mobile phone



Opening Remarks

Kevin Daly, President, *Irish Association of Corporate Treasurers*

To ask questions during the Q&A session, please use details below.

1. Go to **slido.com**
2. Enter the event code **#internationaltax**

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Anti-hybrid Rules Ireland

Harry Harrison, *PwC*

Tuesday 3 March 2020



Background



- ATAD - Anti-hybrid rules required to be introduced in Ireland with effect from 1 January 2020
- Finance Act 2019 now signed into Irish law
- Applies to payments arising on or after 1 January 2020
- Very complex provisions which need to be considered for all tax deductible payments
- Particularly complex in a US MNC context

Three main tests which need to be assessed independently in respect of each tax deductible payment:

1. Deduction without inclusion outcome, which arises due to a specific hybrid mismatch,
2. Double Deduction outcome (where not utilised against dual inclusion income),
3. Imported Mismatch outcome - i.e. outcome 1 or 2 above which is funded by Ireland.

Key Concepts/Definitions

New Concepts and Definitions



Inclusion

‘inclusion’ in respect of a payment means –

- (a) payment **is treated as arising or accruing to the payee**, which:
 - (i) is chargeable to domestic tax or foreign tax (excluding remittance basis taxation)
 - (ii) is a pension fund, govt body or other entity that, under the laws of the territory in which it is established, is exempt from tax,
 - (iii) is **established in a territory**, or part of a territory, that does **not impose tax** (established can include place of effective management), or
 - (iv) is established in a territory that does not impose a tax on profits derived from payments receivable from sources outside that territory (i.e. deemed inclusion for payments to territorial systems),

Or

- (b) that is subject to a CFC charge similar to an Irish CFC charge.

- ***Deduction***

- Any “payment” (revenue or capital in nature) which is taken into account when calculating the tax payable (e.g. royalty payment, S291A TCA 1997 IP deduction, etc.)
- Also includes CGT deductions, as well as income tax deductions

- ***Payments***

- Money or “money’s worth” – exceptionally broad
- Deemed payments in the same entity - allocation of profits from a Head Office to a PE, or from one PE to another PE

- ***Foreign Tax***

- Foreign taxes which can give rise to “inclusion” (and also a second or “double deduction”) specifically includes foreign CFC charges “similar to” Irish CFC, and similar to Irish corporation tax more generally

Test 1 – Deduction without Inclusion Hybrid Mismatch

Deduction without Inclusion – three key components



The following three components need to be present for the transaction to fall within the deduction without inclusion test:

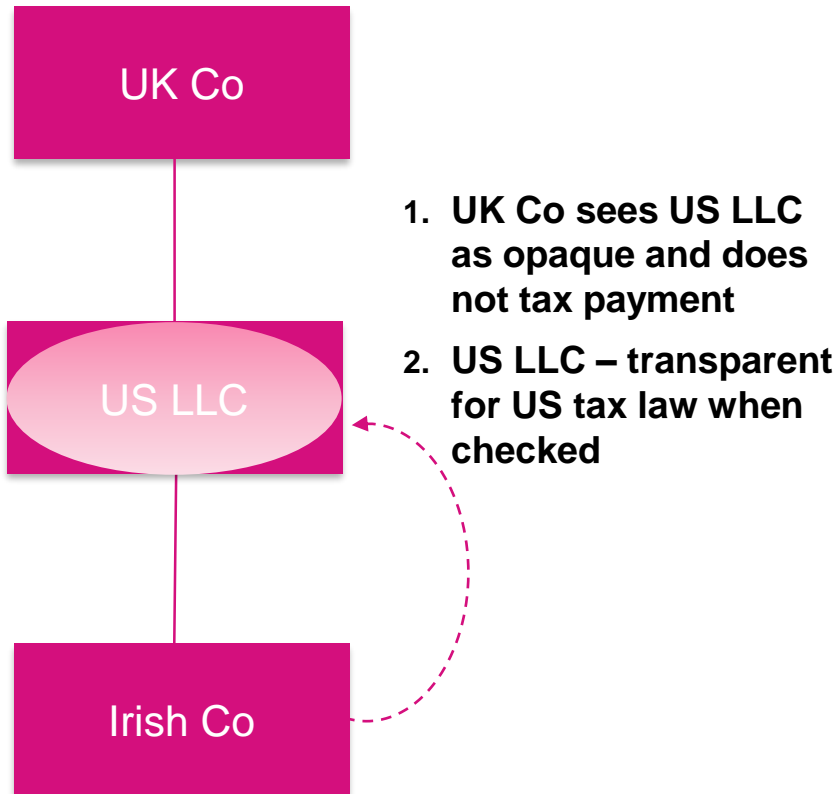
1. Deduction without inclusion in the payee territory, AND

- This outcome is **attributable to**,
- A specific **hybrid mismatch**

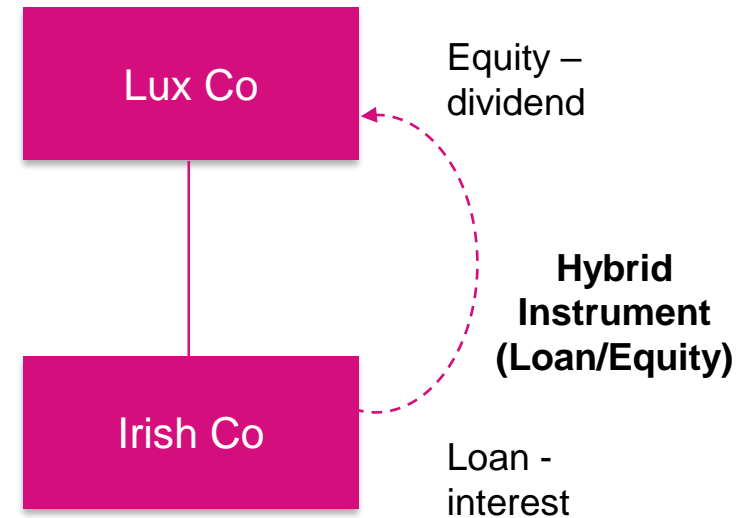
These three components would need to be carefully worked through in all scenarios.

What is a hybrid mismatch? Basic Examples

Hybrid entity



Hybrid instrument



Specific Types of Hybrid Mismatch transaction

1. **Payee Hybrid Entity** - Payment to an entity that is viewed differently in the country it is established, compared to the country of its parent(s) (e.g. transparent vs. opaque)
2. **Payment under a Hybrid Instrument** - Payment under an instrument that is characterised differently in the payee jurisdiction (e.g. interest vs dividend, debt vs. equity)
3. **Disregarded PE** - Payment to a PE that is not recognised/taxed under the laws of the PE jurisdiction, but the PE profits are exempt in the Head Office jurisdiction
4. **PE/Head Office allocation mismatch** - Payment to an entity that has a PE/PEs, and there is a mismatch in how the profits are allocated between Head Office/PEs

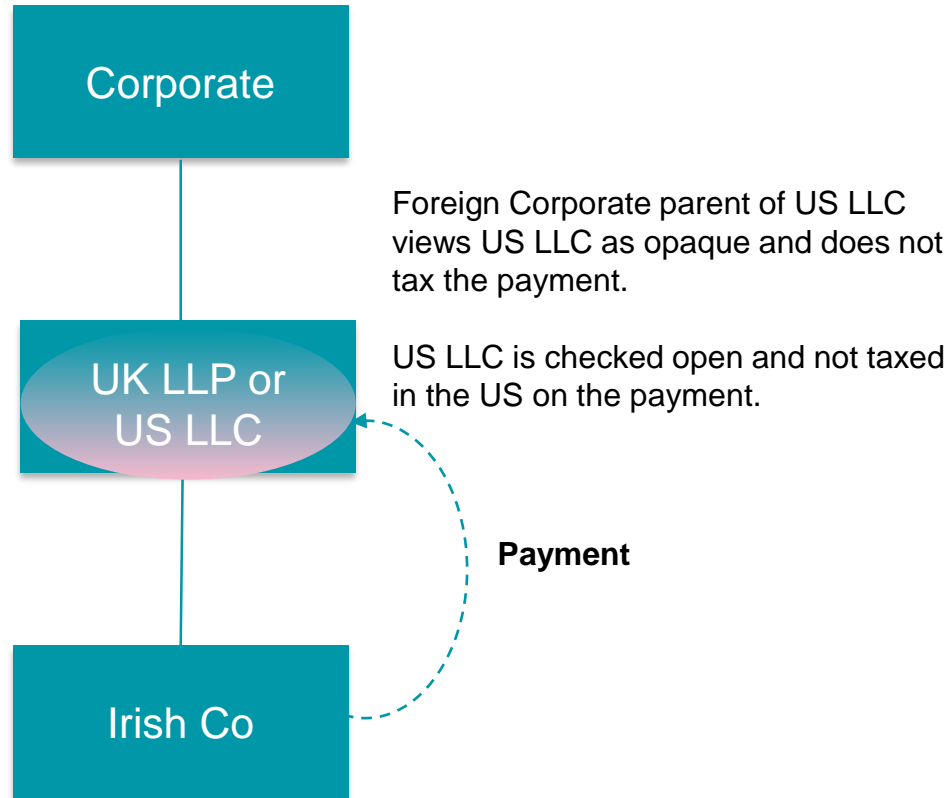
Specific Types of Hybrid Mismatch transaction

