TAXE Committee

Ad hoc Delegation to Dublin, Ireland
28 May 2015

Secretariat : Mr Marcus Scheuren - marcus.scheuren@europarl.europa.eu
Service GSM no: +32-498/981 391

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TAXE COMMITTEE
ad hoc Delegation
to Dublin (Ireland) 28May 2015

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TAXE COMMITTEE

ad hoc Delegation

to Dublin (Ireland) - 28 May 2015

FINAL Draft Programme as of 26/05/15

Wednesday 27 May 2015

Arrival in Dublin in the evening

Thursday 28 May 2015

8.30-9.45 **Meeting with stakeholders**

Venue: European Parliament Conference Room : 43 Molesworth Street, Dublin 2

-Irish Tax Institute *(provisionally confirmed, probably Cora O,Brien)*

Revenue Commissioners *(provisionally confirmed, probably John Fanning)*

10.00 - 11.00 **Meeting with Michael Noonan TD, Minister of Finance**

Venue: Government Buildings, Upper Merrion Street Dublin 2, Ireland,

Tel. +353 (0)1 676 7571

11.15 - 12.30 **Meeting with members of Finance Committee of Irish Parliament (Oireachtas)**

Venue: Leinster House, Kildare Street

12.30 - 13.30 **Working lunch tbc**

Venue: European Parliament Conference Room : 43 Molesworth Street, Dublin 2

Professor Frank Barry of TCD *(confirmed either for working lunch or for final panel)*

Seamus Coffey of UCC *(confirmed either for working lunch or for final panel)*

13.30- 15.00 **Further meetings with stakeholders**

Venue: EP Offices - European Union House, 43, Molesworth Street, IRL Dublin 2

- Feargal O'Rourke, Head of Tax PWC

- Conor O'Brien, Head of Tax, KPMG

- Jim Clarken, CEO of Oxfam Ireland

-Dr Micheál Collins, NERI

Programme ends.

15.00 - 15.30 **Chair only : Press point (tbc)** *Venue: EP Offices - European Union House, 43, Molesworth Street, IRL Dublin 2*

15.30 **Departure for airport**

Flight 17:15 Dublin (DUB) - 19:50 Amsterdam Schiphol (AMS) (Aer Lingus EI610)

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European Parliament

TAXE COMMITTEE
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28 May 2015
Draft list of participants

Members

Alain LAMASSOURE, Chair	
Burkhard BALZ	PPE
Elisa FERREIRA	S&D
Morten MESSERSCHMIDT	ECR
Michael THEURER	ALDE
	GUE
Sven GIEGOLD	Verts/ALE
Marco VALLI	EFDD

Accompanying Members

Brian HAYES	PPE
Marian HARKIN	ALDE
Peter SIMON	S-D
Hugues BAYET	S-D
Matt CARTHY	GUE

Political advisers

Daniel KÖSTER	PPE
Stine LARSEN	S&D
Jami ARVOLA	ECR
Petra SOLLI	ALDE
Sinead NI TREABHAIR	GUE
Michael SCHMITT	Verts/ALE
Andrea CURRI	EFDD

Secretariat

Massimo PALUMBO	Head of Unit
Marcus SCHEUREN	Administrator

EP Office in Ireland

Francis JACOBS, Head of Office

Press Officer

Ronnie KORVER

Interpreters

Aoife KENNEDY (Team Leader)
Lila GUHA
Alexandra HAMBLING

TAXE COMMITTEE
ad hoc Delegation
to Dublin (Ireland) 28May 2015
Information on logistics for participants

Hotel:
DOUBLE TREE BY HILTON – BULRINGTON ROAD
Upper Leeson Street
Dublin
Ireland
Phone: +353 1 618 56 00
Website: http://doubletree3.hilton.com/en/hotels/ireland/doubletree-by-hilton-hotel-dublin-burlington-road-DUBBUDI/index.html

Please take taxi from airport to hotel (and vice versa).
Ca. 30 min. / 16 km airport to hotel

European Parliament Information Office in Ireland
43 Molesworth Street
Dublin 2
Phone: +353 (0)1 605 7900
Head of Office: Francis Jacobs
20 min/ 1.7km walk from hotel to meeting venue, or take taxi

Ministry of Finance
Government Buildings, Upper Merrion Street, Dublin 2
(10 min walk from EP office)

Irish Parliament (Oireachtas)
Leinster House, Kildare Street, Dublin 2
(7 min walk from Ministry of Finance)

Secretariat : Mr Marcus Scheuren - marcus.scheuren@europarl.europa.eu
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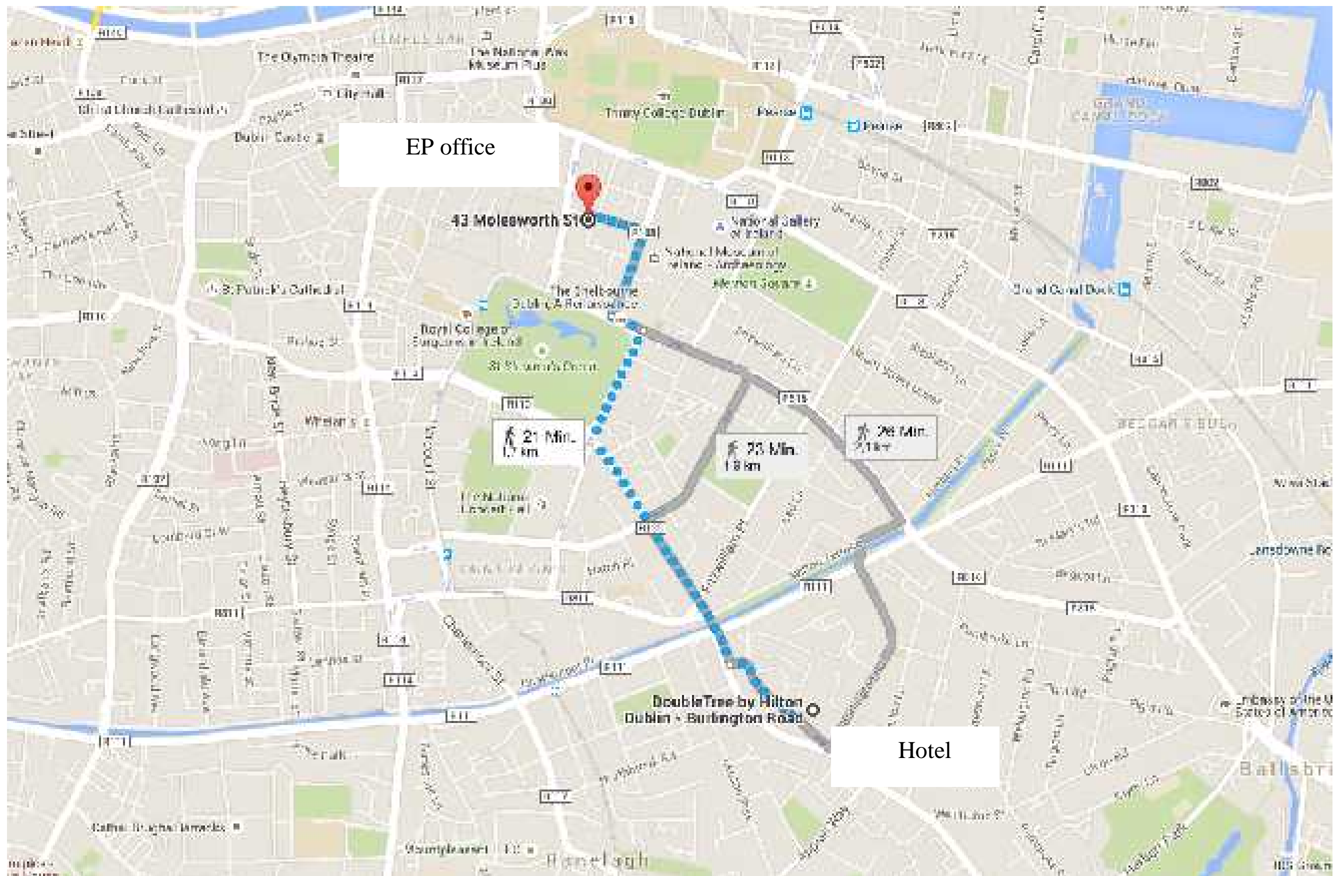

EP office
43 Molesworth St
Hotel
DoubleTree by Hilton
Dublin - Burlington Road
21 Min.
1.7 km
23 Min.
1.8 km
26 Min.
2.1 km
The Olympia Theatre
City Hall
Dublin Castle
Trinity College Dublin
National Gallery of Ireland
St Stephen's Green
Merrion Square
Royal College of Surgeons in Ireland
The National Concert Hall
Grand Canal Dock
Christ Church Cathedral
St. Patrick's Cathedral
Ranelagh
Ballsbridge

Irish Tax Institute Executive

<table>
<tr><td>Cora O'Brien Tax Policy Director Irish Tax Institute. She has led the Institute's work on a range of domestic and international tax policy issues including the introduction of Ireland's International Tax Strategy, the OECD BEPS Action Plan, the EU's VAT and 2015 project and the Digital Economy.

Cora represents the Institute on Main TALC (Tax Administration Liaison Committee) and is a Chartered Tax Adviser and a Chartered Accountant. She is the Institute's Fiscal and Professional Affairs representative at the Confédération Fiscale Européenne (representative organisation for the tax profession in Europe).</td><td> </td></tr>
<tr><td>Martin Lambe, Chief Executive Irish Tax Institute. Prior to his appointment as Chief Executive he served as Director of Finance, Risk & Compliance from 2004-2014. Martin was also Company Secretary of the Institute and is a Fellow of the Association of Chartered Certified Accountants.</td><td> </td></tr>
<tr><td>Olivia Buckley, Communications Director Irish Tax Institute oversees the Institute's media, public affairs and stakeholder relations strategies. She previously held senior communications positions in Government, major Irish corporates and Ireland's leading agri-business organisations.

Olivia was also the Director of We Belong, a highly successful campaign for the EU Lisbon 2 Referendum.</td><td> </td></tr>
</table>

About the Irish Tax Institute

We represent over 5,000 Chartered Tax Advisers (CTA) in Ireland and are part of a global network of 28,000 CTAs. We are the leading provider of tax education in Ireland; our Chartered Tax Adviser qualification is highly respected and is widely recognised as the premier tax qualification. We are also the leading provider of tax legislation publications, commentary books and Ireland's most extensive tax online research database. This database is used by thousands of people including, the Irish Parliament, research bodies, academics, Government and the tax profession.

