ATAD Implementation – Interest Limitation Feedback Statement
Tax Division
Department of Finance
Government Buildings
Upper Merrion Street
Dublin 2
D02 R583

8 March 2021

Dear Sir/Madam

Subject: ATAD Implementation Article 4 Interest Limitation – Public Consultation

We are writing to you in response to your invitation for submissions on the "ATAD Implementation Article 4 Interest Limitation" Feedback Statement document as published by the Department of Finance on 23 December 2020.

First and foremost, we welcome the publication of the Feedback Statement document published by the Department of Finance. The publication of this document, prior to implementing interest limitation rules, reflects Ireland's continued efforts to promote a business environment characterised by certainty and clarity, thereby giving confidence and foresight to key stakeholders in a time of unprecedented change in the international taxation arena.

As the leading advisor to a broad base of taxpayers, ranging from indigenous entrepreneurs and Irish listed entities to foreign-owned multinationals, we can draw on our experience of dealing with complex taxation matters and reflect our concerns and insights with regard to the implementation of the interest limitation rules under the Anti-Tax Avoidance Directive.

We welcome the opportunity to discuss the matters outlined below at your convenience.

Yours faithfully,

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Broader Tax Policy Considerations

As requested by the consultation document, we have set out detailed recommendations and suggestions in response to the specific questions in the body of this submission. We would also like to take this opportunity to reflect not only on the technical concerns but also on the wider process of implementation from a tax policy perspective.

Process of implementation

We recall that the Irish Government had adopted the position that our existing domestic interest deductibility rules are equally effective to those set out in the Directive and thus Ireland would not be required to transpose ATAD Article 4 into Irish law until 1 January 2024. We note the European Commission's finding that our rules are not equally effective to those set out in ATAD, as Ireland does not use a fixed-ratio rule. The European Commission takes the view that we should not be able to rely on the deferral of the rules until 1 January 2024. Acknowledging this position, but cognisant of the existing interest deductibility rules, we are now working towards the introduction of interest limitation rules from 1 January 2022.

As discussed in more detail below, it is our opinion that layering these new rules on top of our already complex interest deductibility provisions will make Ireland both uncompetitive and will place an undue burden on taxpayers from an administrative perspective. However, we have noted that this is the proposed approach to implementation. As such we would stress the importance that these rules are brought in with the least administrative burden on taxpayers and are introduced in such a manner that does not place Ireland at an even larger competitive disadvantage than is currently envisaged by this layered approach.

We also note in the feedback statement that these rules merely result in a deferral of interest deductions rather than an outright restriction. While we understand the theory behind that view, in the majority of cases this would simply not be true in practice. For example, many companies/groups could have relatively steady state EBITDA and debt levels (and indeed the latter will often track the former) as such these rules would indeed result in an outright restriction as any deferred interest would never be utilised in practice. As such these rules will further restrict the deductions of interest for many groups whose interest costs are a bona fide economic cost of doing business.

We are aware that taxpayers have faced a raft of changes to the corporate tax code in Ireland in recent years and have needed to acclimatise to changes such as the introduction of the Controlled Foreign Company rules, the anti-hybrid mismatch rules, changes to our exit tax regime, extended transfer pricing rules and changes to the manner in which IP is depreciated for tax purposes. Taxpayers are struggling in many cases to get to grips with these changes. The introduction of interest limitation rules from 1 January 2022 is far from ideal (for reasons

that will be set out below), but we accept that this is the date that must be adopted, given pressure at EU level to implement the final measures under ATAD.

An implementation process that features stakeholder engagement at its core is the best way to allay fears over the introduction of the rules and we note that this process is a key part of this. Such a process needs to be transparent, sustainable and legitimate. It also needs to be timely. We do feel that the timelines proposed for this process are too close to the date of proposed introduction of the rules. On the basis that this consultation closes in March, with a view to beginning the second stage of consultation in late Q2 or early Q3, this is simply too close to the Finance Bill publication for a complete and comprehensive review of all of the issues to be addressed. Addressing the issue of layering of the new rules over existing legislation could take months alone.

If the timeline proceeds as expected, a best case scenario would see business not having any certainty on the draft rules until the closing of the second part of the consultation, likely in Q3. A worst case scenario with these timelines would result in legislation that has unintended consequences. We believe that waiting until late summer for some of the key concepts of these rules will be too late and will have a detrimental effect on the business community and undermine the Department's stated belief that timely engagement with stakeholders is an essential component of policy development. As such we believe that it is crucial that the next round of key definitions and concepts are shared with stakeholders as soon as possible to allow time for engagement and interaction.

An additional concern we have is that without extensive and continued ongoing engagement on these proposed interest limitation rules the final legislation could result in unintended consequences for some taxpayers as happened as a result of the proposed transfer pricing changes contained in Finance Bill 2020.

We believe that it is critical that ongoing dialogue on this matter is a critical step towards the implementation of a set of rules that are operable for taxpayers.