5. **Payor Hybrid Entity** * - Payment to an entity that is viewed differently in the country it is established, compared to the country of its parent(s)

6. **PE/Head Office deemed payment mismatch** * - Deemed payment within an entity that has a PE/PEs, which results in a mismatch in how the profits are allocated between Head Office/PEs

* Note that hybrids 5 and 6 will not operate to deny a tax deduction, if the tax deduction is being offset/utilised in Ireland against income that is “dual inclusion income” (the particular income is taxed in the countries where the mismatch has arisen).

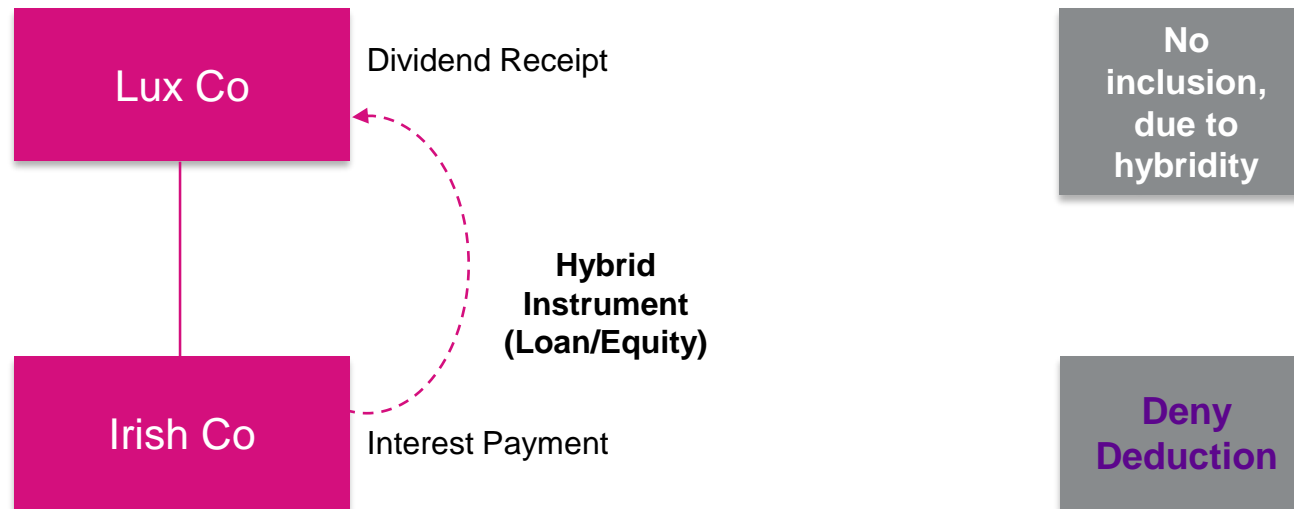
(1) Payment to a Hybrid Entity



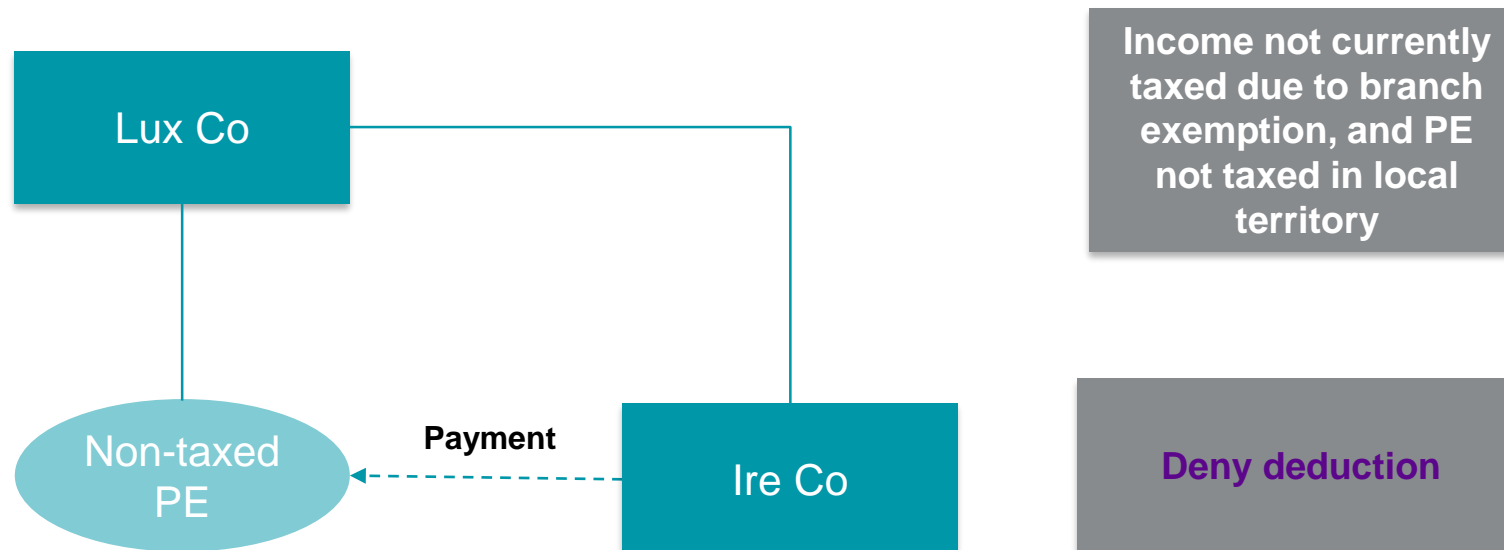
Opaque/Transparent hybridity

Deduction denied if no inclusion

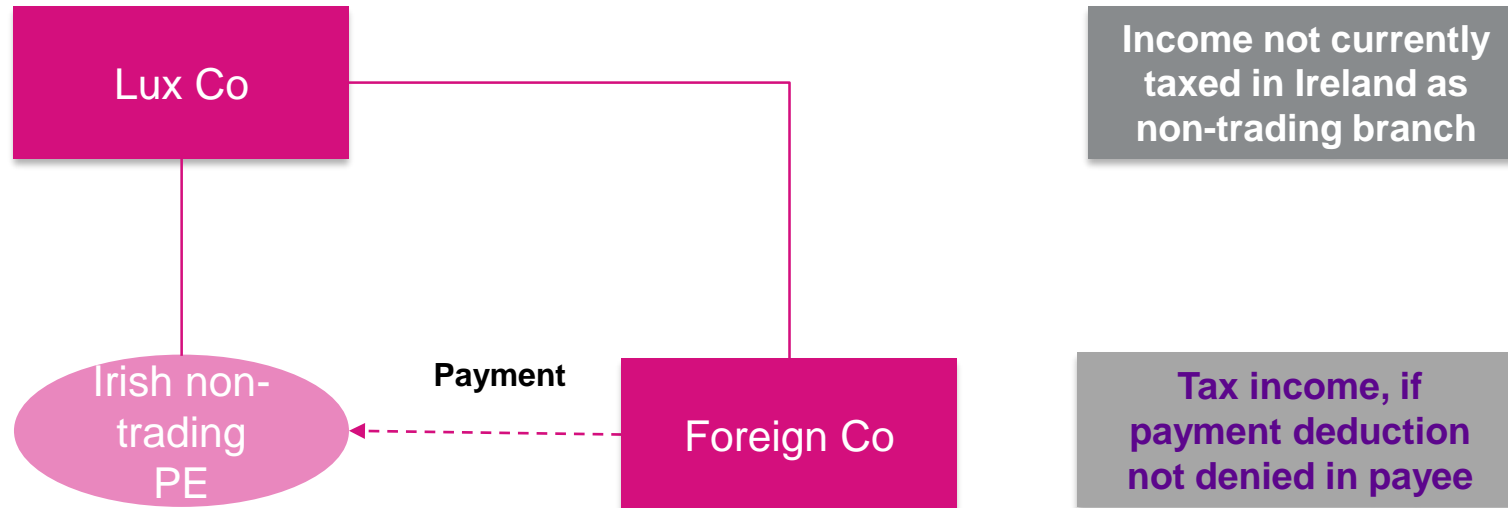