Our members work in tax practice, professional services firms, corporates and the public sector including Revenue, the Department of Finance, the IMF and indeed the European Commission. We also have members in over 100 cities internationally.

The Irish Tax Institute is actively involved with the EU on tax, through membership of various expert groups in the Commission, our work with the Department of Finance and the Irish Revenue and through the various public consultations which have been held in the past.

The Institute is an active member of Confédération Fiscale Européenne (CFÉ), the umbrella organisation representing the tax profession in Europe. CFÉ's members are 32 professional organisations from 25 European countries with 180,000 individual members.

We have also been heavily engaged in the OECD BEPS agenda. We have made **13 submissions** to the OECD in response to BEPS Discussion Drafts, have travelled to OECD public consultations in Paris and have met with senior OECD officials involved in the BEPS project.

The Irish Tax Institute held the first ever US – Irish Global Tax Conference in association with Harvard Kennedy School in Dublin Castle two years ago, providing an important platform for debate and discussion on the EU and OECD tax agenda. Officials from the EU spoke and attended the event, along with policy makers and tax advisers from across the world. The Institute will host the second global tax conference in association with Harvard Kennedy in March 2016 in Dublin Castle.

Professor Frank Barry, Trinity College Dublin, Ireland

Profile

Frank Barry has been Professor of International Business and Economic Development at the School of Business, Trinity College, Dublin since 2007. He holds a PhD in Economics from Queen's University, Ontario, and has held visiting positions at the University of Stockholm, the University of California and the University of New South Wales in Australia. On contract with the Harvard Institute for International Development he served as an advisor to the Ministry of Finance of the Republic of Indonesia. He has been a consultant to the World Bank, the European Commission and other international organisations and has served as a resource person with the Nairobi-based African Economic Research Consortium (AERC) since 2007. His research interests are in international trade and foreign direct investment, macroeconomics, economic history and development.

Selected publications

- "Capital Flight, Safe Havens and Secrecy Jurisdictions", in *Capital Flight from Africa: Causes, Effects and Policy Issues*, Oxford University Press, 2014.
- "Diversifying External Linkages: the Exercise of Irish Economic Sovereignty in Long-Term Perspective", *Oxford Review of Economic Policy*, 2014.
- "Foreign investment and the politics of export profits tax relief, 1956", *Irish Economic and Social History*, 2011.
- "FDI Implications of Recent European Court of Justice Decisions on Corporation Tax Matters", (with Rosemary Healy-Rae), *European Business Organization Law Review*, 2010.
- "Foreign Direct Investment and Institutional Co-Evolution in Ireland", *Scandinavian Economic History Review*, 2007.
- *Multinational Firms in the World Economy*, by G.B. Navaretti and A. Venables with Frank Barry and others, Princeton University Press, 2004.
- "Export Platform FDI: the Irish Experience", Luxembourg: European Investment Bank, 2004.
- *Understanding Ireland's Economic Growth*, Macmillan Press, 1999.

Feargal O'Rourke is the incoming Managing Partner (CEO) of PwC Ireland from 1 July 2015.

He has been the head of PwC Ireland's Tax and Legal Services practice since 1 January 2011. He has played a major role in the Irish Tax policy debate during that time and shared platforms with Irish and foreign politicians as well as key OECD tax officials.

He has also served in various leadership roles in PwC EMEA and PwC Ireland since his admission as a partner in 1996.

He has been appointed by a number of Irish Governments to various tax and tax related roles.

He served for 7 years on the board of Forfás, the Irish State body responsible for the development of Industrial policy and the development of science and technology In Ireland, having been appointed by the Minister for Enterprise Trade and Employment in 1998.

In 2004 he was appointed by the Minister for Finance as one of Ireland's "independent persons of standing" under the terms of the EU Double Taxation Arbitration Convention, a position which he still holds.

Feargal was appointed by the Government in February 2008 as the only Big 4 representative to the 18 person Commission on Taxation. The Commission was asked to review and report back on the structure, efficiency and appropriateness of the Irish tax system and to look specifically at issues such as securing the 12.5% rate of taxation and carbon taxation. The background to, and work of, the Commission can be viewed at http://www.taxcommission.ie/ Many of the recommendations proposed by the Commission have now been implemented.

In 2014, Feargal was appointed to the board of directors of the American Chamber of Commerce in Ireland which is the representative body for the 700 US companies based in Ireland at both Government and Industry level. As part of this role, he chairs the Taxation working group.

He works primarily in the Foreign Direct Investment sector of PwC and advises US companies establishing their operations in Ireland and Europe.

He holds a First Class Honours Bachelor of Commerce degree from University College Dublin and also holds the Diploma in Professional Accounting from that University. He is a Fellow of the Institute of Chartered Accountants in Ireland and an Associate of the Irish Taxation Institute, having obtained 1st place nationally in the final exam.

He has lectured and written extensively on taxation matters and is a frequent commentator in the media on the subject.

E Mail: feargal.orourke@ie.pwc.com

Direct Dial: +353 (0)1 7926480

Twitter: @feargalorourke

LinkedIn: ie.linkedin.com/in/FeargalORourke

Conor O'Brien
Head of Tax and Legal Services
KPMG Ireland

- Conor has been practicing as a tax advisor since 1989.
- He has been KPMG Ireland's Head of Tax and Legal Services for over two years and before that was head of KPMG Ireland's Financial Services Tax Unit.
- He is author of the Irish Institute of Taxation's book on Double Taxation Treaties.
- He is a Chartered Accountant, a member of the Irish Institute of Taxation and holds a Bachelor of Commerce and Masters in Finance from University College Dublin.

Jim Clarken Biog

May 2015

Jim Clarken is CEO of Oxfam Ireland and is an Executive Director of the Oxfam International Confederation, sharing global responsibility for Oxfam's work in over 90 countries. Jim plays a key leadership role within the global Oxfam organisation and has been involved in leading the worldwide transformation of the confederation in recent years.

Jim is a frequent contributor to debate at various UN bodies, the European Parliament and Commission as well as the Irish Parliament on a range of development issues. Due to his expertise in international development and strong business background, Jim has presented at a range of major international fora on issues including Trade, Taxation, Climate Justice, Aid Effectiveness, Resilience, Food Security and HIV/AIDS. He is a passionate advocate of the rights of women and the transformative role that women play in development.

He is a regular media contributor on a range of issues and more recently on the consequences of growing inequality as the key challenge facing our time, as well as the impact of austerity policies and rising inequality in Europe.

He has been instrumental in raising awareness and support in Ireland and internationally in the wake of humanitarian crises including the Syrian crisis, conflict in the DRC, Haiti earthquake, East Africa food crisis, and the Nepal earthquake etc.

Jim formerly served as chair of Dóchas, the umbrella organisation for international development NGOs in Ireland and also chaired the Irish Consortium on Gender Based Violence comprised of civil society and human rights actors, the Irish Defence Forces and the Irish Government.

Jim spent over 15 years working at senior management and board level in a number of private sector and voluntary organisations before moving to South Sudan where he was involved in running a large health, water and sanitation programme as a volunteer. He subsequently worked on child rights issues in Eastern Europe before being appointed Chief Executive of Oxfam Ireland in 2008.

Jim has a Bachelor of Commerce and postgraduate degrees from University College Galway, an MBA from University College Cork and has trained on development issues in Nairobi, Ireland and the UK as well as with various UN agencies.

In 2013, his Alma Mater, University College Cork presented Jim with an alumni award for outstanding contribution to international development.

The Mechanics of Aggressive Tax Planning by Multinational Corporations

Frank Barry
School of Business
Trinity College Dublin

TIDI Development Research Seminar
November 2013

Some NGO Investigations

- ActionAid (2010, 2nd edition 2012) *Calling Time*
  - Report into the tax structures employed by SABMiller (the world's second largest beer company with a dominant share of the African market) in its interactions with Ghana

- ActionAid (2013) *Sweet Nothings*
  - Investigation into Associated British Food's Zambian subsidiary, Zambia Sugar

General Pattern

- Intellectual property (in this case *brand names*) held in zero-tax overseas jurisdictions

- Huge management fees paid to Swiss, Irish and Mauritian subsidiaries

- ‘Treaty Shopping’:
  - Large loans from South African and US commercial banks, borrowed to finance expansion in Zambia, were routed through Ireland despite being borrowed in Zambian currency and repaid via a bank account held by the Irish company in Zambia
  - Takes advantage of a clause in the Ireland-Zambia tax treaty that prevents the Zambian government imposing withholding taxes on such interest payments

1998 OECD definition of 'tax haven'

- Four criteria:
  - (i) No (or only very low rates of) tax

    This criterion on its own is not sufficient

    - Revenue-maximising corporation tax rate is lower for smaller, poorer, more peripheral, late industrialising economies

OECD criterion 2

– (ii) Lack of transparency (special deals available)

OECD criterion 3

– (iii) Secrecy laws preventing the effective exchange of information for tax purposes with other governments

Jurisdictions Ranked in Terms of Secrecy Score

Jurisdiction	Secrecy Score	Jurisdiction	Secrecy Score	Jurisdiction	Secrecy Score
Bermuda	85	Monaco	75	USA	58
Netherlands Antilles	83	Mauritius	74	Cyprus	58
Bahamas	83	Hong Kong	73	Germany	57
British Virgin Islands	81	Singapore	71	Netherlands	49
Liechtenstein	81	Luxembourg	68	United Kingdom	45
Jersey	78	US Virgin Islands	68	Ireland	44
Gibraltar	78	Austria	66	Denmark	40
Switzerland	78	Guernsey	65	Spain	34
Cayman Islands	77	Isle of Man	65		

Criterion 4

- (iv): no substantial activities
  - Vetoed by administration of George W. Bush!