<u>Implementation of the rules with existing legislation</u>

A selection of Ireland's existing interest deductibility rules are set out below:

s.81 – wholly and exclusively trading loans

s.247 – interest as a charge (restrictions in s.243)

s.247(4A – 4G) anti avoidance on s.247 deductions

s.249 – recovery of capital provisions

s.97 – interest incurred in the acquisition or enhancement of property for Case V

s.130 – re-classification of interest as distribution rules

s.817C – unpaid interest

s840A – restrictions on trading interest

Taxpayers are already subject to a number of rules ensuring that interest deductions do not cause undue erosion of the tax base. In an ideal scenario, we would see the Department of Finance approach the introduction of further rules under ATAD Article 4 with a view to undertaking a "root and branch" review of all such rules. This would ensure that the ATAD rules are implemented such as to give effect to the minimum standards required and domestic rules could be fitted around this to ensure that base erosion does not take place in particularly risky arrangements. We find it difficult to understand the policy arguments for not adopting such an approach now rather than having multiple changes over a number of years that will lead to uncertainty for stakeholders over an extended period of time

However, we are aware that this is not the approach that will be adopted, and that the Department intends to layer the new rules on top of the existing domestic rules. This is disappointing and we feel it is an opportunity lost that could have been used to tidy up the range of rules already in existence.

In the absence of such a root and branch approach, we nevertheless ask that the Department give the utmost consideration to how the rules can be layered in such a way that minimises difficulties for taxpayers in applying the rules. We hope that the Department can undertake a full review of the interest deductibility rules at the earliest possible opportunity.

Peer Comparisons

Ireland has had, for many years, a complex system of interest deductibility rules through specific anti-avoidance measures and the restrictive nature of rules on intra-group financing, some of which are set out above. In contrast, many other jurisdictions adopt a much less complex legislative approach to permissible tax deductions for business related financing costs

The imposition of the ratio-based restriction as an additional layer on the current rules is undesirable and would see many taxpayers required to restructure their financing operations. It also significantly detracts from Ireland's attractiveness as a holding company location as intra-group financing becomes more difficult and adds additional compliance and administrative costs.

Other countries, on introducing the ATAD rules, abolished existing rules that sought to achieve a similar outcome, such as the French abolition of the "rabot", "carrez" and existing thin

capitalisation rules. While the French rules remain relatively complex today, the optics of abolishing rules was positive from an investor perspective and had the appearance of simplifying the existing financial expenses deduction restrictions under French law. It would be advisable that Ireland would seek to simplify existing rules wherever possible on the introduction of the new rules to achieve a similar effect.

Consultation Questions Responses

Question 1
What, if any, limited adaptations of the existing legislation could be introduced in Finance Bill 2021, to assist in effectively integrating the ATAD ILR with existing domestic rules?

We welcome the acknowledgement that the introduction of the new rules requires a simplification of the existing anti-avoidance provisions.

The purpose of the restrictions as proposed under the ATAD is to restrict debt push downs. Ireland already has certain legislation that also targets such instances such as Section 247(4A- 4G) and Section 840A in particular. As such we would welcome a removal or scale back of these rules.

With regard to Section 247, we suggest that a modification should be made to ensure that paid but unused interest can be carried forward to subsequent periods. The permanent disallowance of carried forward interest would clearly be at odds with these proposed rules.

Question 2
What, if any, further adaptations of the existing legislation could be considered in later Finance Bills?

To the extent not dealt with in the short term, the following provisions and their interaction with each other should be reviewed in the light of the introduction of the new rules:

s.81 – wholly and exclusively trading loans
s.247 – interest as a charge (restrictions in s.243)
s.247(4A – 4G) anti avoidance on s.247 deductions
s.249 – recovery of capital
s.97 – incurred in the acquisition or enhancement of property for Case V
s.130 – re-classification as distribution rules
s.817C – unpaid interest
s840A – restrictions on trading interest

The multiplicity of other anti-avoidance rules covering the same ground in Sections 817A and 817C should be removed as Section 811C covers this in any event. There should also be symmetry of treatment within groups: any interest (including deemed interest) that is non-deductible for one Irish resident company should not be a taxable receipt for another associated Irish resident company.

Overall, we would call on the Department to commit to a root and branch review of our interest deductibility rules in 2022 with a view to ensuring that our interest deductibility regime is modernised and less complex and uncompetitive versus other jurisdictions from 1 January 2023.

Question 3
Comments are invited on this possible approach, including whether any other matters should be considered in the transposition process. (More detailed questions relating to each step are contained later in this paper, so responses to this question should focus on the general approach.)

We understand the rationale behind the proposed approach as it will mean that the corporation tax computation will not need to be altered and the approach does allow the rules to be layered on top of the existing process for taxpayers. However, some consideration must be given to the overall complexity of the proposed approach, the new definitions that are required and the significant additional burden that this places on taxpayers. This further emphasises the difficulties that are associated with layering new rules onto an already complex legislative system. As such we would urge that, where possible, the rules below are simplified to the greatest extent possible and we have provided comments which we believe will help in this regard.

Question 4
Comments are invited on this possible definition of 'interest equivalent'.

As the purpose of this rule is to limit the amount of net deductible interest to 30% of EBITDA, then it would seem to follow that the concept of interest equivalent should be symmetrical as between "borrowing costs" and "taxable interest". Accordingly, we agree with the broad approach being suggested in the Feedback Statement. However, we are surprised to note that the proposed definition of borrowing costs is not as prescriptive and therefore does not appear to align with the Directive definition. We would advocate that this be corrected while preserving the symmetrical approach on the revenue side. We would propose that the following definition of interest equivalent income be used:

'Interest equivalent' means interest income on all forms of debt, other income economically equivalent to interest and income earned in connection with the raising of finance, including, without being limited to, receipts under profit participating loans, imputed interest on instruments such as convertible bonds and zero coupon bonds, amounts under alternative financing arrangements, such as Islamic finance, the finance return element of lease payments, capitalised interest included in the balance sheet value of a related asset, or the

accrual of capitalised interest, amounts measured by reference to a funding return under transfer pricing rules where applicable, notional interest amounts under derivative instruments or hedging arrangements related to an entity's lending transactions, foreign exchange gains and losses on lending transactions and instruments connected with the provision of finance, guarantee fees for financing arrangements, arrangement fees and similar income related to the borrowing of funds;

In terms of "amounts economically equivalent to interest", we make the following specific points:

- It is clear from the definition in the Feedback Statement that finance lease income/expense would be considered interest equivalent. We would seek confirmation regarding whether the financing element of operating lease payments is considered interest equivalent.
- Does the definition of interest cater for implied interest or interest arising as a result of transfer pricing adjustments?
- We believe that gains and losses on loan portfolios (including non-performing loans) and fair value movements on all forms of debt should be included as "interest equivalent".

We also make the following points and suggest inclusions for expenses incurred in connection with raising finance. To put context around this, we feel that there has been a focus on payments made which does not acknowledge that deductions are also taken for non-payments.

- In the event that loan payments are accelerated by taxpayers such that an early repayment fee is triggered, would that fee be considered equivalent to interest or an expense incurred in connection with raising finance?
- In relation to these expenses, it should be paid expenses in raising finance or to the extent that expenses are typically incurred but where they are not recognised in the P&L, we seek clarity on whether these should be calculated by reference to transfer pricing.
- We would suggest that fair value and foreign exchange related movements, as well as impairments on loans be included as part of the definition of expenses incurred in connection with the raising of finance.

Question 5

Comments are invited on these possible definitions of 'taxable interest equivalent' and 'deductible interest equivalent'.

Relevant Profits

While we note that the feedback statement states that this definition will be dealt with in the next feedback statement, it is difficult to comment on either of the above definitions without understanding relevant profits. As such we would recommend that "relevant profits" should be defined as the total profits of an entity, including chargeable gains. Our commentary below and in the other questions has taken this assumed definition.

Taxable interest equivalent

The suggested definition of taxable interest equivalent includes any amount that is "taken into account" in calculating the relevant profits of a relevant entity. In the case of a regulated fund it seems clear that the profits of the fund are "taken into account" in calculating its relevant profits before being taken out of the charge to Irish tax by the relieving provision contained within S739C TCA 1997. It would be helpful if explicit confirmation of this was provided.

Deductible interest equivalent and interaction with S291A

In addition, under the provisions of S291A interest incurred in connection with a loan to acquire qualifying IP is prima facie deductible for tax purposes, but is subject to the 80% cap on deductibility of interest and amortisation that may lead to a deferral of such expenses to later accounting periods. We suggest that the definitions are sufficiently clear that only interest actually deductible in the period under consideration is taken into account in this calculation, and that interest incurred in the period and deductible under S291A at some later date is excluded. This would also feed into the definition of "exceeding deductible interest equivalent" at 5.2 and question 6 below.

Question 6

Comments are invited on these possible definitions of 'exceeding borrowing costs' and 'exceeding deductible interest equivalent'.

As noted earlier it is critical that these key definitions ensure that there is clear symmetry between what a paying taxpayer is required to include as a "borrowing cost" and a recipient taxpayer can include as "taxable interest equivalent". For example, if a borrower is required to include the interest element of a Profit Participating Note as a borrowing cost, a lender should also be entitled to treat the return earned on its Note as interest equivalent income. See also comments at Question 5 above in relation to S291A interest deductions.

Question 7
Comments are invited on this possible definition of 'EBITDA'.

The definition of EBITDA requires the definition of relevant profits which we have discussed above and we will continue to assume that relevant profits means the total profits of a company for the purposes of our answer here.

In the definition of "I" in the formula we cannot understand the reference made to "a portion". In our view this should be simply exceeding borrowing costs. The reference to a portion is overly complex and it is not clear what it seeks to achieve.

We suggest that in the definition of "DA" that thought is given to scenarios where capital allowances are disclaimed and how this could impact upon the ultimate calculation of EBITDA.

Question 8
Comments are invited on the above possible approach to the operation of the ILR.

Utilisation of relief point

As we have set out at the beginning of this consultation, the approach being proposed is overly complex as it seeks to retrofit this Directive onto our already complex Schedular tax system with multiple tax rates. While we understand the rationale for using a Case IV approach, it is unlike any system that we are aware of that is in operation in other jurisdictions. We understand that the reason this approach is being adopted is to reduce complexity for taxpayers but this merely further signals that it is becoming increasingly difficult to retrofit EU directives and other international tax initiatives into our overly complex tax code. Rather than taking such an approach we believe that a fundamental review of our code is required to simplify rather than further complicate tax compliance and administration in this country.

If the proposed route of layering is taken, then we agree that it makes sense to apply a tax value approach to restrictions and carry forwards under the new rules. We note however that the Case IV charge cannot be offset by any " loss, deficit, expense or allowance". This could create a cash tax charge for a company in a significant current year or brought forward loss or excess capital allowances position and is clearly inequitable. We understand that this is being considered and will be rectified in future drafts of the proposed legislation.

