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Pillar Two consultation
Tax Division – Business Tax Policy
Department of Finance

Pillar Two Implementation - Feedback Statement March 2023
A&L Goodbody LLP Response

A Chara,

1 Introduction

We welcome the opportunity to engage with this consultation process.

We hope that there will be further opportunity to comment on the legislation as its drafting progresses prior to its implementation, in particular the drafting of the qualified domestic top-up tax (**QDTT**) provisions in due course.

2 Section 1: General Approach to Legislation

We have included in the Appendix to this submission our comments on specific sections of the draft legislation. However, there are a number of larger issues which should be considered in relation to the legislation.

Alignment with the EU Directive and OECD Model Rules

The draft legislation closely follows the EU Council Directive on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union (the **Directive**), which we consider is the correct approach to ensure consistency across all Member States.

However, we believe that there are opportunities to add clarity and simplicity to the legislation without deviating from the intended effect of the Directive. By way of example, we look to the recently published UK Finance Bill which contains draft legislation for the introduction of top-up taxes in line with the OECD Model Rules. While the substance of the legislation follows the Model Rules, its drafting does not rigidly follow the format of the Model Rules. This approach has added significant clarity to the rules, which we expect will be of great benefit for UK taxpayers in meeting their compliance obligations.

The introduction of this new tax will add significant complexity for taxpayers and, in our view, it is preferable to invest time now in drafting clear legislation. We have noted where there may be opportunities to add such clarity in the relevant sections set out in the Appendix to this submission.

The Directive is explicitly intended to follow the OECD Model Rules (the **Model Rules**) and Commentary (the **OECD Commentary**). Again, we consider this is the correct approach so that there is consistency, to the extent possible, across all jurisdictions that implement the Model Rules (whether within the EU or outside).

To this end, we suggest that an explicit statement is added to the legislation that it should be construed to ensure, as far as practical, consistency with the Model Rules and OECD Commentary current at time of enactment of the Irish legislation. This could be done in a similar way to the approach taken for transfer pricing under s.835D Taxes Consolidation Act 1997 (**TCA**). The recent UK Finance Bill 2023 also provides an example of how the OECD Commentary can be incorporated into domestic legislation.

In our view, legislative action will be required in future in order to update Irish rules to align with future iterations of OECD Commentary (similar also to the approach taken with respect to the relevant OECD transfer pricing guidelines that are applicable under Irish law at any given time). Where new OECD Commentary is issued, it will be important that this is implemented in Ireland quickly so as to minimise the possibility of inconsistent application of the minimum tax rules within a multinational enterprise group or large-scale domestic group (a **Group**) across different jurisdictions.

The process to be followed to implement updated OECD Guidance into Irish law, as far as possible, should be put in place now to facilitate the speedy implementation of the updated OECD Commentary into the Irish legislation.

In addition, Revenue guidance on this Part of the legislation will need to be kept up to date with updated OECD Commentary.

One key outstanding issue in respect of the Model Rules, is their interaction with the US GILTI regime and other CFC regimes. This is of particular relevance with respect to the interaction between GILTI and the QDTT. It is clear from the OECD Commentary that QDTTs are intended to take precedence over CFC charges generally. That being the case, it is imperative that consensus is reached on the creditability of QDTTs against CFC charges generally and, in particular, GILTI. As a small open economy with a high degree of foreign direct investment and hundreds of subsidiaries of US MNCs within scope of Ireland's proposed QDTT, this is of vital importance. It is incumbent upon Inclusive Framework members to engage on these issues as a matter of urgency so that taxpayers have clarity on how the rules will operate and double taxation is avoided.

Finally, we note the importance of introducing a territorial tax regime into Irish domestic legislation in line with the adoption of Pillar 2. We understand it is intended that this will be addressed in Finance Act 2023. The current rules on taxation of foreign dividends are extremely complex and impose a significant administrative burden for taxpayers. The Directive and Model Rules permit the exemption from tax on most dividends (other than certain short-term portfolio shareholdings and where an election has been filed to treat the dividends as taxable) so having a similar exemption under Irish domestic rules should reduce complexity for affected Groups, and for other shareholders.

Qualifying Top-Up Taxes in other Jurisdictions

As many provisions depend on whether other jurisdictions have implemented an income inclusion rule (**IIR**), undertaxed profit rule (**UTPR**), and/or a QDTT, Revenue should publish a list of jurisdictions it considers to have done so. This should, of course, be in line with those jurisdictions that have properly implemented the Model Rules.

For example, it is expected that all EU jurisdictions (other than those availing of the transitional provisions where there are 12 or fewer UPEs of MNE Groups in that Member State) will have qualifying IIRs and qualifying UTPRs (and qualifying QDTTs where they have opted to implement a QDTT) from 31 December

2023 (by virtue of having implemented the Directive). Confirmation of this should be published at an early stage.

Excluded Entities

The 2022 OECD Commentary to Article 5.1 of the Model Rules provides that the IIR and UTPR should not apply to excluded entities (as defined).

Subsection (2) of the section titled *Scope of this Part* provides that this Part shall not apply to excluded entities (as defined therein). However, this could be interpreted as merely providing that an excluded entity will not be liable to operate an IIR or UTPR in respect of low-taxed constituent entities (**CEs**) within its group or in respect of itself. We would suggest that it should be made explicit in the legislation that an excluded entity within a Group should be disregarded when computing the qualifying income or loss of CEs in a Group and covered taxes. Such change could either be made in the section titled *Scope of this Part* or in the sections dealing with computation of qualifying income or loss and covered taxes.