(2) Payment under a Hybrid Instrument



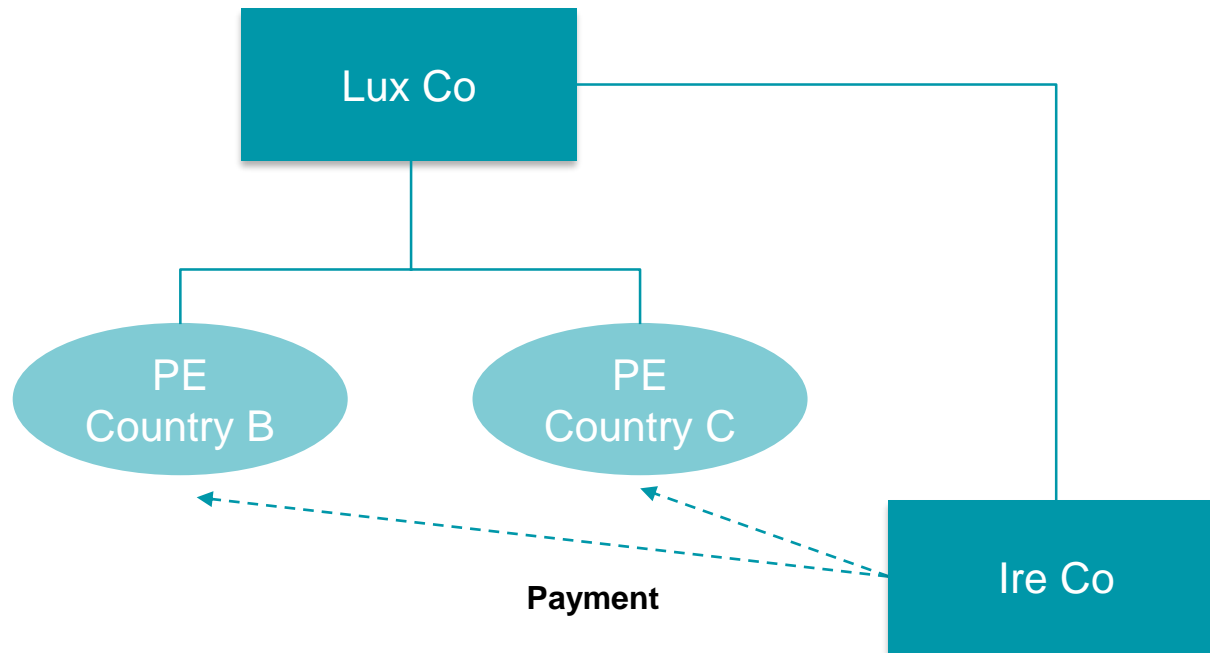
(3) Payment to a disregarded PE – deduction denied



(3) Payment to a disregarded PE – income now taxed



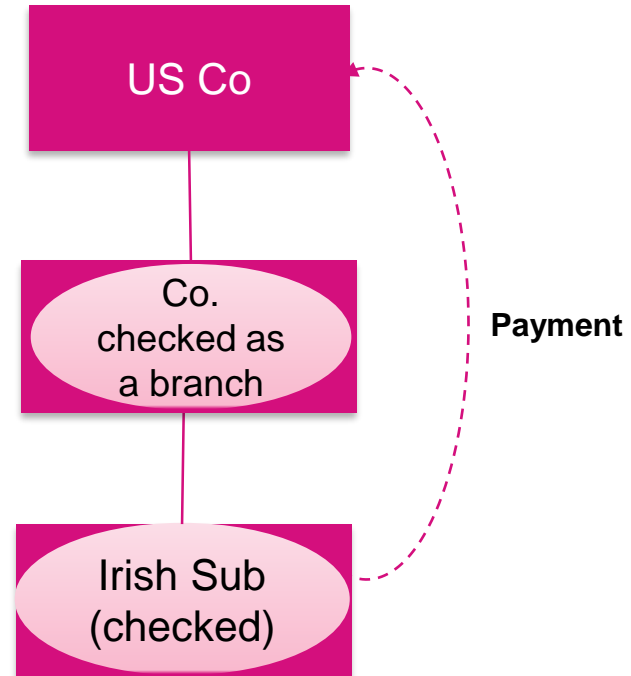
(4) HO/PE allocation mismatches



Income not fully included as a result of profit attribution

Deny deduction for amount not included anywhere

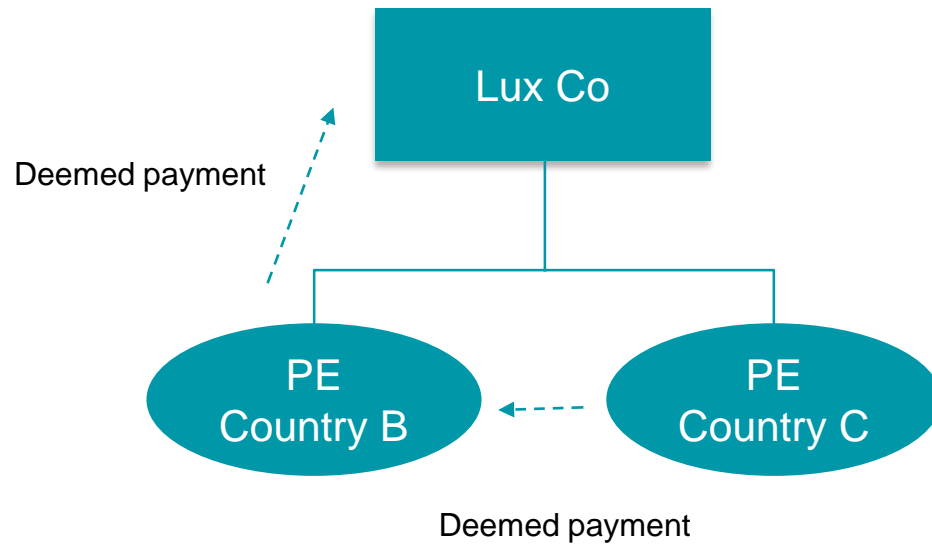
(5) Payment by an Irish Hybrid Entity



Payment ignored as Irish Co is checked as a branch of US Co for US tax purposes

Deduction denied, unless it is being utilised/ offset against dual inclusion income in Ireland

(6) Deemed payments HO/PE mismatches



Deemed payment to HO / other PE is not included

Deduction denied unless it is being utilised/ offset against dual inclusion income in Ireland