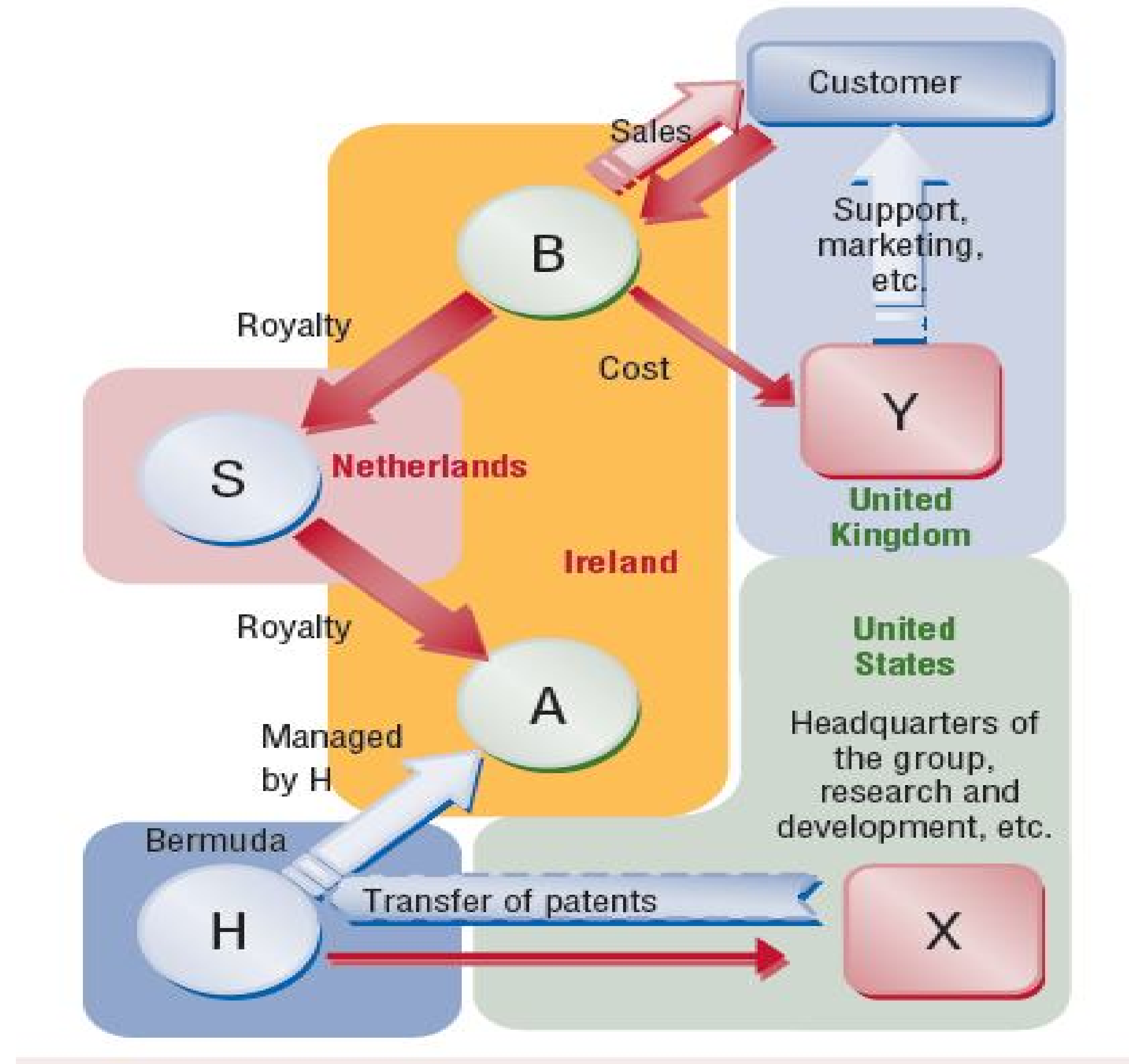
Why?

- New York Times headline of May 30 2000:

EU Complains that Use of Tax Havens gives US Firms a Competitive Advantage

  - "…. illegal effort to subsidize US exports by making them more competitive"

Structures employed by some US MNCs



Origins of Caribbean tax regimes

- During the 1920s and 1930s, Switzerland, Liechtenstein, Jersey, Panama and the Caribbean began to develop the characteristics of tax havens
- Off the shelf companies: New Jersey and Delaware in late C19th
- 'Virtual' residency (incorporation without tax residency): UK law court rulings culminating in 1929 case.

- Tax-exempt holding company: Luxembourg, 1929.
- Banking secrecy: Swiss Banking Act of 1934
- Eurodollar market
  - From 1957 Bank of England decided that transactions undertaken by UK banks on behalf of lenders and borrowers who were not located in the UK were not subject to UK regulation. However since they took place in London, no other authority could regulate them either

Brief history of US tax policy

- Until 1962, foreign subsidiaries of US corporations were able to avoid US taxation so long as their profits remained offshore ("deferral")

- Kennedy Administration proposed to switch to a different principle
  - that overseas income of US corporations should be taxed exactly the same as income earned in the US
- Congressional Republicans argued that this would damage the international competitiveness of US MNCs (who would face higher total taxes than many of their foreign competitors)

- US State Department also has an interest in the debate

The 1962 compromise

- US taxes cannot be deferred on passive income (royalties etc.... i.e. the income deriving from ownership of intellectual property)

  - "Subpart F"

US has been gridlocked on deferral ever since....

- Irish Times; Oct 11, 1975:

  "Keating Warns US of Tax Risk to Development"

  (Justin Keating, Minister for Industry & Commerce)

  - "US Legislature discussing deferral of US taxation by overseas subsidiaries of US corporations..."

- New IRS regulations (“check the box”) introduced in 1997 paved the way for creative tax-avoidance planning options.

- “… thwarts the application of Subpart F”

- The IRS rapidly tried to row back on “check the box” but corporate lobbying prevented this

- Instead, was written into law (as the Look-Through Rule)

Memo from Senator Levin, Subcommittee chairman, 20 Sept 2012

Check-the-box tax regulations issued by the Treasury Department in 1997, and the CFC Look-Through Rule enacted by Congress as a temporary measure in 2004, have reduced the effectiveness of the anti-deferral rules of Subpart F and have further facilitated the increase in offshore profit shifting, which has gained significant momentum over the last 15 years. On

- “Check the box” (CTB) allows certain foreign entities to be amalgamated for US tax purposes.

- Gave rise to the *hybrid entity*: marriage of holding company and operating company

- The holding company and the operating company are both incorporated in Ireland so by US law they are Irish companies.

- Irish law is different. The two companies are American because that's where ownership and control resides.

- The operating company is tax resident in Ireland because it has substantive operations here. The holding company is not, because it doesn't!

Did Ireland relax its laws when US "check the box" rules came in?

- No. Finance Act 1999 tightened them.

- Ireland's low corporation tax regime originated in 1956 as '*export profits tax relief*'

FABER-
CASTELL

- Ireland’s low corporation tax regime is “the unique and essential foundation stone of Ireland’s foreign investment boom”

  – Padraic White, Managing Director of the IDA (1981-90)

DIRECTORATE GENERAL FOR INTERNAL POLICIES

POLICY DEPARTMENT A: ECONOMIC AND SCIENTIFIC POLICY

Documentation for the visit to Ireland of the TAXE Committee

May 2015

EN

This document was requested by the European Parliament's TAXE Committee

AUTHOR

Prof. dr. Elly VAN DE VELDE

RESPONSIBLE ADMINISTRATOR

Dirk VERBEKEN

Manuscript completed in May 2015

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1. **CIT**

- **Context**

- Joseph P. Brothers, "From the Double Irish to the Bermuda Triangle", *Tax Analysts* 2014, 694:

On 14 October 2014, Irish Finance Minister Michael Noonan announced that the country **would be strengthening some of its domestic tax rules**, a decision undertaken partly in reaction to the negative attention wrought by the current EU investigation.

These measures include **eliminating** (though not necessarily with immediate effect) the **"management and control" exception to the tax residency rules**, so that any Irish-incorporated business entity would also and without exception be an Irish tax resident liable for tax on its worldwide income.

However, Noonan also defended other taxpayer-friendly aspects of Irish tax policy, particularly the country's 12.5% tax rate on trading income. **The EC letter does not criticize that 12.5% tax rate**.

- **Subject**

- Ireland, Country analysis 2015 (IBFD):

Any company incorporated in Ireland is generally deemed to be a **resident** for tax purposes.
This rule **does not apply to** companies carrying on, or related to companies carrying on, a trade in Ireland, provided that they are either under direct or indirect control of persons resident, or traded on a recognized stock exchange, in an EU Member State or in a tax treaty country. Companies are related if they are members of a 50% group. Previously, the common law test for corporate residence depended on **where the central management and control of the company took place**.

With effect of 23 October 2014, a company that is **incorporated in Ireland but is not tax resident there is nevertheless regarded as an Irish resident if**:

- the company is not regarded as a tax resident of any territory;
- the company is managed and controlled by an EU Member State or in a country with which Ireland has a tax treaty in force; and
- the country applies a "place of incorporation" test of residence, but not a central management and control test.

For companies incorporated before 23 October 2014, this rule is effective from **1 January 2015**.

Under the **Finance Act 2014**, **all companies incorporated in Ireland are treated as Irish resident for tax purposes with effect from 1 January 2015**. This is to remove the effectiveness of the "double-Irish" type tax avoidance schemes for companies established on or after that date. The rules will take effect for existing companies from **1 January 2021.**

- **General CIT**

- The **tax base** of a company is its **worldwide income**, after deduction of all expenses which are wholly and exclusively incurred for the purpose of the trade, subject to some specific provisions and exemptions, and after deduction of charges on income.

- **CIT rate** for **trading profits** will remain **12,5%** (resident and non-resident companies).
  Non-trading income and foreign income are also subject to the 25% rate.
  In the case of **foreign dividends**, the 12,5% rate applies if the dividends are paid by a company resident in an EU Member State or in a territory with which Ireland has a tax treaty, where certain conditions are met. In addition, the 12,5% rate applies to foreign dividends paid by a quoted company (or by its 75% subsidiary) that is not resident in either such state, if the shares of that company are regularly traded on a recognized stock exchange in an EU Member or in a tax treaty state. The rate also applies to foreign-source dividends paid out of the trading profits of private companies in territories with which Ireland does not have a tax treaty, if such a territory is party to the OECD Convention on Mutual Administrative Assistance in Tax Matters.

- **Capital gains** are subject to an effective tax rate of 33%. The disposal of a substantial interest in an offshore fund, however, attracts capital gains tax of 40%.

- **Dividend withholding tax** generally applies to payments of dividends at the 20% standard rate of income tax. However, such payments between resident companies are exempt. On interest and patent royalty payments, as well as on charges on income, tax is generally deducted at the 20% standard rate of income tax. An exemption applies in all cases for payments within 51% groups.

- **Exempt income** includes domestic dividends (with some exceptions) and income from commercially managed woodlands in Ireland.
  Special rules apply in respect of domestic dividends paid by a company that immigrates to Ireland after 3 April 2010. Domestic dividends are generally exempt, but if that company, while under the control of Irish residents, makes a distribution (i) to a connected resident company with the following 10 years, (ii) out of profits earned before it became resident in Ireland, that distribution is charged to corporation tax.
  There is an exemption from corporation tax for certain companies to trade in any of the tax years starting from 2009 until 2015. The exemption applies for 3 years from the commencement of the trade.