However, for the purposes of illustrating the issues that would arise, we set out below an example (assumes that the €3m de minimis threshold applies to this taxpayer):

	EUR
Profits (none relate to interest income)	67,000,000
Deduct Taxable Interest Expense (5,000,000 of which is legacy debt) Capital Allowances	 (55,000,000) (90,000,000)
Tax Adjusted Profit/(Loss)	**(78,000,000)**
Step 5	
Exceeding Deductible Interest Equivalent Exceeding Borrowing Costs EBITDA	55,000,000 - 5,000,000 - 3,000,000 = 47,000,000 47,000,000 - 0 = 47,000,000 -78,000,000 + 47,000,000 + 90,000,000 = 59,000,000
Step 6	
A: 30% of EBITDA B: Exceeding Borrowing Costs Non-deductible interest expense B - A **Tax Impact** @ 12.5% Collected by Case IV charge with no offset allowed	59,000,000 X 30% = 17,700,000 47,000,000 47,000,000 - 17,700,000 = 29,300,000 **3,662,500**
Step 7	
Carry forward to next Accounting Period	29,300,000

As illustrated above, what is proposed is not an interest limitation rather it is the imposition of a penal charge for exceeding borrowing costs. In a true interest limitation regime the effect would be to reduce the amount of losses available for carry forward to the next period by displacing the restricted exceeding borrowing costs into a separate pool of unused interest deductions. In this example, without any offset of the Case IV charge imposed to give effect to the interest limitation the taxpayer is effectively made to pay to carry forward the higher loss from the year.

Deeming an amount to arise as Case IV income "for the purposes of the Corporation Tax Acts" could produce unintended consequences. For instance, it risks a close company surcharge of c.15% being applied on the deemed amount in addition to Corporation Tax at 25% which would be a tax charge in excess of the tax value of any restriction. To protect against such issues arising, it may be necessary to limit the effect of the deeming provision (e.g. by excluding the deemed amount from being treated as "income" for certain purposes of the Corporation Tax Acts).

Question 9
Comments are invited on this possible approach to carrying forward non-deductible 'exceeding borrowing costs'.

As we previously stated in our prior submission on this matter it is our view that Ireland should implement all three of the options with respect to carrying forward losses to give taxpayers an option of implementing any of (a), (b) or (c). We don't believe that Ireland is restricted to implementing only one of these rules. This is supported by the wording of the Directive.

As mentioned above, we also see there could be a mechanical issue with the carry forward in situations where a tax loss arises. This should be rectified to ensure that no restrictions are placed on carried forward amounts.

The legislation suggests that the entity must make a claim to carry forward the interest tax credit. It would appear to be unnecessary to force taxpayers to make such a claim.

Question 10
Comments are invited on this possible approach to carrying forward 'excess interest capacity'.

As with the carry forward of exceeding borrowing costs we would suggest that there are mechanical issues associated with the way this carry forward interacts with the rest of the legislation. We reference our comments on question 6 here.

Question 11

Comments are invited on this possible approach to the de minimis exemption, and on the potential need for anti-avoidance provisions to accompany such an exemption.

We do not believe there is any policy reason why Ireland should not introduce the de minimis threshold. We recommend that the full €3,000,000 de minimis threshold is legislated for.

To incorporate anti-avoidance provisions, we recommend that a bona fide commercial test be included with the De Minimis threshold. This would prevent artificial dis-aggregation structures.

On a point of flexibility for taxpayers we further recommend that groups be allowed to allocate the De Minimis threshold whatever way they choose within their own group.

Question 12

Comments are invited on the above possible definitions, including how single companies not coming within the ATAD definition of 'standalone entity' could be treated.

We would like to have clarity on the use of the words "fully included" in the definition of "worldwide group" and the impact that these are proposed to have on what entities should be included in a worldwide group. We have further noted this point in our answer below to question 19.

Furthermore, the definition of worldwide group includes the ultimate parent and all subsidiaries which are fully included in the ultimate consolidated financial statements. This definition should be considered in the context of subsidiaries of an "investment entity" (as defined for the purposes of the International Financial Reporting Standards ("IFRS")). Entities that meet the definition of an investment entity in accordance with IFRS 10, do not consolidate certain subsidiaries and instead measure those investments that are controlling interests in another entity (i.e. their subsidiaries) at fair value through profit and loss. Such entities are quite common in the financial services sector and if an entity is regarded as an investment entity then under IFRS it is a requirement that the results of certain subsidiaries are to be consolidated in this manner. The proposed definition of worldwide group based on the requirement to "fully" include the results of an entity could have the undesired outcome of excluding investment entities and their subsidiaries from falling within the scope of a worldwide group. If so, these entities which are in a group which fall under the scope of IFRS 10 would be adversely impacted as they would not be able to adopt a group ratio to assist with limiting the blunt nature of the fixed ratio rule, as permitted by ATAD. This will also be relevant when considering the appropriate definition for a notional Irish group.

The definition of standalone entity does cause some difficulties given the narrow interpretation of the Directive definition. Examples of standalone entities should include bankruptcy remote SPVs (such as securitisation transactions that are eligible for the repo facility of the European Central Bank and repack vehicles). Assuming these are not “part of a consolidated group for financial accounting purposes” and have no permanent establishment, the only question is whether they have any “associated enterprise”. While a standard SPV may have a 100% shareholder the shares have limited economic value (but must exist for company law purposes) and a trustee will generally hold the shares on trust for charitable purposes. This is done for good commercial reasons (including as a requirement of the European Central Bank, rating agencies and commercial lenders) so that, from an economic and insolvency perspective, the SPV is not part of a larger group (and is not in any group with the share trustee). It would seem that this fact pattern is precisely what a “standalone entity" should be. Accordingly, so long as it is not “part of a consolidated group for financial accounting purposes” and has no permanent establishment, a normal SPV, all of the shares of which are held on trust for charitable purpose for bona fide reasons should be a “standalone” entity for the purposes of the rules.