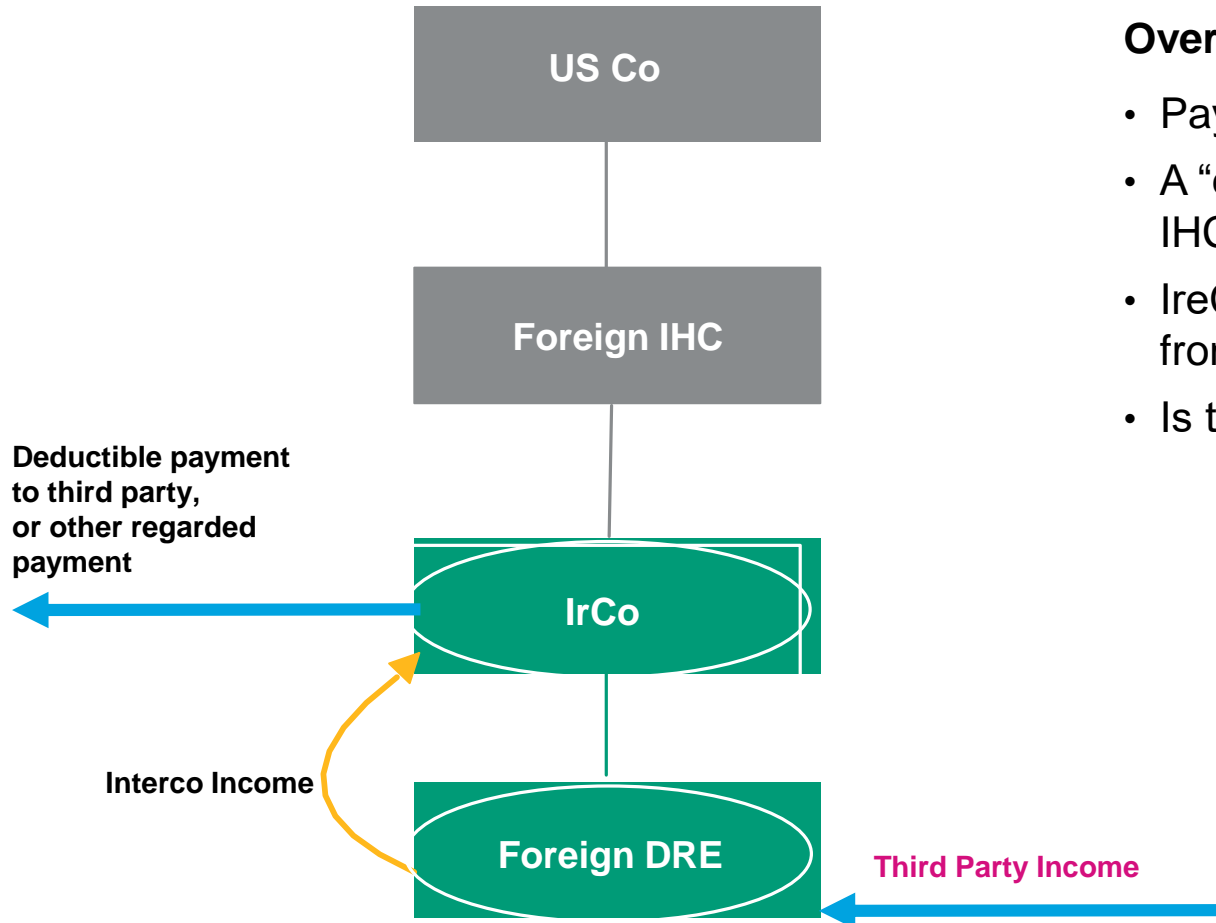
Test 2 – Double Deduction Mismatch Outcome

Double deduction which is not offset/utilised against “dual inclusion income”

Question: Are two deductions being taken for a single payment?

- Does not necessarily need hybrid payments or entities
- Just that there is a deduction in Ireland, and also a deduction of an “associated enterprise” in a foreign territory in respect of the same payment (deduction in foreign territory could be due to the operation of a CFC taxation regime)
- Includes tax deductions in respect of third party payments
- **Problem arises to the extent these deductions are not being utilised/offset in Ireland against “Dual Inclusion Income”**
- This test therefore requires detailed analysis and consideration of foreign CFC provisions (including US CTB elections, Subpart F and GILTI)

Double Deduction – An Example



Overview

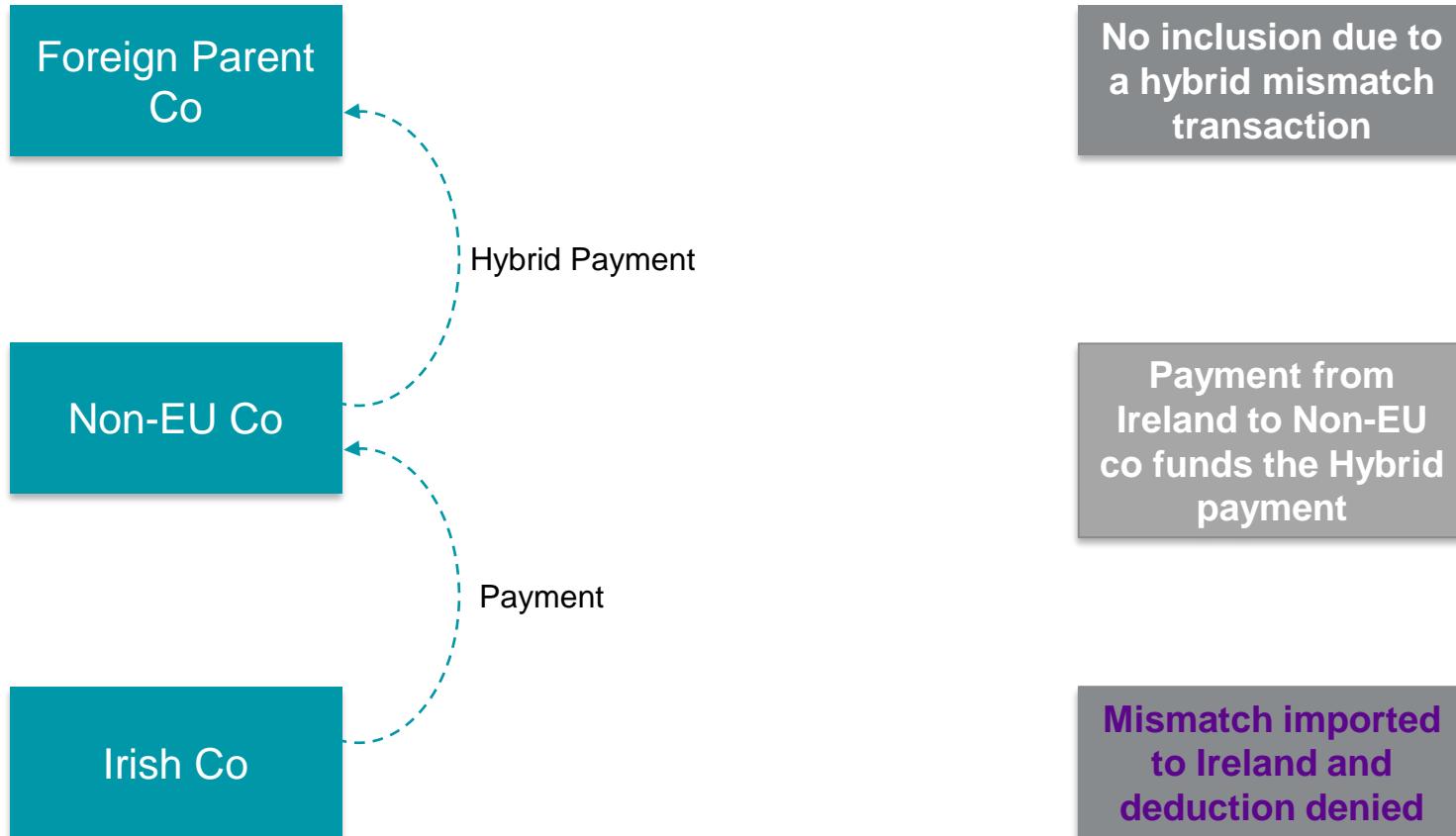
- Payment from Ireland to a third party
- A “check the box” election is made for all subsidiaries below Foreign IHC
- IreCo’s income includes intercompany income which is disregarded from a US tax perspective
- Is there “dual inclusion income”?

Test 3 – Imported Mismatch

Imported mismatch transactions

- Payments to an EU established payee are outside the scope of the Irish imported mismatch provisions.
- A hybrid mismatch which Ireland is not a party to can be imported to Ireland, and an intercompany tax deduction denied where:
 - it would be “reasonable to consider” that
 - a payment by Irish co to a payee established outside the EU
 - “directly or indirectly funds” a hybrid mismatch outcome (i.e. either a double deduction hybrid mismatch outcome or one of the deduction without inclusion hybrid mismatch outcomes) in another entity.
- A tax deduction is denied “for so much of the payment” as corresponds to the mismatch outcome as has not already been neutralised by similar foreign anti-hybrid provisions (so full amount may not always be denied).