- **Expenses are deductible**, provided that they are incurred wholly and exclusively for the purposes of the company's trade. Interest is generally deductible, whether as trading expenses or as a charge on income. The same applies to royalty payments.
  Anti-avoidance legislation applies to limit relief for interest accrued but not paid on loans between connected companies, and for interest on loans to acquire an interest in another company where capital is recovered by a company connected to the investing company. Anti-avoidance rules also apply, in certain

circumstances, to deny relief for interest on intra-group loans taken out to finance the acquisition of fixed assets from a group company.

- **Trading losses** can be carried **forward** for an indefinite period of time; additional conditions apply depending on the type of trade carried out.
  A trading loss may be set off against other income and capital gains of the same or **preceding** accounting period (further rules apply depending on the type of trade carried on); 3 years for losses incurred in the final year of trading.

➢ **Tax incentives**

There are tax incentives (with accelerated depreciation):
- R&D tax credits (a 25% corporation tax credit applies in respect of qualifying R&D expenditure. Until 31 December 2014, the credit applied to the expenditure in excess of an amount of baseline expenditure, which was determined by reference to relevant R&D expenditure incurred in 2003. With effect from 1 January 2015, the restriction of the baseline expenditure is removed);
- tonnage tax;
- real estate investment trusts (REITs) regime (an Irish resident company incorporated in Ireland, which is listed on the main market of a recognized stock exchange in an EU Member State. REITs are exempt from corporation tax on the income and chargeable gains from property rental business. In April 2015, a new REIT guidance was released.

2. NEW GAAR

❖ David Fennell, "Finance Act 2014 – New General Anti-Avoidance and Mandatory Reporting Rules", *Irish Tax Review* 2014, 108-113 (part 1) and *Irish Tax Review* 2015, 53-60 (part 2).

❖ Brian Duffy, "Changes to Ireland's general anti-avoidance regime", *International Tax Review* (online) 2015:

The **Finance Act 2014** introduced **substantial changes to Ireland's GAAR**.

The measures **simplify the procedure** the Irish tax authority ("Revenue") must follow to withdraw any tax advantage which arose to a taxpayer as a result of a transaction the primary purpose of which was to achieve the tax advantage. A tax advantage is essentially a reduction in the tax payable.

The **New GAAR** will govern **transactions** entered into on or after 23 October 2014. Whilst the provisions contained in the New GAAR are broadly similar in principle, on further examination it is clear that in practice these changes could lead to an increase in successful challenges being made by Revenue under the current GAAR and in particular should curtail the possibility of a taxpayer successfully challenging a case on procedural grounds.

The main changes are:

- The requirement that a Revenue officer must form and issue an opinion that a transaction constitutes a tax avoidance transaction before being entitled to

withdraw a tax advantage has been removed. Under the New GAAR a Revenue officer may withdraw a tax advantage if it is reasonable to consider, based on certain considerations, that the transaction is a tax avoidance transaction. Consequently, the New GAAR removes the taxpayer's right to appeal the opinion formed by Revenue that the transaction fell within the general anti avoidance provisions on certain specified grounds.

- In line with the legislative changes made in the 2012 Finance Act there will be no time limit for raising a notice of assessment under the New GAAR.
- The surcharge which becomes payable on a Revenue finding that a transaction resulted in a tax advantage has been significantly increased from 20% to 30% of the amount of the tax advantage.
- The protective notification regime remains; if a taxpayer files a valid protective notification no surcharge will apply. If a valid protective notification is filed outside the prescribed time limits various reduced surcharges apply depending on the circumstances.
- A protective notification cannot be made where the transaction was one which should have been disclosed under the mandatory disclosure regime.
- Increased supporting documentation is now required for a valid protective notification. The taxpayer is now obliged to furnish all documentation pertaining to the transaction along with an opinion as to why the taxpayer believes the transaction is not tax avoidance and does not fall within the general anti avoidance provisions.

3. ATR

- Ireland, Corporate Taxation, Country Surveys **2015** (IBFD):

Revenue "opinions" are issued upon request where the circumstances are **complex** or a transaction is **unusual** and the existing **information services do nog provide the clarity required**. The opinions are **not legally binding**; it is open to Revenue officials to review the position when a transaction is completed and all of the facts are known."

There is no formal legislation nor procedure on ATRs. In fact, a system of "ATR" does not exist: in Ireland, Revenue "opinions" can be obtained.

- Fédération des Experts Comptables Européens, *Survey on advance tax rulings* (nineties):

"There is **not a formal system** of advance tax rulings in the Republic of Ireland.
However, practitioners do get **informal opinions** from the Revenues Commissioners – particularly, in relation to **inward investment** and the International Finance Services Centre (**IFSC**). Such opinions are **not binding** on the Revenue commissioners, but are not normally queried by them after the event."

- "Ireland", *International Survey on Advance Tax Rulings*, **2003** (IBFD).

Ireland has a well-developed **informal consultative system**, through which taxpayers may obtain **the opinion** of the Revenue **on the tax treatment of a proposed transaction or series of transactions** with **confidence that it will be adhered to**.

Although the **Irish Constitution and tax legislation** place constraints on the ability of tax officials to set limits on the application of tax legislation, the **Revenue have traditionally been willing to express opinions** in relation to the interpretation of tax legislation in particular cases. Over the past five decades, this willingness developed particularly in relation to **inward investment**, and has gradually been **extended to all taxpayers**. However, until recently, **formal guidelines** in relation to the format and content of ruling requests were practically non-existent. Only one document, Statement of Practice SP-CT/3/90, dealing with requests for entitlement to the 10% rate of tax for manufacturing activities, was issued by the Revenue.

In **July 2002**, a comprehensive set of **guidelines for taxpayers seeking a "Revenue Opinion" was released**. The emphasis on "opinions" rather than "rulings" reflects the Revenue's awareness of the constitutional and legislative constraints under which they operate. They interpret and apply tax legislation, but they do not amend or create it. The courts, also, have been scrupulous in avoiding making tax law. However, they have established that the **Revenue may be bound by opinions** given by them on a **full disclosure of all relevant facts**.

These **guidelines** specify the **type of information that should be provided** when seeking opinions, and identifies the **appropriate offices** to which they should be addressed. This **semi-formalization of the prevailing practice** falls short of the introduction of a rulings system. It is generally believed that a **more formalized ruling system cannot be introduced without a constitutional amendment**.

The amount of information available to taxpayers and practitioners on tax matters has increased significantly. During 1998, in anticipation of requests from taxpayers and their representatives, **the Revenue released, in a no-names form, an index and summaries of opinions expressed by them in response to requests from taxpayers**. The volume and user friendliness of the information available have been improved since then, with access being provided to a wealth of information via Revenue publications and their website. There is **no disclosure or publication of opinions** expressed by the revenue authorities to a taxpayer. However, opinions that are believed by the Revenue to be **of general interest** to taxpayers are usually made available on a **Revenue Precedents database**, or on a **"no-names" basis by request under the Freedom of Information Act**.

No fees are payable for an advance opinion.

- Arthur Cox, *Tax Rulings in Ireland*, Lex Mundi, **2011**:

a. Do taxpayers have the right to request a ruling from the tax authorities? If yes, please clarify if it is a constitutional right or if it is granted by tax law.

There are no "rulings" available in Ireland, however, the Irish tax authorities do on occasion give **advance opinions**. These are available either (in a small number of cases) as a matter of tax law or (more commonly) by practice. For example, in the case of certain reliefs, it is necessary to apply in advance to Revenue, whereas for other types of transaction, say large reorganisations, the Revenue will issue advance opinions on request.

b. Is the issuance of tax rulings limited to certain topics, or can they be obtained on every tax issue?

Under **tax law**, advance opinions may only be obtained on **certain topics**. As a matter of **practice**, advance opinions can be sought in respect of **any tax issue**. However, as the Irish Revenue would have limited resources, they would actively discourage issuing any form of clarification in respect of routine matters. Likewise they will not opine on a matter where anti-avoidance is concerned. There is another more generic system where a request for clarification on the interpretation of legislation can be submitted to Revenue, but the response time for that system can be a number of weeks, so it is rarely used by advisors.

[These advance rulings were generally provided on a company's qualification for Ireland's manufacturing relief. The key tax issue upon which taxpayers are requesting advance rulings from the Irish tax authorities is **whether income from a particular activity would be regarded as trading income (taxed at 12.5%) or passive income (taxed at 25%)**. In May 2003, the Irish tax authorities released a document titled Guidance on opinions on classification of activities as trading.]

[Opinions expressed by the Revenue are **specific to the taxpayer in question**. The confidentiality that surrounds all dealings between the Revenue and taxpayers ensures that details of any opinions remain confidential. The revenue state in the 2002 Guidelines: "An opinion given in relation to a specific case should not be relied on in other cases."

However, where the taxpayer or his adviser has a similar set of facts in another situation, the **constitutional requirement** under Art. 40 for **equality of treatment** of all citizens before the law provides a strong basis for insistence on application of the same tax treatment to all taxpayers.]

c. Are tax rulings definitive or can they be revoked by the tax authorities? Is a tax court authorization required to do so?

The nature of a Revenue opinion is that it is **not definitive, and can be revoked**. Revenue would however **rarely do so**, especially where they are aware that a taxpayer has implemented a transaction on foot of a Revenue opinion. Even if not revoked, the Revenue opinion should not be relied upon unless full disclosure has been made to the Revenue in the request.

[The **legal nature of advance opinions** obtained by taxpayers from the Revenue Commissioners has been considered in the Irish courts. Referring to the subordination of Inspectors of Taxes to the Revenue Commissioners in Sec. 161(1) of the ITA 1967, Blayney, J., stated: "An Inspector is not bound by a prior opinion expressed to the taxpayer by the Revenue Commissioners".

The Revenue state in the 2002 Guidelines: "Opinions given by Revenue are **not legally binding** and it is open to Revenue officials to review the position when a transaction is complete, and all the facts are known. In this regard, it is important to disclose the full facts and circumstances surrounding the transaction."

If the taxpayer does not act exactly in accordance with the proposals presented, or if these form only part of the overall picture, he may lose the benefit of the opinion.]

d. Do tax authorities have a deadline to start a tax ruling revocation process? If so, please describe the process and how long it takes.

There is no deadline for the Revenue opinion process. However, for large transactions, a response will usually be available within 2-4 weeks. For smaller transaction, it can take longer.

e. Does the taxpayer have any legal defense against a tax authority attempting to revoke a tax ruling? If so, please explain the defense.