To the extent that such entities cannot fall within the definition of a standalone entity, it appears that such entities would be disproportionately impacted by the rules given the entities are not, on the face of it, capable of availing of the consolidated financial statements group provisions. We would encourage that consideration be given to allowing such entities to avail of consolidated financial statements group provisions to the extent that they cannot avail of the “standalone entity” provisions.

Furthermore, the definition of standalone entity states that the company must be “chargeable to corporation tax” on all of its profits. This is a very restrictive definition as there are numerous cases where a portion of a company’s profits may not be so chargeable.

In the definition of ultimate parent, we are unclear as to why in (b)(i) the words “results” and “fully included” are used and the primary purpose for same. It is unclear whether this section is referring to full consolidation or whether it is also attempting to take into account Joint Ventures/associates.

There are also practical issues with investments in the FS sector as some investments (in LLCs for example) will not be required to prepare financial statements and also some investment vehicles don’t consolidate their investments in the “normal” way as they hold them at fair value. In both cases the inclusion of their “results” may not be an objective exercise.

Furthermore, it is important to note that in certain circumstances an entity may be fully consolidated by two parents. This could happen where there is a listed group within the control of another ultimate listed or private group.

Question 13

Comments are invited on how Ireland might implement ATAD Articles 2(10) and 4(8), having regard to the different accounting standards and State Aid rules.

GAAPs permitted under the ICAV Act may be a useful point of reference in this regard and an extract from s116 of the ICAV Act is set out below.

> *"(4) The annual accounts may be prepared in accordance with—*
>
> *a) generally accepted accounting practice in the State,*
> *b) international financial reporting standards, or*
> *c) subject to subsection (5), an alternative body of accounting standards.*
>
> *(5) To the extent that the use of any alternative body of accounting standards does not contravene any provision of this Part, a true and fair view of the assets and liabilities, financial position and profit or loss of an ICAV may be given by the use by the ICAV of those standards in the preparation of its annual accounts.*
>
> *(6) In this section "alternative body of accounting standards" means standards that accounts of bodies corporate are to comply with which are laid down by any such body or bodies having authority to lay down standards of that kind in—*
>
> *(a) the United States of America,*
> *(b) Canada,*
> *(c) Japan, or*
> *(d) any such other country or territory as may be prescribed by regulations made by the Minister,*
>
> *as may be prescribed by regulations so made."*

Section 279 Companies Act 2014 permits certain Irish incorporated US listed companies to use US GAAP for consolidated reporting purposes, provided certain conditions are met. It is important that such groups can continue to rely on these financial statements for the purposes of these rules. We would suggest that the definitions make it clear that by virtue of Section 279 the use of US GAAP forms part of the "national financial reporting system of a Member State" as envisaged by ATAD and that the legislative definitions include the following wording after the term "international accounting standard": (or, where permitted under Section 279 Companies Act 2014, US accounting standards as therein defined")

It will be important to provide flexibility to the taxpayer in this regard in light of the international nature of many groups which operate in Ireland.

Question 14

While 'standalone entities' generally present a low risk of BEPS, the OECD notes that, in certain cases, they may be large entities held under complex holding structures involving trusts or partnerships, meaning that a number of apparently unrelated entities are in fact controlled by the same investors. What is your assessment of how the ILR could apply to such entities?

Orphan vehicles are typically Special Purpose Vehicles that should be considered a standalone entity, where it is not part of a consolidated group for financial accounting purposes, has no permanent establishment and shares are held on trust for charitable purpose for bona fide reasons. In these circumstances it should be considered a "standalone" entity for the purposes of ATAD.

We would note that the policy intent of such structures is to provide a platform to facilitate collective investment in a tax neutral manner and there are significant targeted anti-avoidance measures already in place in the Irish tax code to ensure that policy objective is achieved. Consequently, and in light of the stated policy objective within the Feedback Statement, we do not believe that any additional anti-avoidance measures beyond our existing stringent domestic anti-avoidance measures currently in place should apply to such scenarios.

Question 15

Comments are invited on the above approaches to defining and exempting "legacy debt" and more generally on the concept of a 'modification' in the context of legacy loans.

We think that trying to define the term debt is an unnecessary exercise that is overcomplicating this rule for taxpayers. It is clear that for intercompany transactions it is important that the definition goes beyond documented loans and also covers legacy undocumented debt. As such the definition should cover all debt.

Modification of an existing arrangement is being defined wider than is required by the Directive and we would recommend that it be amended to align with it. Modifications made that were provided for within the legacy arrangement and corporate restructurings should not impact grandfathering. This should also cover assignments and novations of debts between parties.

Another area that could cause certain issues would be unpaid s247 interest that is carried forward. We would suggest that such interest is also carved out as legacy debt where the accrual was incurred on legacy debt.

Question 16

Comments are invited on potential approaches to the criteria relevant to the 'long-term public infrastructure project' exemption.

Ireland has a long-established policy of encouraging investment in infrastructure projects. Therefore, this exemption is important to promote this as a long-term policy and an exemption for infrastructure loans should be provided for in the legislation.

ATAD Article 4 defines long-term public infrastructure to mean "a project to provide, upgrade, operate, and/or maintain a large-scale asset that is considered in the general public interest by a Member State". In our view, there are all manners of projects (ranging roads, broadband, aircraft, hospitals, bridges, wind farms and other projects) which could be considered to be public infrastructure projects. It is impossible to be exhaustive.