Imported mismatch



Recap and summary of areas of focus

Proposed next steps



- Consider group review now to identify key risk areas, in particular in relation to:
 - Any obvious specific hybrid arrangements,
 - Whether the double deduction mismatch rules give rise to a restriction, and in particular whether the income of Irish companies would all represent “dual inclusion income”
 - Reviewing the most material intercompany tax deductions
- All payments are in scope
- US MNC analysis is more complex

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DAC 6 Ireland

Fiona Carney, *PwC*

Tuesday 3 March 2020



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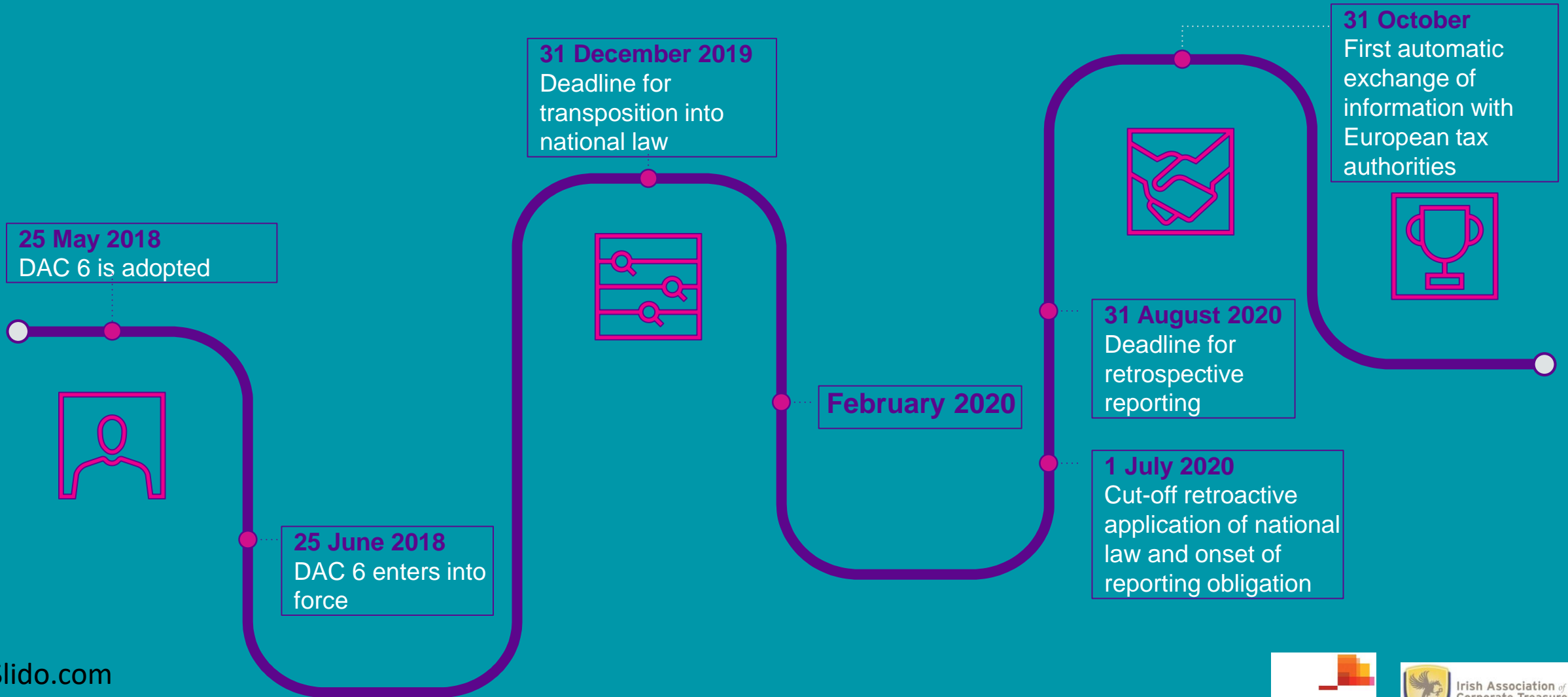
Goals and levels of reporting EU Directive 2018/822 of 25 May 2018 (known as “DAC 6”)

Stated Goals:

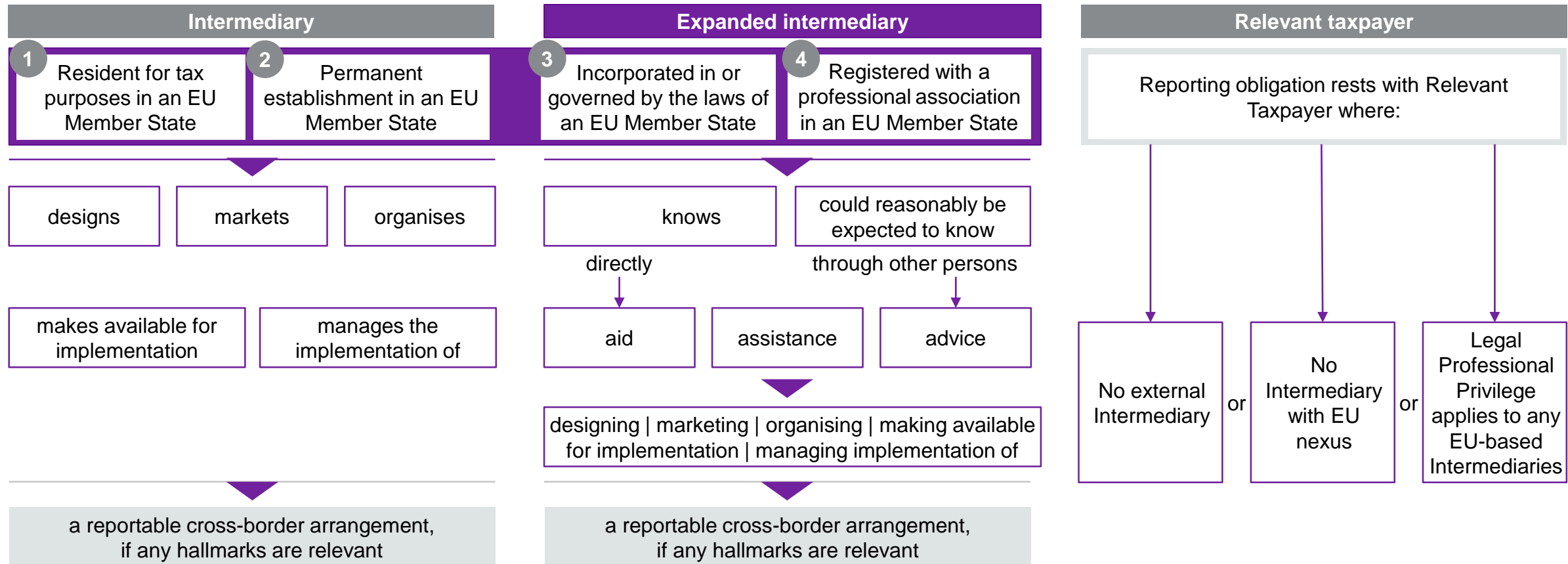
- Improve transparency
- Provide tax authorities with earlier access to information on **potentially aggressive tax-planning arrangements**
- Transposed into Irish legislation as part of **Finance Act 2019**
- Provisions require an **“Intermediary”** (or taxpayer in some circumstances) to report details of any **“Cross-border Arrangement”** that contains at least one of the **“Hallmarks”** listed in Annex IV to the Directive



Timeline



Relevant roles and activities

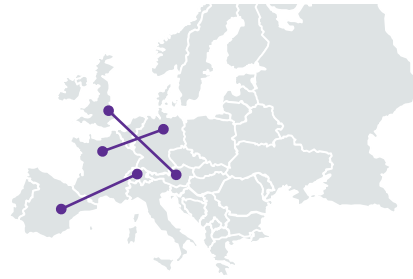


Expanded Intermediary: can provide evidence that they did not know and could not reasonably be expected to know of involvement in reportable arrangement. Based on relevant facts and circumstances/available information/relevant experience and understanding

Cross-border arrangement

A Cross-border arrangement is an arrangement that concerns either more than one Member State or a Member State and a third country where at least one of the following conditions is met:

EU + EU



The participants...

- not all of the participants are resident for tax purposes in the same jurisdiction
- one or more participant is resident for tax purposes in more than one jurisdiction
- one or more participant has a permanent establishment in another jurisdiction that is of relevance for the arrangement
- one or more participant carries on an activity in another jurisdiction without being resident for tax purposes or creating a permanent establishment in that jurisdiction.

EU + non-EU



The arrangement...

- has a possible impact on the automatic exchange of information, or
- has a possible impact on the identification of beneficial ownership.

Non-EU + non-EU



Arrangements not within the scope of application...

- No cross-border tax arrangement without EU connection.

EU DAC6 Hallmarks

Hallmarks subject to the Main Benefit Test

A Generic hallmarks

1. Confidentiality clause that would prevent the disclosure of a potential tax advantage
2. Contingency fees/success fees based on tax advantage obtained
3. Standardised documentation and/or structure

B Specific hallmarks

1. Acquisition of loss-making company, discontinuation of its main activity and use of its losses in order to reduce tax liability
2. Conversion of income into capital, gifts or other categories of revenue taxed at a lower level or exempt from tax
3. Circular transactions resulting in the round-tripping of funds

C Specific hallmarks of cross-border transactions

1. Deductible cross-border payments made between associated enterprises, where in the jurisdiction of tax residency of the recipient:
 - no or almost no corporate tax is imposed,
 - the payment benefits from a full exemption from tax, or
 - the payment benefits from a preferential tax regime

Main Benefit Test

That test will be satisfied if it can be established that the main benefit or one of the main benefits which, having regard to all relevant facts and circumstances, a person may reasonably expect to derive from an arrangement is the obtaining of a tax advantage.