A taxpayer could raise the defences of estoppel and **legitimate expectation**. The basis of both defenses being that the Revenue in issuing the opinion would have known or ought to have known that the taxpayer would be relying on the opinion, and had therefore a legitimate right to expect that the tax treatment would be as set out in the Revenue opinion. In response to such defenses, the Revenue might argue that as a matter of public policy it is necessary to revoke the opinion. Alternatively, they might suggest that full disclosure had not been made to Revenue.

f. What is the effect of a revocation of a tax ruling? (i.e. Is the revocation retroactive with resulting liability for the taxpayer- principle amount owing, interest, penalties, etc.- or does it take effect only from the date of the revocation?)

There is **no set formula for the effect of a revocation of a Revenue ruling**. Typically if Revenue wished to change their position on a matter, this would be done by making some form of public statement that all transactions done after a certain date would cease to benefit from a certain type of treatment, thus completed transactions would be grandfathered.

However, if they were (which would be very unusual) to withdraw an opinion after a **taxpayer had relied upon it to effect a transaction**, (and assuming the withdrawal was upheld) it would be most difficult for them to seek interest and penalties in addition to the tax, and indeed most likely they would not be successful in seeking to levy interest and penalties in those circumstances. The more usual course of action is **to prevent future transactions and not to alter the treatment of existing transactions in any event**.

4. APA

- **TP Legislation**

As part of the 2010 Finance Act, enacted in April 2010, Ireland has introduced broad-based transfer pricing legislation. Irish transfer pricing legislation formally endorses the OECD Transfer Pricing Guidelines and adopts the arm's-length principle. Therefore the documentation requirements applied under the OECD Transfer Pricing Guidelines are approved.

The new transfer pricing rules apply to arrangements entered into between associated persons (companies) on or after 1 July 2010, involving the supply or acquisition of goods, services, money or intangible assets and relating to trading activities within the

charge to Irish tax at the trading rate of 12.5%. However, an exemption from the new rules is available for small- and medium-sized enterprises.

- **APA**

There are **no specific Irish legislative provisions dealing with APAs**. However, the Irish tax authorities have been willing to negotiate and conclude bilateral advance pricing agreements with treaty partners, and they are **generally willing** to consider entering such negotiations once a case has been successfully accepted into the APA programme of the other jurisdiction. Reference is made to the EU APA Guidelines.

The Irish Revenue Commissioners are the competent authority.

A Revenue opinion may be obtained but does not have the status of a unilateral APA.
Bi- and multilateral APAs may be obtained.

The Irish tax system does not provide any related procedure rules; the reference is made to the EU APA Guidelines for the case of APAs between an Irish and other EU associated company. There is no practical experience with pre-filing meetings.

No fee.

FEATURED PERSPECTIVES

From the Double Irish to the Bermuda Triangle

by Joseph P. Brothers

Joseph P. Brothers is an associate with Caplin & Drysdale in Washington.

The ''double Irish'' tax planning strategy employed by Apple and other multinational companies has been in the mainstream press of late, as has the challenge brought by the European Union. This article explains how the strategy works, the gist of the EU position, and the reaction of the Irish government.

Recently, the EU's antitrust and competition regulators have criticized aspects of the so-called double Irish arrangement, suggesting that some details of this scheme constitute unlawful state aid from the Republic of Ireland to Apple in contravention of article 107(1) of the Treaty on the Functioning of the European Union (TFEU). The investigation relates specifically to Apple, but similar complaints could be lodged against many other firms who employ the scheme (or parts of it).

This article is divided into four parts. Section I describes the mechanics, beginning with a generalized ''double Irish Dutch sandwich'' avoidance structure. At each stage, the ways in which Apple's use of the double Irish structure differs from the typical arrangement are identified. Section II articulates the basic elements of the state aid doctrine under EU competition law and how it is relevant to the current controversy. It also describes and analyzes the EU's investigation of Apple. Section III describes measures recently undertaken by Ireland's Finance Ministry in response to the criticism. Section IV is devoted to commentary.

In brief, the Irish Finance Department's decision to toughen Ireland's idiosyncratic corporate residency determination rules is unlikely to significantly impede the basic mechanics of the strategy or to allay the EU's concerns. The double Irish structure depends most crucially on the U.S. check-the-box entity classification rules to create a hybrid entity mismatch arrangement, as well as the cost-sharing provisions of Treas. reg. section 1.482-7.

At its most basic level, the point of the structure is simply to shift income from an Irish operating subsidiary into a holding company located in a zero-tax jurisdiction, while also avoiding inclusions to the U.S. parent that might result from outbound intellectual property transfers. From the U.S. perspective, the operating subsidiary is disregarded under the check-the-box regime so that the cash flowing into the holding company does not trigger subpart F inclusions to the U.S. parent. At the same time, the separate status of the holding company is recognized for Irish tax purposes so that these payments can be deducted against the taxable income of the Irish subsidiary. The structure depends in large part on the cost-sharing rules of Treas. reg. section 1.482-7 to avoid the possibility of deemed royalty inclusions under section 367(d) or other transfer pricing adjustments between the U.S. parent and the foreign subsidiaries.

By contrast, Ireland's current management and control test for corporate residency (the rule behind the double Irish neologism) plays a much smaller role in the structure compared with the other elements. It also has attracted outsized media and regulatory attention compared with the more important factors. It appears that the EU is attacking the wrong target. It is focusing on Irish domestic tax law, when the real culprits, if any exist, are:

- the U.S. check-the-box rules;
- the U.S. cost-sharing safe harbor under Treas. reg. section 1.482-7; and

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- the general international tax principle that wholly owned shell entities located in tax havens (regardless of whether the term ''located'' means incorporated, managed, or something else) should be respected as economically independent entities rather than mere instrumentalities of their parent companies or overall corporate groups.

Accordingly, the Irish Finance Department's response (changing Ireland's corporate residency rules so that the double Irish may give way to the Irish-Bermuda) will likely prove unsatisfactory to the EU.

I. Mechanics of the Strategy

This section describes in broad terms a generalized or prepackaged double Irish or double Irish Dutch sandwich structure, and at each stage describes whether and how Apple's specific structure differs from this generalized model.

A. A Generalized Structure

A typical version of the double Irish or the double Irish Dutch sandwich structure involves at least three or four business entities. The group's top level parent is usually tax resident in the United States. In Step 1, the parent entity forms a wholly owned entity organized under the laws of Ireland but managed and controlled in a tax haven such as Bermuda (hereinafter ''Ireland HoldCo''). In Step 2, Ireland HoldCo forms another wholly owned entity at a level one tier below, which is organized, managed, and controlled in Ireland (hereinafter ''Ireland OpCo''). The lowest level operating entities are sometimes (as in Apple's case) branches or permanent establishments of Ireland HoldCo rather than separately incorporated subsidiaries (that is, ''Ireland Operating PE'' or ''Ireland Operating Branch'' rather than Ireland OpCo). But in most cases the operating entities are separately incorporated, wholly owned, Irish-registered, and Irish-controlled companies. Apple is also unique in that its version of Ireland HoldCo (the intermediate level, tax haven resident entity) is not resident in Bermuda but rather is resident ''nowhere.'' This article explains below how this subsidiary, Apple Operations International (AOI), avoids filing a residence-based tax return in any jurisdiction, in addition to skirting inbound tax obligations in any jurisdiction.

Many businesses have recently added another step to the structure. Ireland HoldCo, rather than directly forming Ireland OpCo, forms a Dutch holding entity (Netherlands HoldCo). Netherlands HoldCo, in turn, forms Ireland OpCo.

Regarding actual business operations, Ireland OpCo typically sells products to consumers in Europe and the Middle East and collects the corresponding gross receipts. Operating subsidiaries in other countries typically perform customer service and marketing functions (for example, ''France ServiceCo''); these entities are usually reimbursed on a cost or cost-plus basis by Ireland OpCo.

U.S. parent company and Ireland HoldCo jointly develop the IP embedded in the business's products. These entities typically enter into a cost-sharing arrangement in order to jointly fund and develop new IP (such as new software code). Under this arrangement, the U.S. parent typically retains the domestic IP rights as well as legal ownership of the IP, with Ireland HoldCo making a buy-in payment in exchange for the right to co-develop and exploit the software in the foreign marketplace. Ireland HoldCo sublicenses the foreign IP rights to Ireland OpCo in exchange for a royalty payment (in a Dutch sandwich scenario, there is an additional layer of sublicensing, this time from Ireland HoldCo to Netherlands HoldCo, and then from Netherlands HoldCo to Ireland OpCo). Ireland OpCo is responsible for manufacturing and selling digital products to customers in Europe and elsewhere.

Ireland OpCo is taxed on income from sales to European customers at the Irish ''trading income'' rate of 12.5 percent. However, the entity's taxable income base is reduced via the deductible royalty payments flowing up the corporate structure to Netherlands HoldCo or Ireland HoldCo. In Apple's case, the company's equivalent of Ireland OpCo does not actually sublicense the IP from further up the corporate chain; instead, it may simply sell its digital products with the IP embedded in its product inventory.

On the U.S. side, the parent minimizes potential subpart F inclusions by checking the box and electing to treat Ireland OpCo as a disregarded entity (along with Netherlands HoldCo, if it exists). This has the effect of:

- combining the foreign operations into a single entity so that the combined entity's manufacturing activities are substantial enough to prevent base company sales income; and
- causing the intra-entity royalty payments to be ignored, in order to avoid any foreign personal holding company income (FPHCI).

Graphically, the structure is shown in Figure 1.

B. U.S. Tax Treatment

1. Subpart F

Ireland HoldCo is typically a wholly owned subsidiary of the U.S. parent company. It therefore qualifies as a controlled foreign corporation under subpart F of the Internal Revenue Code.[1] Cognizant of Ireland HoldCo's controlled foreign corporation status, tax planners carefully craft the structure to ensure that little or none of the income flow taking place within it gives rise to foreign base company sales income (FBCSI) under IRC section 954(d) or FPHCI under IRC section 954(c).

[1] *See generally* IRC section 957.