In relation to the planning system, there is a concept of strategic infrastructure assets which is set out in Schedule 7 of the Planning and Development Acts. Projects which are considered significant in a planning context, such as those noted in Schedule 7, should represent the same concepts which can be classified as public infrastructure projects. Projects can also be considered for the general public interest irrespective of whether they are privately owned or whether a fee is charged to the public for their use.

In relation to housing, it is notable that in an Irish context, housing has been subject to specific planning provisions, under the Strategic Housing Regulations which derive from the Planning and Development (Housing) and Residential Tenancies Act 2016. In a housing context, from a public policy perspective, it is notable that the State has determined that there is a public interest in the development and supply of housing. Given how public housing policy has developed, there is a strong argument for the inclusion of housing as part of the public infrastructure exemption.

In this context, we believe that a broad view should be taken on what loans qualify in this category. Furthermore, the nature of public infrastructure will always change and it is not possible to conceive now what will be the public infrastructure of the future. As a result, we recommend that there should be no exhaustive definitions and the concept of public infrastructure projects should be kept as flexible as possible. This could be achieved by providing a list of strategic projects that could be updated by the Minister from time to time as required.

Question 17

Comments are invited on the exemption generally and this possible definition of 'financial undertaking'.

We would view this as a very important exemption given the importance of the financial services industry to Ireland. We would also encourage that cognisance is given to the significant oversight of financial services groups in Ireland by the Irish regulator. In many cases, such financial services groups will include entities that, prima facie, may not fall within the definition of a "financial undertaking" as a standalone entity but are subject to significant oversight as a result of being part of a broader regulated group.

As noted in further detail in our response to Question 27, the interaction with the financial undertaking exemption and the notional local group concept are extremely important. Where an exempt financial undertaking elects to be within a notional local group they should not be treated as a financial undertaking for ILR purposes unless all other entities within the notional local group are also financial undertakings.

Finally, we would note the financial services sector and European regulation in relation to the sector is evolving at an increased pace due to technology. It appears that the Directive given definition of "financial undertaking" already appears outdated and we would encourage you to ask for European Commission commitments to a periodic review of this definition.

Question 18

If Ireland were to provide only one of the two "group ratios", which would be preferred?

It seems clear from the ATAD preamble in paragraph 7, that the EU is encouraging a taxpayer to use either of the above methods to calculate their interest restriction. We should not be approaching this decision on the basis that including any group rule is somehow being generous. The opposite is the case, not providing for a group rule could be overly restrictive, as recognised by the OECD. This is particularly the case for Ireland where, as noted at the outset and recognised in the Feedback Statement, a fixed ratio rule is not our primary defence against BEPS.

Given the optionality provided for in Article 4(5) and the assertions in both the EU ATAD and the BEPS Action 4 report that the adoption of group ratio rules should still align with BEPS aims, we strongly recommend that both options are legislated for. This provides the taxpayer with the option of adopting one method depending on their circumstances and therefore a group of taxpayers should not be adversely impacted through the implementation of these rules above another. We note that the Equity or Earnings method can each result in anomalous

results. Both options have pros and cons depending on the taxpayer's particular factual circumstances.

Earnings method:

- Earnings can be volatile. This makes it difficult to plan going forward and calculate the cost of debt for financial planning purposes – this is particularly relevant now in relation to Covid-19;
- Loss making companies may be obliged to pay tax if there is a disallowance of interest expense for tax purposes.
- The earnings method may not suit heavily capitalised industries or groups.

Equity method:

- Asset values are more stable leading to greater certainty though some asset types may be less stable than others.
- Some valuable assets (such as intangibles) may not be recognised for accounting purposes. Different accounting standards and group policies may also lead to very differing results in terms of recognition and value.

The application of either of these rules will be particularly case specific, both within particular industries, but also across different industries, and across different stages of the economic cycle.

Question 19

Noting that the same definition of 'worldwide group' applies for the "group ratios" and the definition of 'standalone entities' (see 8.2), does that alter your response to Question 12 above? Also, how could entities such as joint ventures be treated for the purpose of the "group ratios"?

Our response to Question 12 does not change as a result of the "group ratio" provisions. As noted in our response to Question 12, to the extent that certain entities cannot fall within the definition of a standalone entity, it appears that such entities would be disproportionately impacted by the rules given the entities are not, on the face of it, capable of availing of the consolidated financial statements group provisions. We would encourage that consideration be given to allowing such entities to avail of consolidated financial statements group provisions to the extent that they cannot avail of the "standalone entity" provisions.

We would also note that in Q12 we have asked for clarification with respect to the concept of "fully included" with respect to the definition of "worldwide group" and "ultimate consolidated

financial statements". To the extent that this is seeking to encapsulate JVs/associates, we believe that would be helpful in dealing with JVs for the purposes of "group ratios".

The ability for optionality with respect to whether you avail of the "group ratios" and which option you avail of will be required due to commercial situations such as JVs.

Question 20

Technical analyses are invited as to whether the "Group Ratio Rule" (third-party interest divided by EBITDA) should be calculated based on the group's consolidated accounts or using tax adjusted values. The accounting figures for EBITDA and borrowing costs may bear little resemblance to the Irish tax concepts while the tax-adjusted values give rise to practical difficulties such as how to treat intra group transactions and negative EBITDAs. Taking account of the provisions of ATAD Article 4(5)(b), and the issues identified above, how could this aspect of the "Group Ratio Rule" be designed?