Hallmarks not subject to the Main Benefit Test

C Specific hallmarks of cross-border transactions

1. Deductible cross-border payments made between associated enterprises, if the recipient:
 - is not resident for tax purposes in any tax jurisdiction, or
 - is tax resident in a country which the EU or OECD have assessed as non-cooperative
2. Deductions for same depreciation claimed on asset in multiple jurisdiction
3. Relief from double taxation on same income/capital claimed in multiple jurisdictions
4. Asset transfers where there is a material difference in the amount treated payable in consideration for the asset in the jurisdictions involved

D Specific hallmarks for AEOI and beneficial ownership

1. Undermining the CRS reporting obligation by, e.g. use of products, jurisdictions, or legal entities, not subject to reporting (among others)
2. Use of jurisdictions with weak anti-money-laundering legislation
3. Use of non-transparent legal or beneficial ownership chain

E Specific hallmarks for transfer pricing

1. Use of unilateral safe harbor rules
2. Transfer of hard-to-value intangibles between associated enterprises
3. Intragroup cross-border transfers of assets/functions/risks where the projected annual EBIT of the transferor(s) for the following three years falls by more than 50% as a result of the transfer

Compliance and administration

- Electronic reporting of “**specified information**” listed
- Revenue will assign a **reference number** to a cross-border arrangement that has been reported
- **Five-day window** for:
 - intermediary to share reference number with taxpayer/any other intermediaries
 - taxpayer to share reference number with other taxpayers involved in same arrangement
- Taxpayer must disclose reference **number on tax return** for any chargeable period in which they:
 - enter into arrangement, or
 - obtain/seek to obtain a tax advantage from the arrangement.
- Can claim exemption from reporting with proof that same information has been reported by another person



Penalties

- Penalties to be determined by the courts having regard to:
 - in the case of an intermediary, their fee or likely fee in connection with the arrangement
 - in all other cases, the amount of any tax advantage gained or sought from the arrangement
- Upper limits - arrangements reportable after 1 July 2020:
 - penalty of up to €500 per day for failure by intermediary/taxpayer to report within 30 days
 - penalty of up to €500 per day for failure by intermediary to share reference number within five days
- Upper limit - arrangements reportable under transitional measures
 - penalty of up to €4,000 for failure by intermediary/taxpayer to report by 31 August 2020



Revenue guidance



Rules are currently live



Broad scope of hallmarks and other definitions giving rise to many interpretation difficulties



Many practical issues likely to arise in light of tight timeframes



Revenue guidance expected to issue in March



Several submissions have been made to Revenue on matters for consideration in guidance



TALC sub-group on DAC 6 to meet on 11 March



XML Schema - draft to issue shortly



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Transfer Pricing Update

Kevin Norton, *Deloitte*

Tuesday 3 March 2020

Deloitte.



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Agenda

- Irish rule changes
- New content in the OECD Transfer Pricing Guidelines
- Some practical implications



Irish rule changes



New legislation introduced

For accounting periods on or after 1 Jan 2020



<ul style="list-style-type: none"> Irish TP rules broadened to cover non-trading arrangements, excluding certain domestic arrangements Review all transactions that may previously been outside of Irish TP rules, e.g., IFLs, licence agreements, rents, etc. <p>Extends to non-trading income</p>	<p>Adopts 2017 OECD Guidelines</p> <ul style="list-style-type: none"> Brings latest OECD Guidance into Irish legislation (including HTVI and profit splits) Legislation also emphasises substance over form Historical analyses likely to require updates to ensure compliance with latest guidance (DEMPE, control of risk, etc.) Test substance of arrangements 	<ul style="list-style-type: none"> Master File >€250m Local File >€50m Specific Irish TP documentation is now mandatory. <p>Enhanced TP documentation</p>	<p>Removes grandfathering</p> <ul style="list-style-type: none"> Pre-July 2010 arrangements are now within the scope of TP rules Check if any transactions were treated as grandfathered. A TP analysis will now be required 	<ul style="list-style-type: none"> Capital transactions of +€25m are subject to TP rules (with some exceptions) from 1/1/2020 Greater documentation will be required to support the values in capital transactions. This will be an important area of focus for Irish Revenue. <p>Extends to capital transactions > €25m</p>	<p>Extends TP to SMEs</p> <ul style="list-style-type: none"> Documentation requirement: <ul style="list-style-type: none"> Small=Exempt Medium=Simplified <p>! Subject to ministerial order</p>
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New content in the OECD Transfer Pricing Guidelines

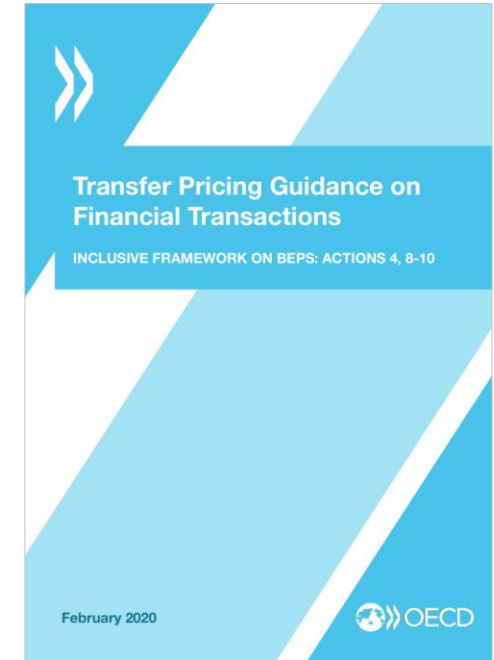
New content in the OECD Transfer Pricing Guidelines

Structure of the new guidance

- A** Introduction
- B** Accurate delineation of financial transactions
- C** Treasury function:
 - Treasury centre services
 - Intra-group loans
 - Passive association
 - Cash pooling
 - Hedging
- D** Guarantees
- E** Captive insurance
- F** Risk-free and risk-adjusted rates of return

New Chapter X
OECD Transfer
Pricing Guidelines

Added to Chapter I
OECD Transfer
Pricing Guidelines



Accurate delineation of financial transactions

Accurate delineation of financial transactions

Balance of debt and equity funding

Accurate delineation of the balance of debt and equity funding:

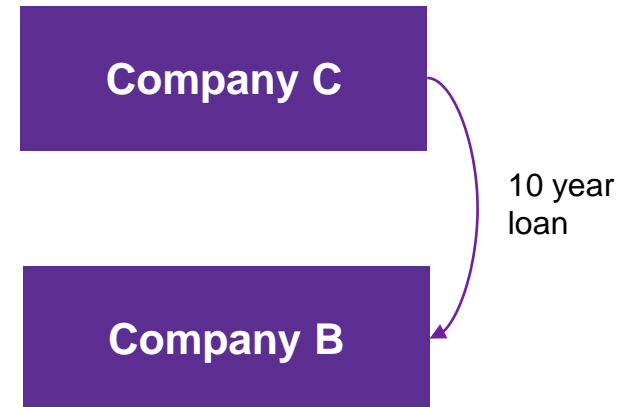
Not the only approach to determine whether debt should be respected as debt for transfer pricing purposes

Not intended to prevent other approaches to address debt/equity balance or interest deductibility under **domestic legislation**

Debt / equity distinction:

- Should (part of) a loan be regarded as e.g. a contribution to equity capital?

Example:



To consider:

- Financial projections
- Ability to service/repay
- Options available
- Two sided perspective
- Not 'all or nothing'

Accurate delineation of financial transactions

The actual transaction



- Identify the **commercial or financial relations**
 - Industry-, entity- and transaction-specific matters
 - Regulated entities: due regard to regulatory constraints + footnote reference

“... The regulatory approach to risk allocation for regulated entities should be taken into account and reference made as appropriate to the transfer pricing guidance specific to financial services businesses in the *Report on the Attribution of Profits to Permanent Establishments* (OECD, 2010).”