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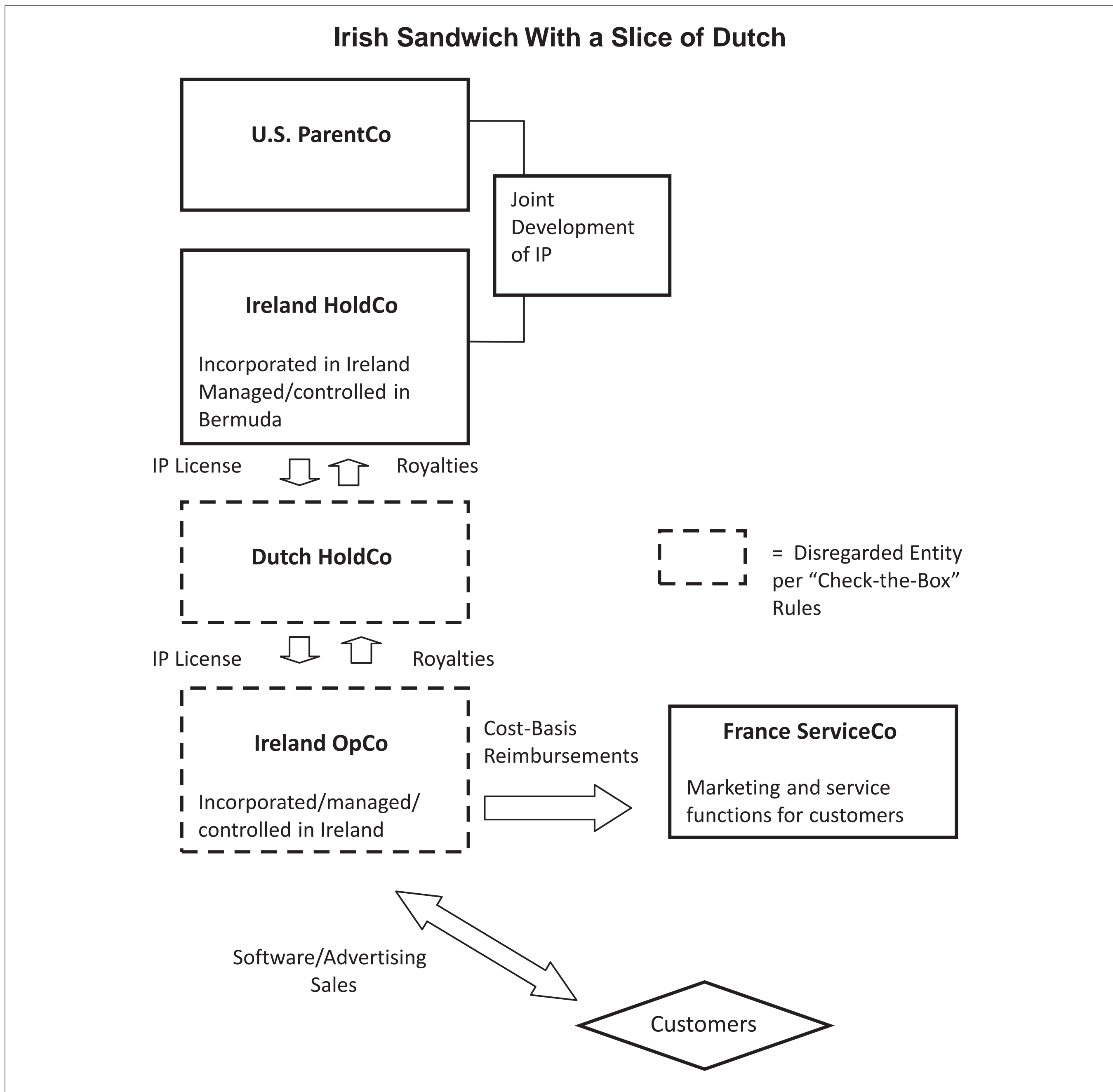

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The parent company achieves both of these objectives by electing to disregard the wholly owned Ireland OpCo (and Netherlands HoldCo conduit entity, if it exists) as separate entities for U.S. tax purposes, while retaining separate entity treatment of Ireland HoldCo.[2]

a. 'Manufacturing' activities of combined subsidiaries sufficient to avoid FBCSI. At all times during the double Irish scheme, Ireland OpCo conducts real business activity and has a tangible, physical presence in Ireland. The entity is managed and controlled in Ireland[3] and typically employs at least a handful of software engineers or other highly educated, value-adding employees. In Apple's case (and many others), Irish activities also

[2]*See generally* Treas. reg. section 301.7701-1.

[3]But not in Apple's case (Ireland Operating PE); Apple's software engineering and sales activities take place in Ireland, but the entity is managed and controlled in a tax haven jurisdiction.

include distribution and sales functions by purchasing inventory from controlled entities or third-party manufacturers and reselling them to European customers. Irish subsidiaries or branches usually participate in the joint development of new IP alongside their U.S.-based counterparts.[4]

The Ireland-based IP development activity is crucially helpful from a U.S. tax perspective, since it allows the company to credibly rely on the manufacturing exception to the FBCSI rules.[5] According to this exception, a CFC that ''substantially transforms'' the input materials into a final product or otherwise engages in activities that are ''substantial in nature'' and that are ''generally considered to constitute the manufacture, production or construction of property'' does not suffer FBCSI on the resulting sales (which would trigger income inclusions to the U.S. parent).

Treasury regulations relating to FBCSI apparently provide little guidance regarding sales of software-embedded products whose constituent components are predominantly intangible in nature. The IRS has been similarly reluctant to issue guidance on its view regarding application of the manufacturing exception in these contexts.[6] Nonetheless, firms employing the double Irish have relied on the exception in taking the position that they are not subject to the current inclusion requirements established by section 954(d).

Ireland OpCo is usually disregarded as a separately taxable entity. As such, the manufacturing activities are imputed to Ireland HoldCo, which is credited with all of the IP and software design functions that would have been limited to Ireland OpCo absent such an election.

b. Royalty payments flowing up the corporate chain are ignored, and therefore do not give rise to FPHCI. Without the election to disregard Ireland OpCo and Netherlands HoldCo as separately taxable entities, the FPHCI rules might be implicated. FPHCI might arise from Ireland HoldCo's passive receipt of royalty income from its wholly owned subsidiary Ireland OpCo or Netherlands HoldCo.[7]

However, the royalty payments are ignored for U.S. tax purposes[8] as a result of the election to disregard the lower level subsidiaries. The structure therefore gives rise to no FPHCI and thus no subpart F inclusions to the U.S. parent.

c. Same-country exception for some items of passive income (but only absent the Dutch sandwich component). FPHCI includes most forms of passive income, including royalties. However, some categories of passive income flowing to a CFC that qualify under the same country exception of section 954(c)(3) do not trigger subpart F inclusions to the U.S. parent. Interest and dividends are excluded from FPHCI if they are received from a related entity incorporated in the same country as the recipient CFC and substantially engaged in business in such country.[9] Also, rents and royalties are excluded from FPHCI if they are received from a related entity for the use of, or the privilege of using, property within the CFC's country of incorporation.[10]

Since both Ireland HoldCo and Ireland OpCo are incorporated in Ireland, and Ireland OpCo uses sublicensed IP rights (that is, ''property'') within Ireland to carry out its operations in Ireland, interest, dividend, and royalty payments from Ireland OpCo moving into Ireland HoldCo might not generally trigger subpart F inclusions even absent the check-the-box election. This rule would only matter, of course, if Ireland HoldCo were receiving payments directly from the operating subsidiary rather than through Netherlands HoldCo.

2. Avoiding Section 367(d) Deemed Royalties

A U.S. company that transfers specific items of intangible property to a foreign transferee is deemed to have sold the property in exchange for payments that are contingent upon the income generated by the property.[11] For the double Irish or the double Irish Dutch sandwich, this means that software rights transferred to Ireland HoldCo might give rise to deemed income to the U.S. parent ''commensurate with [the] income'' generated by that software.[12]

From the perspective of section 367(d), software represents an especially taxpayer-friendly form of IP in that it usually becomes obsolete not long after its initial creation. In the scheme at issue, the U.S. parent may exploit this taxpayer-friendly characteristic of software by transferring a nearly obsolete form of the code to Ireland HoldCo, then jointly developing subsequent versions alongside the Ireland HoldCo-disregarded entities group.

The U.S. parent may be required to recognize some de minimis section 367(d) income inclusions on the initial transfer, but these inclusions are usually minor because of the limited income-generating potential of that barely marketable version of the software code.

[4] *See* Treas. reg. section 1.482-7 (discussed in more detail below).

[5] *See generally* Treas. reg. section 1.954-3(a)(4).

[6] *See generally* IRS Memorandum, Vaughan #8083 (Apr. 1, 1991) (stating that the manufacturing exception would *not* be satisfied merely by imprinting completed software code onto floppy disks, but providing little guidance regarding when it *would* be satisfied).

[7] *See generally* IRC section 954(c)(2)(A), (c)(1)(A).

[8] But (fortunately) not for Irish tax purposes, as explained below.

[9] *See* IRC section 954(c)(3)(A)(i).

[10] *See* IRC section 954(c)(3)(A)(ii).

[11] *See generally* IRC section 367(d)(2)(A), (C).

[12] *Id.*

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Software updates are developed under a qualified cost-sharing arrangement between the U.S. parent and Ireland HoldCo.[13] The group's U.S. parent usually retains the legal ownership and domestic exploitation rights, while Ireland HoldCo makes a buy-in payment in exchange for the right to exploit the underlying property overseas. As long as the cost-sharing agreement remains in effect, the U.S. parent should have no additional section 367(d) income regarding the jointly developed software once the initial transfer of code (which is not particularly marketable in light of its imminent obsolescence) has occurred.

C. Foreign Tax Treatment

1. Ireland OpCo

Irish domestic corporations are generally taxed at 12.5 percent on net ''trading income'' but at a higher 25 percent rate for ''passive income.''[14]

Irish tax law does not provide a succinct or precise definition of the term ''trading income,'' but the Irish Revenue authorities have published guidance about when business activity qualifies for the taxpayer-friendly ''trading'' rate.[15] According to this guidance, key factors determining whether income from corporate operations qualifies as ''trading income'' include:

- whether value-adding activities take place in Ireland;
- whether skilled employees are located in Ireland; and
- the nature of the activities performed and the commercial rationale for locating the business in Ireland.

Ireland OpCo's net income from its European sales transactions should be taxed at the (lower) trading rate because of the IP development activities and distribution functions physically based in Ireland.

Importantly, Ireland OpCo employs a variety of techniques to minimize the taxable income base upon which this 12.5 percent rate is assessed. One of these may involve exploiting Ireland's relatively permissive transfer pricing regime. Until 2010, Ireland had an informal and loosely structured statutory scheme regarding transfer pricing. The country promulgated its first detailed transfer pricing legislation in 2010.[16] Generally, this legislation codified the arm's-length principle into Irish statutory law.