The rules would not be operable unless they are based on the group's consolidated financial accounts.

Question 21

How might third-party borrowings be defined for the purpose of the "Group Ratio Rule"? Should it be borrowings excluding amounts borrowed from other members of the 'worldwide group'? Taking account of the definition of 'standalone entity' (see 8.2), which recognises that BEPS can occur between 'associates', should it also exclude borrowings with 'associates'? Accounting standards require that transactions with related parties are disclosed: should borrowings with a related party be excluded?

As these rules are not Ireland's primary defence against BEPS (as we have existing very complex targeted rules) we suggest that ensuring that these rules are as simple as possible should be the goal and, as such, following the accounts to the greatest extent possible for items such as third party borrowings. In our view anything that is classed as external debt in the consolidated accounts should be classed as external borrowings. Any concern about associate enterprises should be dealt with by our existing interest deductibility specific anti-avoidance rules (see below).

We note that the OECD Action 4 Report notes that a group ratio rule should be supported by a targeted rule to address the risk that a group ratio could be inflated using interest paid to a related party outside the group and gives examples of paying interest under a structured arrangement (e.g. a back-to-back arrangement), excessive interest payments to a related party or interest to a related party which is subject to no or low taxation on the corresponding interest income. Ireland already has targeted rules which would disallow an interest deduction in these

circumstances (e.g. Section 835AJ (Financial instrument deduction without inclusion mismatch outcome), Section 835AU (Structured arrangements), our recently amended Transfer Pricing provisions, Section 130(2)(d)(iii)(II) in respect of excessive interest etc.).

Question 22

How would the application of "group ratios" work, in practical terms, where an exempt 'financial undertaking' (see 8.5) is a member of a 'worldwide group'?

It would not be possible to "deconsolidate" one or more financial institutions from a worldwide group (and in many such groups there would be numerous financial institutions). As such the financial institutions should be left as part of the group for the worldwide ratios. The proposed concessions in the rules are there to allow highly leveraged groups to not be impacted unfairly by the restrictions or to ensure that the asset to debt profile of an entity is in line with the overall group. As such the consolidated accounts of the worldwide group including financial undertakings provide the best proxy to allow these determinations to be made. BEPS Action Paper 4 indicates that entities with tax-exempt income should continue to be regarded as part of a worldwide group (see examples 3a and 3b) when calculating the restriction. Applying the group ratio rule to groups with mixed income sources ensures that a deduction is given for a proportionate share of the interest expense which funds taxable income. The paper does not indicate that deconsolidation is required or appropriate.

Question 23

Comments are invited on the possible definitions of notional local group (including how consortia and joint ventures should be treated). In particular:

(i) How should the notional local group be defined? Should it be based on an existing definition (such as that used for group loss relief) or be a new definition?

The notional local group will need to have flexibility to cover a number of different scenarios. We would suggest that the primary test is based on the financial accounts as this aligns with the many of the other provisions discussed above. However there are also scenarios where entities that are not consolidated for financial accounting purposes (such as investment entities) should be included in the local notional group if they can be included in the losses group (s411) for corporate tax purposes. It would also be necessary that each group could choose which entities were to be included in the local notional group. This would be important as certain groups may not wish for example separate divisions to be included in a single group and as such they may actually choose to form two notional local groups.

(ii) If a new definition is adopted, are there issues relating to the interaction of a new notional local group for ILR purposes and existing group reliefs?

The key point to be considered in our view is the interaction between any non-deductible interest carry forward (i.e. "the interest tax credit") and other grouping provisions as this provision envisages the interest tax credit being offsetable against a taxpayer's broader CT charge. We would note that in all cases the maximum "value" of the interest tax credit utilised in any year is capped at the "interest capacity". Put simply, sheltering cannot be obtained above 30% of EBIDTA on a per "taxpayer" basis. We would envisage additional tracking be required from a taxpayer administrative perspective but that would be a taxpayer choice as to whether they opted into the new notional local group provision. We would welcome the opportunity to work through some examples with you on this topic.

(iii) Does the way in which the notional local group is defined impact your views on any of the other issues raised in respect of local groups?

No.

(iv) What considerations should be given to the operation of the two "group ratios" where the notional local group approach is adopted? For example, it is relatively easy for a single company to compare its balance sheet to the group consolidated balance sheet, in order to calculate if relief is available under the "Equity Ratio Rule (as detailed in section 9.3). But what difficulties might a notional local group encounter in carrying out that comparison, particularly where it does not prepare local audited consolidated accounts?

We agree that there could be complexities here given the likelihood that the notional local group, in the majority of instances, will not have consolidated financial statements. It is however difficult to comment on the method to address these complexities without understanding the proposed mechanics of the local notional group. We would therefore welcome further engagement on this matter.

Question 24
Where an optional "group approach" is provided, the following questions arise:

(i) Should a group election be irrevocable or for a finite period only?

We do not see a policy reason as to why a notional local group approach should be irrevocable or for a finite period. As well as there being no clear policy reason why such an approach would be taken, this would give rise to significant commercial issues, e.g. in merger and acquisitions activities.

(ii) What is the best way to manage carried forward amounts held both prior to the formation of the group and immediately before the cessation of the group?

Any prior year amounts carried forward should be refreshed every year and added to the current amount.

(iii) What type of anti-fragmentation rules, if any, might be required?