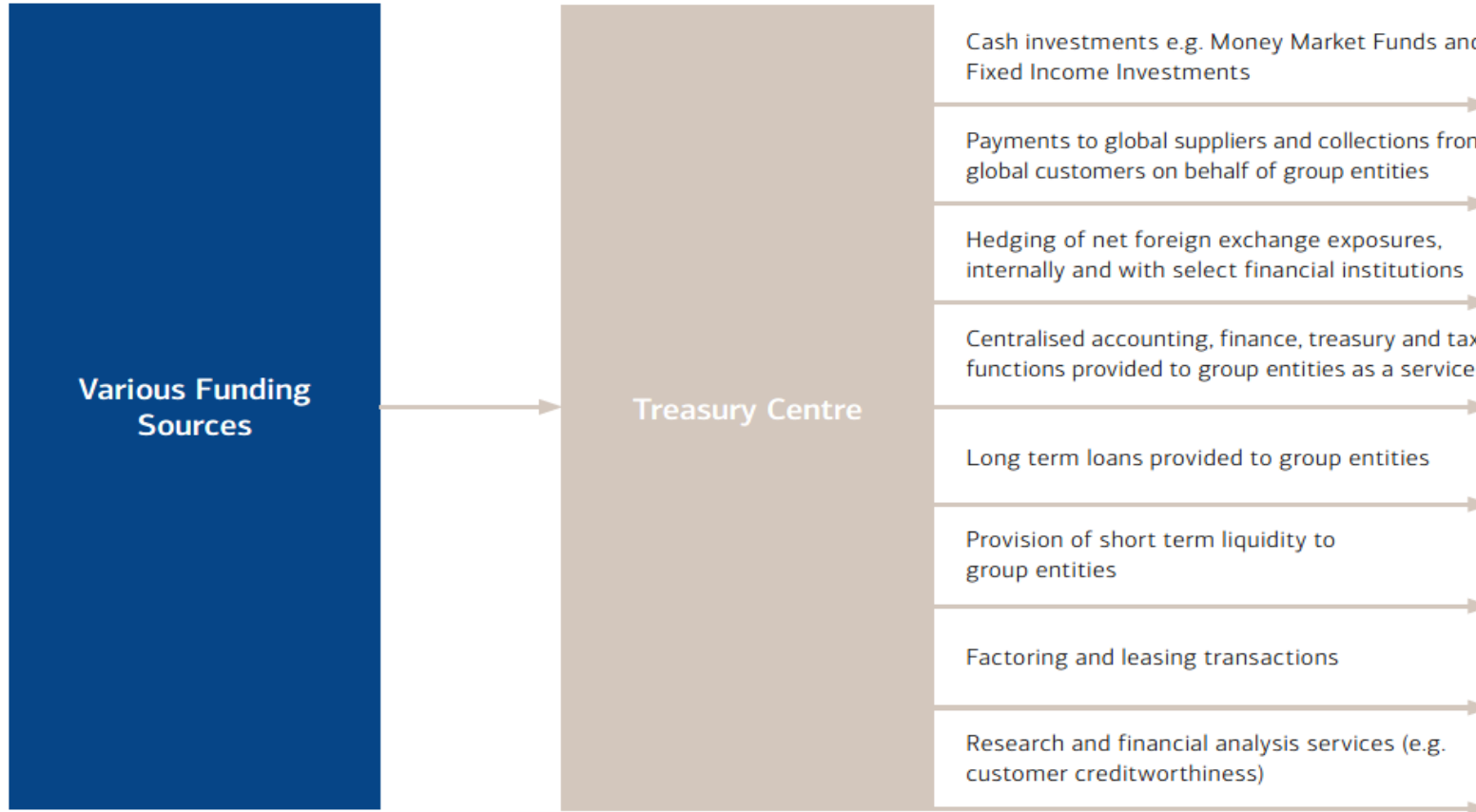
Footnote to D1.2.1

- Consider **all other options realistically available** to the parties
- Consideration of the **economically relevant characteristics**:
 - Contractual terms
 - Functional analysis (functions performed, assets used, risks assumed)
 - Specific terms of financial instruments (repayment, security, currency etc.)
 - Economic circumstances
 - Business strategies

Treasury function

Treasury function

- Different degrees of treasury **centralisation, autonomy** and **functionality**.
- Often, treasury is a support-service to the main value-creating operation:
 - Remunerated through a service fee
- Higher strategic decisions may be the result of group-level policy



Risk-free and risk-adjusted rates of return

Extracts from Actions 8-10 Final Report

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“If [the enterprise] does not in fact control the financial risks associated with its funding (for example because it just provides the money when it is asked to do so, without any assessment of whether the party receiving the money is creditworthy), then it will not be allocated the profits associated with the financial risks and will be entitled to no more **than a risk-free return...**”

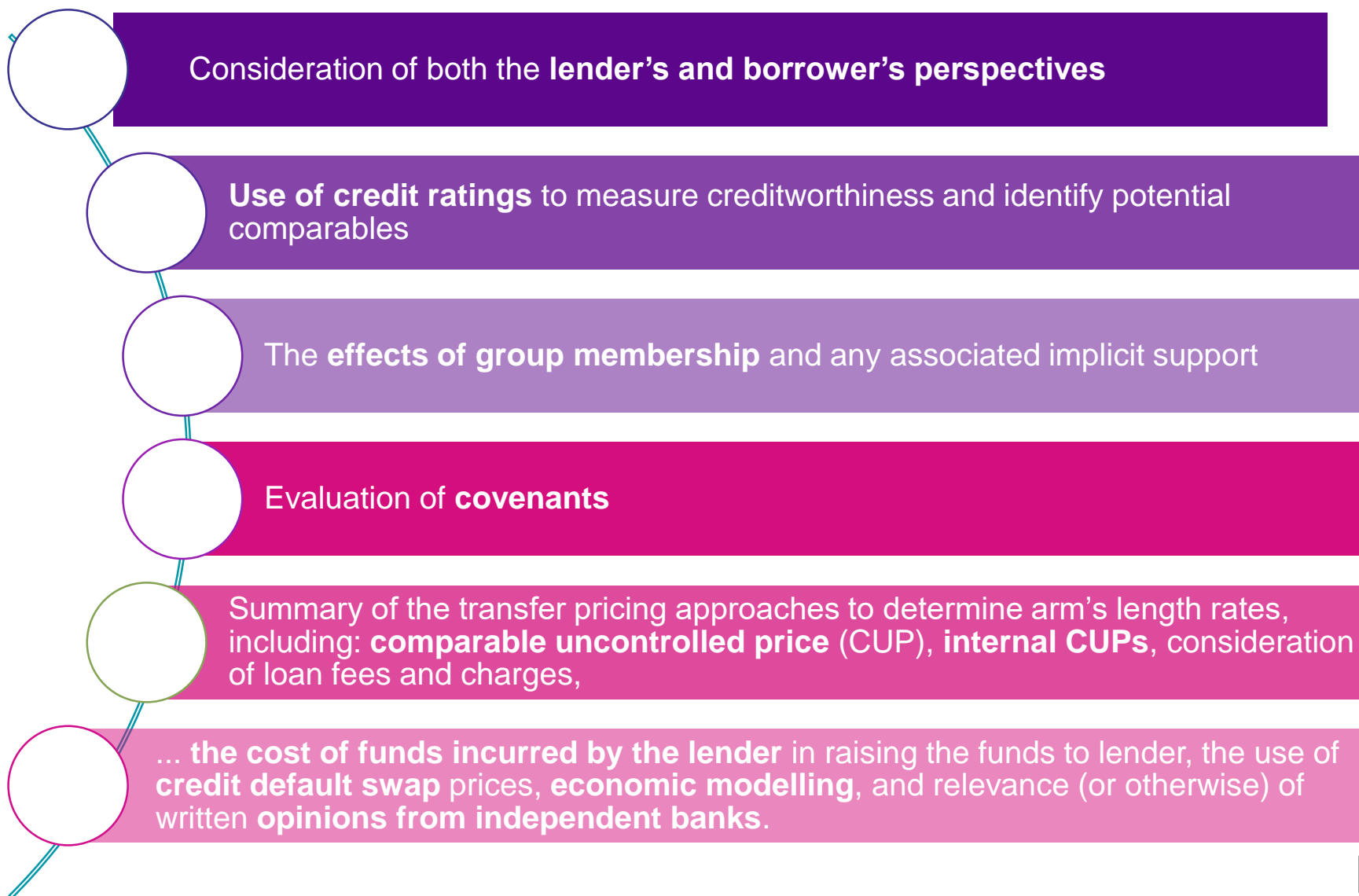
“capital without functionality will generate **no more than a risk-free return**, assuring that no premium returns will be allocated to cash boxes without relevant substance...”