Before 2010, Ireland OpCo would exploit Ireland's lack of formal transfer pricing rules by paying an aggressively overpriced royalty in exchange for the IP sublicense (or a high price for inventory purchases) from Ireland HoldCo. Moreover, as explained below, Ireland negotiated advance pricing agreements with Apple and other firms in which the Irish transfer pricing authorities may have allowed some firms to operate at below arm's-length profit levels. The EU's current antitrust investigation is focused primarily on these taxpayer-favorable APAs. The gravamen of the EU's claim is that Ireland's *selective* acquiescence to these below arm's-length prices amounted[17] to illegal state aid to Apple (and possibly others) in violation of EU competition law.

In some circumstances, Ireland OpCo may be required to withhold taxes on the royalty payments flowing up the corporate chain to Ireland HoldCo (whether via the intermediary of Netherlands HoldCo or not). According to Irish domestic law, companies must withhold taxes on ''annual payments'' of royalties. An ''annual payment'' clearly includes payments made regarding patents, but does not necessarily include other types of royalties, such as copyright or trade secret royalties.[18] Apparently, Irish IP law is ambiguous on whether a license to use software code should be placed into the former or the latter category. Ireland OpCo typically construes this ambiguity in its favor, taking the position that its royalty payments are not captured by the ''annual payments'' provision and therefore not subject to withholding tax. As a caveat, note that these provisions of Irish law draw no distinction between resident and nonresident recipients of royalty payments. The withholding tax would apply whether the royalty payments coming out of an Irish entity are bound for another Irish entity or, for example, a Bermuda entity.[19]

The uncertainty regarding the annual payment rules may be responsible for the increasing popularity of the Dutch sandwich step. This provides additional protection to Ireland OpCo regarding its position that it is not required to withhold tax on outgoing royalty payments.

2. Ireland HoldCo

From the perspective of Irish tax law, Ireland HoldCo is not an Irish corporation but rather a resident of Bermuda (or, in Apple's case, a California resident corporation; see below). Generally, Ireland's domestic tax law follows the U.S.-style place-of-incorporation rule for determining corporate tax

[13] *See generally* Treas. reg. section 1.482-7.

[14] *See* TCA 1997, section 21 and 21A.

[15] *See* ''Guidance on Revenue Opinions on Classification of Activities as Trading,'' Irish Revenue Guidance Document, *available at* http://www.revenue.ie/en/practitioner/tech-guide.

[16] *See* 2010 Finance Act, section 42, *codified at* TCA section 835A-835H.

[17] And continue to ''amount,'' since the APAs are apparently still in force.

[18] *See In Re Hanbury,* 38 TC 588 (defining the term ''annual payment'' as a ''pure income profit''), TCA 1997, section 237.

[19] As explained below, Irish tax law considers an Irish-incorporated company managed in Bermuda to be a tax resident of Bermuda, not Ireland, so even if Irish domestic law *did* distinguish between foreign and domestic royalty recipients, the Irish incorporation of the holding entity would be without consequence on the Irish side.

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residency. However, there is an important exception. A company incorporated in Ireland may claim residency in its country of ''management and control,'' but only if two prerequisites are satisfied:

- the company must be ''in control'' of a resident Irish corporation; and
- the company must be ''controlled'' by a company that is resident in a state with which Ireland has an income tax treaty.[20]

Ireland HoldCo satisfies both of these criteria. It ''controls'' Ireland OpCo, which is fully tax resident in Ireland, and it is ''controlled'' by its U.S. parent company, which is entitled to the benefits of the Ireland-U.S. tax treaty.

Consequently, Ireland HoldCo is ordinarily not taxed by Ireland. The royalties flowing into the company's coffers from lower-tier subsidiaries therefore escape Irish income taxation that would have resulted if Ireland followed the U.S. place of incorporation rule.[21]

Also, Apple's corporate structure does not involve any entities located in tax havens such as Bermuda. In Apple's structure, the analogue to the generalized Ireland HoldCo (that is, the tax haven entity collecting the company's non-U.S. profits) is a company known as AOI. AOI is a shell entity incorporated in Ireland and whose directors mostly reside in California. It is not liable for any U.S. tax. In fact, AOI files no residency-based corporate income tax returns in any jurisdiction. From a U.S. perspective, it is resident in Ireland,[22] but from an Irish perspective, it is resident in California.[23] As a result, it has been described as being tax resident ''nowhere.''[24]

How AOI manages to avoid triggering U.S. inbound taxation is not entirely clear, but it may be on the basis of the higher inbound threshold afforded by the Ireland-U.S. tax treaty.[25]

Despite these differences, AOI fulfills a role that is substantially similar to that of an entity filing tax returns in the Cayman Islands or Bermuda (that is, declaring a tax residency, and remitting a tax of zero dollars on the basis of that residency status).

It may matter at the margin whether the generalized Ireland HoldCo is resident ''nowhere'' or resident in Bermuda, but the overall functioning of the generalized double Irish structure would seem to be minimally affected by this difference.

3. Netherlands HoldCo

Some firms,[26] especially in recent years, have elected to ''sandwich'' a Netherlands conduit entity between Ireland OpCo and Ireland HoldCo. This company acts as a tax treaty conduit entity, allowing Ireland OpCo to avoid withholding taxes that *may* be owed (but are not *necessarily* owed, as explained above) on its royalty payments to Ireland HoldCo.

According to the Ireland-Netherlands tax treaty, royalty payments may only be taxed in the country of residence (assuming the receiving entity does not have a PE in the source country).[27] Thus, Ireland OpCo is relieved of the uncertainty described above about whether it must withhold tax on the royalties under the ''annual payments'' provision of Irish domestic law. Moreover, there is no limitation on benefits clause in the Ireland-Netherlands treaty, so there is no requirement[28] that Netherlands HoldCo be anything more than a shell entity. Little or no taxable profits remain in the Netherlands, since Netherlands HoldCo pays virtually the same royalty to Ireland HoldCo as it receives from Ireland OpCo. The arrangement relies on the same bilateral treaty in mirror-image fashion to avoid Dutch withholding taxes on this second transfer. Importantly, according to Dutch domestic law, Ireland HoldCo is an Irish tax resident entitled to the benefits of the Ireland-Netherlands treaty (even though Irish domestic law regards it as a Bermuda tax resident).

The entities involved in the scheme may take additional comfort regarding their (lack of) withholding obligations from a number of EU-wide laws that seek to eliminate withholding taxes within the Union. For example, the interest and royalty directive eliminates tax on cross-border interest and royalty payments made between associated companies of different EU member states. For the purpose of the directive, two companies are ''associated'' if, in relevant part, one owns at least

[20]*See generally* TCA 1997, section 23A (defining ''control'' as 50 percent ''commonality of shareholding'').

[21]A substantially identical result would occur if the holding company had simply been incorporated in Bermuda.

[22]Perhaps because its California directors perform activity sufficient to qualify under the ''management and control'' test in Irish tax law.

[23]Those same directors *avoid* carrying out sufficient activity to trigger inbound U.S. taxation obligations.

[24]*See, e.g.,* Carl Levin and John McCain, ''Offshore Profit Shifting and the U.S. Tax Code — Part 2 (Apple Inc.),'' Memorandum — Permanent Subcommittee on Investigations (Senate Committee on Homeland Security & Governmental Affairs), 2 (May 21, 2013) (hereinafter ''Senate memorandum'') (stating that from 2009 to 2012, AOI ''reported a net income of $30 billion, but declined to declare any tax residence, filed no corporate income tax return, and paid no corporate income taxes to any national government for five years'').

[25]*See* Ireland-U.S. treaty article 4(1)(a) (defining ''resident of a Contracting state'' as a person liable to taxation on a residency

(Footnote continued in next column.)

basis under the domestic laws of either country). It is not clear how Ireland's unique tests of residency mesh with the ''liable to tax'' requirements.

[26]But not Apple, apparently.

[27]*See* Ireland-Netherlands tax treaty, articles 10(1) and 10(4).

[28]For treaty purposes, at least.

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25 percent of the other.[29] In the double Irish Dutch sandwich scheme, this requirement is easily satisfied because each subsidiary is usually wholly owned by the one above it. The interest and royalty directive attempts to ferret out abusive schemes by incorporating a general antiabuse provision in its text, but this is rarely enforced.

Finally, Dutch domestic law does not levy any withholding tax on royalty payments to nonresident companies lacking a Dutch PE.[30] Thus, even under ordinary Dutch domestic law, Netherlands HoldCo would probably not be required to withhold tax on the royalties it pays to Ireland HoldCo.

In sum, the scheme provides at least four layers of insurance regarding withholding tax obligations. If tax enforcers try to claim that the companies involved in the scheme have neglected their withholding tax obligations on royalties passing up the chain, the company under scrutiny may rely on one or more of:

- Irish domestic law;
- the Ireland-Netherlands tax treaty;
- the EU directive on interest and royalties; and
- Dutch domestic law.

II. The EU Crackdown

The EU has begun to pressure the Irish government into curbing some taxpayer-favorable rules. The crackdown has been spearheaded by the European Commission's Directorate General for Competition, State Aid Registry office.

In general, the European Commission acts as the EU's executive branch and is responsible for implementing and enforcing EU treaty law. The commission derives its jurisdiction from article 17 of the Treaty of the European Union (TEU), as well as articles 244-250 of the TFEU. These treaties, which have gradually evolved from the original legal instruments establishing the European Coal and Steel Community (ESOC), were recently ratified again by the 2007 Treaty of Lisbon.

The TEU and TFEU are directly binding on all EU member states. Article 107(1) of the TFEU forbids any EU member state from selectively providing aid to businesses in a manner that distorts competition or is otherwise ''incompatible with the common market'' among EU member states. Article 108(2) of the same treaty gives the European Commission broad authority to investigate potential violations of this prohibition, while other articles allow the commission to order a ''suspension'' of the offending aid.[31]

The commission's State Aid Registry Office is investigating whether some of Ireland's APAs, which it negotiated with Apple in 1991 and 2007 and which are still in force, amount to illegal state aid in violation of Ireland's obligations under the treaty provisions described above.

In a letter dated June 11, 2014, and published on September 30, 2014 (referred to below as ''EC letter''), European Commission Vice President Joaquín Almunia informed Ireland's Foreign Minister Eamon Gilmore that the commission was initiating a formal investigation into whether Irish transfer pricing practices regarding Apple amount to prohibited state aid in violation of the TFEU's competition rules.