There should be a bona fide test included to ensure that any breaking of a group is for purely bona fide commercial reasons.

Question 25
Would a mandatory but less complex "group approach" be preferable to an optional "group approach"?

In our view it is critical that maximum optionality be given to taxpayers and as such optionality is a necessity.

Question 26
Is it practical to make a single company responsible for reporting information to Revenue on behalf of the notional local group and allocating amounts (including excess interest capacity and amounts carried forward) among group members?

Where exceeding borrowing costs and EBITDA fall to be calculated at the level of the group, the members of a group should have discretion to fully or partially allocate any restriction imposed by the Interest Limitation rules. As Ireland already has sufficient existing targeted avoidance measures to protect against base erosion from interest payments, this ATAD interest limitation rule should not impose further conditions about how a local group can, or cannot, allocate interest deductions as the group wishes within its local group. This approach would be consistent with the discretion which Irish companies currently have in the surrender of group relief among group companies, as the group so wishes. In essence we do believe it is practical for a single company to be responsible for reporting the notional local group information to Revenue but we do also see certain difficulties with the approach and, as stated above, we would urge that the rules provide maximum flexibility for taxpayers. As such we would welcome further engagement on this point and around the operation of the local notional group in general.

If so, the following questions arise:

(i) What criteria should be used to determine the reporting company?

We believe that this should be determined by the group itself similar to the VAT group remitter concept.

(ii) How should changes in group structures that alter the position of a reporting company in a group (mergers, acquisitions etc.) be managed?

Changes in the group should be notified to Revenue.

(iii) What information should be returned to Revenue by the reporting company? Should any information be reported at an entity level?

The following information should be reported:

- The companies in the notional local group for the accounting period
- The exceeding borrowing costs of the notional local group
- Whether the notional local group is relying on the 'group ratio' rule or the 'equity escape' rule, and details in that regard.
- The interest capacity and non-deductible interest of the notional local group being carried forward into that accounting period as well as any capacity and/or non-deductible interest available for carry forward to future periods.
- The allocation of any ILR charge imposed on the notional local group between the companies in the group (as noted above in a similar way to the surrender of losses).

It will also be necessary for some of this information also to be reported in each group members own tax returns.

(iv) Is there an alternate manner in which information reporting should be dealt with?

We are still considering whether, within the proposed legislative framework outlined, an alternative approach may also be viable.

Question 27

How should intragroup transactions be treated for the purpose of calculating the consolidated 'EBITDA' and 'exceeding borrowing costs' of the notional local group? ATAD Article 4(1) provides that the results of the notional local group should "comprise the results of all its members". Should the ILR be applied to the notional local group by reference to the amalgamated results of its members, or by reference to the results of the group having disregarded all intragroup transactions (akin to how an accounting consolidation is prepared)? How would this work, in practical terms, where an exempt 'financial undertaking' is a member of the notional local group?

We believe that it is very important that optionality is provided here for taxpayers. For many the simplest method of calculation will be by amalgamation of the inputs into the proposed 7 step process This would likely be the least complex manner to compute results for the notional group involving the minimum additional administration.

However, some groups may already compute consolidated financial statements for their notional local group or have straight forward group structures and in such cases it would be important that they could base their calculation on these consolidated results which would disregard intragroup transactions. The method of calculation and application could be outlined in the return for each entity within a group. The ability to disregard intra group transactions could also be very important in the context of certain notional local groups where there is no debt funding from outside the Irish group which from a policy perspective should not result in an ILR charge.

Where an exempt financial undertaking elects to be within a notional local group they should not be treated as a financial undertaking for ILR purposes unless all other entities within the notional local group are also financial undertakings.

Question 28

How should ILR restrictions be allocated among members of the notional local group? In particular:

(i) How should the notional local group allocate its exceeding deductible interest to the members of the group?

We believe that there should be maximum flexibility for the group remitter to allocate the exceeding deductible interest to the members of a group. We believe that certain mechanisms such as how group companies could pay for such could be considered (potentially in a similar manner to the existing group relief provisions).

(ii) What should happen in scenarios where the notional local group as a whole has negative EBITDA but some of its members have positive EBITDA?

As the local notional group should be considered a single taxpayer then we believe it will be the results of the group as a whole and not of the individual entities that would need to be considered.

(iii) How should excess interest capacity carried forward and/or deductible interest carried forward be operated in a notional local group scenario – should these amounts be carried at an entity or a group level?

They could be carried at either an entity or group level but it will be important that they are refreshed as an attribute of the group each year.

(iv) How should the charge (calculated under Step 6 in section 6 of this paper) be dealt with when applying the ILR to a notional local group? For example, should it be applied at the head of the group or at entity level?

See above.

(v) How should changes in membership of the notional local group be dealt with?

See above.

Question 29
Would the answers to Question 28 be different for mandatory application of the "group approach" versus optional?

As outlined above we do not believe that the group application should be mandatory.

Question 30
Where there are different accounting period end dates throughout the group, what approach should be taken to standardise and apportion group transfers of 'exceeding borrowing costs' and interest capacity?

See our answer above.

Question 31
There are provisions throughout the Tax Acts which provide for the order in which certain reliefs are deemed to be used, such as in section 403 TCA 1997. How should the interaction of the ILR and such rules be dealt with?

We believe that maximum flexibility for the taxpayer should be provided in terms of the order of offset.

Question 32
Comments are invited on any other technical issues that may require consideration.

We are still considering other technical issues, including legislative drafting and we would welcome continued engagement on such matters.