“[...] would not be entitled to **any more than a risk-free return** as an appropriate measure of the profits it is entitled to retain, since it lacks the capability to control the risk associated with investing in a riskier financial asset”

Intra-group loans

Intra-group loans

Determining an arm's length rate of interest



Intra-group loans

Credit ratings and passive association

- Depending on the level of passive association, it may be appropriate for an entity to have a credit rating **closely linked to that of the multinational group**
- Conversely, where there is evidence that no support would be provided, it may be appropriate for an entity to be considered on the basis of its **stand-alone credit rating only**
- Passive association – factors to consider:
 - legal and regulatory obligations
 - relative strategic importance of the entity to the group (e.g. core, highly strategic)
 - operational significance
 - potential reputational impacts
 - stated policy
 - history of support
- Fact-based approach, taking account of **quantitative** and **qualitative factors**
 - ‘rebuttable presumptions’ in 2018 consultation question not taken forward

Cash pooling



Cash pooling

Accurate delineation of cash pool transactions

“The accurate delineation of the cash pooling transactions will depend on the particular facts and circumstances of each case. As cash pooling is not undertaken regularly, if at all, by independent enterprises, the application of transfer pricing principles requires careful consideration”

- The **wider context** should be considered – not just the balance amounts
- Participation of cash pool members includes being part of a **collective strategy** seeking to benefit all cash pool participants
- **No cash pool member would expect to participate if it made them any worse off than their next best option**

- Cash pool arrangements are **short-term liquidity arrangements**.
- **Longer term positions** should be treated as something else (e.g. term deposits/loans)
- Year on year patterns, as well as financial management policies, could be indicators for whether a balance remains part of the cash pool

Cash pooling

Pricing of cash pool transactions

Rewarding the cash pool leader:

Merely performing a
co-ordination function
agency, low level of functionality

Service provider remuneration

Additional functions undertaken

- controls and bears financial risks
- has financial capacity

Enhanced reward

Rewarding the cash pool participants:

- No prescriptive approach
- Consider realistically available alternatives to participating in the cash pool arrangement as well as evaluating risks borne by the cash pool leader, the presence of cross-guarantees, and the contribution of other participants to the cash pool.

Cross guarantees and rights of set off that may be required in the cash pool

– to the extent represents credit enhancement due to the implicit support of other group members:

- No guarantee fee due, and
- Support in the event of a default regarded as a capital contribution

Guarantees



Guarantees

Effect of group membership

- An appropriate benefit - **lower cost of debt funding** - for the borrower is needed for it to be willing to remunerate the guarantor with a commensurate fee
- Different types of intra-group credit support – depends on facts and circumstances:

Explicit guarantee

- Legally binding
- Usually provides relevant rights to creditor to enforce commitment

Implicit support

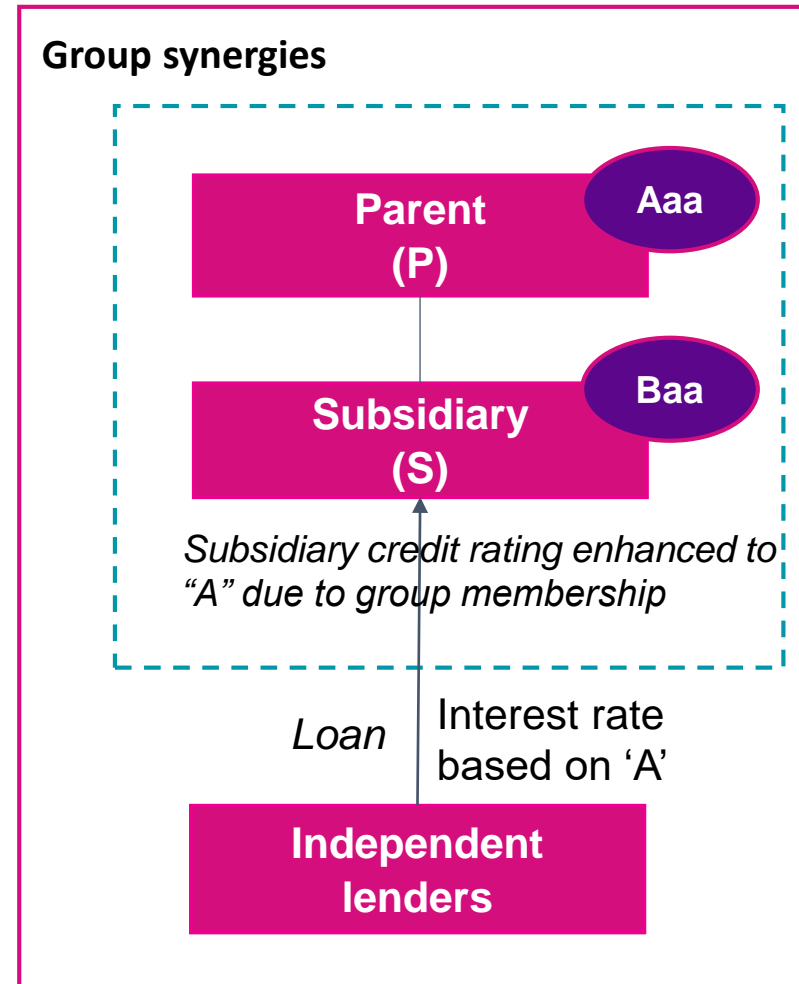
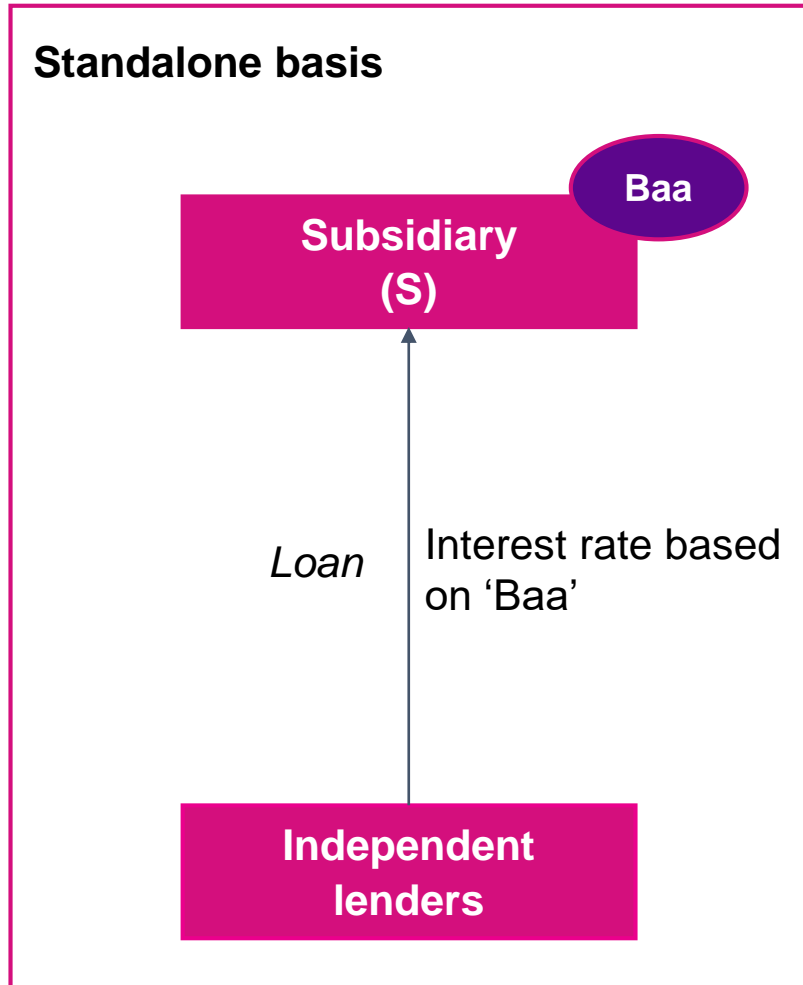
- Includes a 'letter of comfort' and other lesser forms of support
- Attributable to borrower's group member status/passive association

Where guarantee leads to access to a larger amount of borrowing, need to ask:

1. Whether a portion of loan should be accurately delineated as a loan to guarantor (followed by equity contribution to borrower)?
2. Whether guarantee fee in respect of remaining portion of loan is arm's length?

Guarantees

Example – Implicit support



Benefit of implicit support attributable to passive association:
“not from the provision of a service for which a fee would be payable”

Some practical implications

Transfer pricing aspects of financial transactions

Practical implications



- **Documentation** and visibility of financial transactions
- Tax authority **experience**
- **Double taxation**
 - Treaties and Mutual Agreement Procedure

Panel Discussion

Questions and Answers