According to the letter, two APAs, originally negotiated in 1991 and amended in 2007, have allowed Apple to operate several unincorporated Irish branches in the country at below arm's-length profit levels.[32] These APAs relate to two of Apple's Irish incorporated but non-tax-resident Irish branches — Apple Operations Europe (AOE) and Apple Sales International (ASI). AOE is a 100 percent owned subsidiary of AOI, which is an Irish incorporated, nonresident company lacking any branch or otherwise taxable presence in Ireland.[33] ASI is a 100 percent owned subsidiary of AOE, and is subject to Irish taxation in the same general manner as its parent company, that is, as an Irish branch or PE, but not as an Irish tax resident (ASI's management and control activities, like those of AOE, occur outside Ireland). ASI's primary function is described as:

> procurement of Apple finished goods from third-party manufacturers . . . onward sale of those products to Apple-affiliated companies and other customers, and logistics operations involved in supplying Apple products from the third-party manufacturers to Apple-affiliated companies and other companies.[34]

The EC letter argues that by allowing ASI and AOE to operate at below arm's-length profit levels, the Irish government unlawfully and selectively provided and

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[29]*See* TCA 1997, sections 267G-267L (Irish domestic legislation promulgated under the EU directive).

[30]*See generally* KPMG Country Profile — Netherlands, at 2, *available at* http://www.kpmg.com/Global/en/services/Tax/regional-tax-centers/european-union-tax-centre/Documents/eu-country-profiles/2013-netherlands.pdf.

[31]*See generally* BNA Tax Management Portfolio, ''Business Operations in the European Union,'' 999-2nd, A46(8)-(9) (2013).

[32]*See* EC letter, at 16-19.

[33]AOI also lacks any taxable presence anywhere (even in a tax haven). By analogy to the more generalized ''double Irish'' scheme described above, AOE resembles Ireland OpCo and AOI resembles Ireland HoldCo. One potentially important distinction is that AOE's Irish tax liability is imposed on the basis of its branch/PE in Ireland rather than its residency status — even though AOE maintains an office in Ireland, its management and control is situated elsewhere (perhaps in a tax haven).

[34]EC letter, at 8. AOE's Irish branch apparently ''manufactur[es] a specialized line of personal computers.'' EC letter, at 8.

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continues to provide indirect state aid to Apple that threatens the fairness of the EU's common market. In crafting its argument, the EC letter cites case law promulgated by the Court of Justice of the European Union, which has held that article 107(1)'s ban on state aid captures not only direct state subsidies but also ''measures which in various forms mitigate the charges which are normally included in the budget of a [commercial] undertaking.''[35] On the basis of this principle, the letter contends that granting Apple selectively favorable transfer pricing treatment violates the relevant article of the TFEU.

The bulk of the EC letter consists of complaints that Ireland incorrectly employed the cost-plus method in order to calculate appropriate profit levels for ASI and AOE's branch activities. The implication is that Ireland selectively permitted Apple to operate in Ireland at below arm's-length profit levels, allowing the company to misallocate what should have been ASI and AOE's profits either to other subsidiaries in the corporate group or to other taxable branches.

It is difficult to assess whether the agreed-upon cost-plus markups for ASI and AOE are appropriate or whether they are below what would be acceptable or sustainable for a company (or branch) operating at arm's length. Some experts believe the profit levels are not inappropriately low; indeed, according to knowledgeable observers, these profit levels probably are at the high end of what a similarly situated company would expect to collect. The European Commission apparently thinks otherwise.

The EC letter concludes by conveying the commission's decision to open a formal investigation into Ireland's putative violation of the state aid prohibition according to its procedural powers under article 108(2), and warns both Apple and the Irish state that ''all unlawful aid may be recovered from the recipient [Apple, in this case].''[36]

III. Irish Legislative Response

On October 14, 2014, Irish Finance Minister Michael Noonan announced that the country would be strengthening some of its domestic tax rules, a decision undertaken partly in reaction to the negative attention wrought by the current EU investigation.[37]

These measures include eliminating (though not necessarily with immediate effect) the ''management and control'' exception to the tax residency rules, so that any Irish-incorporated business entity would also and without exception be an Irish tax resident liable for tax on its worldwide income.[38] However, Noonan also defended other taxpayer-friendly aspects of Irish tax policy, particularly the country's 12.5 percent tax rate on trading income. The EC letter does not criticize that 12.5 percent tax rate. Indeed, the EU's state aid doctrine is supposedly *not* intended to affect ''legitimate'' tax competition among or between member states.

IV. Comment

In light of the heavy media and legislative attention focused on the idiosyncratic ''management and control'' test for Irish corporate residency, it is odd that the substance of the EU's state aid investigation of Ireland essentially amounts to an allegation that Irish APA negotiators *might* have committed errors in their cost-plus analysis regarding the profitability of Apple's Irish branches. As noted, the EC letter does not focus on or criticize the residency rule.

It may be that the transfer pricing complaint is just a subterfuge for venting frustration at the residency rule. After all, the state aid doctrine under EU law requires that Ireland has provided a *selective* advantage to a firm or groups of firms.[39] Ireland's management and control exception is (or was) available to any company with Irish corporate charters, so it would not provide a sufficient legal basis for a European Commission competition complaint. This may explain why the profit levels discussed in the EC letter do not seem, at first glance, to be inappropriately low; in reality, there may have been little wrong with the APAs under scrutiny. It may also shed light on why Ireland's legislative response (eliminating the double Irish possibility) is often characterized as a response to the EU's aid investigation, even though the two are not directly linked.[40]

There is, however, another possibility, which is that Ireland's residency rules may not actually play an especially important role in allowing this avoidance arrangement to work. Rather than a subterfuge for attacking Ireland's domestic tax law, the EU investigation may reflect a generalized set of grievances regarding the U.S. check-the-box rules, the cost-sharing regime, and legal fictions shared by most domestic tax laws

[35]EC letter, at 15 (*citing Adria-Wien Pipeline* (C-143/00) [2001] ECR, I-8365, para. 38).

[36]*See* EC letter, at 21 (*citing* article 14, Council Regulation (EC) No. 659/1999).

[37]*See generally* John Campbell, ''Irish budget: Michael Noonan is to abolish 'Double Irish' tax structure,'' BBC News (Oct. 14, 2014), *available at* http://www.bbc.com/news/world-europe-29613065.

[38]*See id.*

[39]*See* EC letter, at 19.

[40]*See, e.g.,* Casey Egan, ''Ireland ends 'double Irish' tax loophole favored by Apple, Google, Facebook,'' Irish Central (Oct. 15, 2014), *available at* http://www.irishcentral.com/news/Ireland-ends-double-Irish-tax-loophole-favored-by-Apple-Google-Facebook.html (''The 'double Irish' has permitted corporations registered in Ireland to be tax resident in other countries. . . . However, Ireland's allowance of the double Irish has come under heavy fire in recent months, *with European Union . . . officials calling for an end to the loophole*'' (emphasis added)).

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that allow U.S. and European value creation to be redirected to Bermuda, the Cayman Islands, or, in the case of Apple's AOI subsidiary, ''nowhere.'' The double Irish may at bottom represent a colorfully named yet fairly standard hybrid entity mismatch arrangement, one that would not necessarily be damaged by Ireland's elimination of its management and control exception.

It is probably best to explore this possibility via a counterfactual. The counterfactual assumes that in the general avoidance structure described in Section I, Ireland HoldCo has been transformed into Bermuda HoldCo (in Apple's case, assume that AOI, rather than claiming residency ''nowhere,'' asserts that it is a Bermuda resident, is run (minimally) by some Bermuda resident directors, and timely files whatever documents are required by the Bermuda authorities reflecting a residency-based Bermuda tax of nil — since Bermuda has no income tax).

On the U.S. side, most of the crucial details would function more or less identically. The check-the-box election does not require any same country showing, so the activities of the Irish operating subsidiary would still be imputed to Bermuda HoldCo, thus avoiding FBCSI. By the same token, any royalties paid from Ireland OpCo to Bermuda HoldCo would still be ignored from the U.S. perspective so that no FPHCI income would result. At the same time, these royalties would still be deductible against the trading income of the Irish operating subsidiary. The cost-sharing arrangement would not be affected.

Admittedly, Bermuda HoldCo would no longer be able to take advantage of the Irish tax treaty network, but the consequences here are not especially severe. Even if the royalties went directly to Bermuda from Ireland, Irish domestic law would likely not require a withholding tax, as noted above (and any uncertainty would relate to the eligibility of the royalty payments, not the identity of the destination country). If the royalties were indeed paid as a result of a *patent* license, thus triggering Irish withholding, this could be eliminated by routing the payments through Netherlands HoldCo and triggering available tax treaty entitlements. Dutch domestic law does not impose withholding even on patent royalties, so there would be no need to use a tax treaty on the back end of this conduit arrangement, when the royalties would be transferred from Netherlands HoldCo to Bermuda HoldCo. Bermuda HoldCo would no longer be entitled to benefits under the Ireland-U.S. tax treaty, but this never seemed to matter in the first place because Ireland HoldCo may never have been in danger of triggering inbound U.S. tax obligations (and almost surely would not be in danger of U.S. inbound taxation if the directors lived in Hamilton, Bermuda rather than Cupertino, California).

One potentially significant drawback to using Bermuda HoldCo rather than Ireland HoldCo would be that the ''same country exception'' for some passive income under subpart F would no longer be available (because the name on the corporate charter would have changed from ''Ireland'' to ''Bermuda''). However, the protection from inclusions to the U.S. parent afforded by this rule is redundant in light of the check-the-box rules. If check-the-box is eliminated, the change from Ireland HoldCo to Bermuda HoldCo may represent a more significant change. Under current law, the situation would be little different than before.

This counterfactual is intended to illustrate that the Irish ''management and control'' residency rule is not doing heavy lifting in this avoidance arrangement. The double Irish works mainly because of the hybrid entity mismatch possibilities available because of the check-the-box and the cost-sharing regime under U.S. domestic rules.[41] The elimination of the residency rule may entail significant tax costs for companies already employing the structure in terms of reorganizations or recognition events, but these costs would relate to the costs of corporate restructuring rather than any unique avoidance opportunity afforded by the residency rule itself.

In sum, whatever flaws are being exploited in structuring the double Irish, they are not related to flaws or lack of coherence in the Irish domestic tax system. As a result of Ireland's residency rule change, the double Irish may soon become the ''Bermuda Triangle''; indeed, AOI, which is tax resident ''nowhere,'' seems to have already disappeared into it. This may excite headline writers but will likely cause few problems for tax planners (at least as long as check-the-box remains in place). Accordingly, the EU is likely to be left unsatisfied. ◆

[41]In his testimony to the U.S. Senate hearings on Apple's tax structuring, Harvard Law School professor Stephen Shay said that ''In sum, for its non-U.S. sales Apple's use of cost sharing transfers the return to R&D performed in the United States to Ireland (or the ocean).'' Testimony of Stephen Shay, Permanent Subcommittee on Investigations (Senate Committee on Homeland Security & Governmental Affairs) (May 21, 2013).

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