3 **Section 2: QDTT**

The Feedback Statement notes there are two possible approaches to applying the QDTT:

- Preparing a detailed part of the legislation to set out all of the elements require to calculate an implement a QDTT, separate and stand-alone from the parts of the legislation required to implement the IIR and UTPR; or

- Preparing shorter provision(s) which would reference the detailed provisions relating to the IIR with any necessary modifications.

We consider the second option the better course of action.

Many of the affected Groups will have to compute top-up taxes, including QDTTs, in multiple jurisdictions and so, to the extent the computation rules are similar in all relevant jurisdictions, this should make compliance easier for taxpayers.

The QDTT is permitted to be computed based on local accounting standards and we think this option should be available for Irish taxpayers.

The legislation should also make clear the order of application between the IIR, UTPR and QDTT. As currently drafted, an Irish constituent entity (**CE**) of a Group can be required to operate the IIR or UTPR in respect of itself where certain conditions are satisfied. Such entities would also be within the scope of a QDTT so it should be clarified whether they will be subject to tax under the QDTT provisions or the IIR/UTPR provisions and the extent to which one is creditable against the other.

4 **Section 3: Administration**

We agree with the proposed approach of keeping the top-up taxes separate to the existing corporation tax regime.

Registration and De-Registration

It will be important that any additional compliance obligations imposed on Group entities is not unduly burdensome.

We note the proposed 12 month deadline for a CE to register where it is a member of a Group that is within the scope of the GloBE Rules. However, we consider that this period may be too short in cases where there is particular complexity around determining whether the Group has exceeded the €750 million threshold; the general GloBE Returns are not due until 15 months after the end of the relevant fiscal year, so it may be the case that Groups are not certain until closer to that deadline whether they are within scope. This could particularly be the case in the context of a merger or demerger undertaken by a Group.

This registration should not require any more information than is necessary. In particular, it should not require taxpayers to submit details to Revenue that Revenue already has access to through another source.

Filing of GIR and Notifications

We agree with the proposed approach and would add that the obligation for a GIR to be filed by a CE in Ireland should also be discharged if a GIR is filed by any parent entity (not just an ultimate parent entity) where there is a qualifying competent authority agreement for exchange in place between Ireland and the jurisdiction where the GIR is filed.

Where there is exchange of information relating to the Model Rules (either in the EU or outside), it is important that the information exchanged does not go beyond the minimum required under the Model Rules. The purpose of such exchange should be solely to ensure compliance with the top-up taxes under the Model Rules and tax authorities should not be given information beyond what is necessary for that purpose. Tax authorities should not be entitled to request exchange of this information for any other purpose and should not be permitted to use the information provided for any purpose other than in connection with the top-up taxes.

Domestic Returns / Self-Assessment

We have no particular comments on this approach. We would ask for clarification of whether, and to what extent, this information would be shared with other tax authorities and, again, to the extent it is shared, the information should not be capable of being used other than for the purposes of compliance with the Model Rules.

Payments & Group Payments

We agree with the proposed approach.

We also consider that, even where a single entity is designated (by the Group) as the entity responsible for filing the domestic return, each CE of a Group should not be liable for any top-up tax attributable to other Group members. This is particularly important for regulated financial entities who have to carefully ringfence their liabilities to specific entities.

To the extent that the obligation to operate the IIR or UTPR arises in Ireland, only the parent entity should be liable for this tax and it should not be assessable against any other Irish CE of the Group.

General comment on reporting obligations/requirements:

Given the significant administrative burden created for taxpayers by the Model Rules, efforts should be made to reduce this burden where reasonably possible. One key way to lighten this administrative load is to have the systems for reporting and computing the tax operate consistently across jurisdictions.

The Department/Revenue should review the reporting requirements implemented across the EU and other implementing OECD jurisdictions and monitor any changes to those systems. The Irish system should be made as similar to other jurisdictions as reasonably possible, without requiring taxpayers to provide more information than what is required by the Directive and Model Rules. In terms of similarity, this should be both in terms of the information required and also the form of the return itself.

We would be happy to discuss any of the issues referred to in more detail. Please reach out to any of the below at any stage:

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Yours faithfully

A&L Goodbody LLP

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APPENDIX – Draft Legislation

1 Chapter 1: Definitions

1.1 *Definitions*

1.1.1 It should be confirmed whether any of the terms defined in s.4 TCA are used in this Part and, if so, it should be made clear that those definitions in s.4 TCA are to apply. One such example would be the defined term "generally accepted accounting practice" (see further below).

1.1.2 *"fiscally transparent entity"* is defined, but that term is not used in the draft legislation (rather, it refers to entities being "fiscally transparent" or not).

1.1.3 *"Member State"* is not defined. *"third country territory"* is defined as a territory that is not a Member State. If (presumably) Ireland is not a "Member State", it also needs to be excluded from the definition of third country territory.

1.1.4 *"parent entity"* – this definition is ambiguously drafted. Based on the description and examples contained in the OECD Commentary, we think this definition should be *"means (i) an UPE other than an excluded entity, (ii) an IPE, or (iii) a POPE"* (rather than *"means an UPE other than (i) an excluded entity, (ii) an IPE, or (iii) a partially-owned parent entity"*).

1.1.5 "*qualified IIR*", "*qualified UTPR*", and "*qualified domestic top-up tax*" are all defined terms. However, the legislation also uses the terms "qualifying IIR", "qualifying UTPR" and "qualifying domestic top-up tax*"*.

1.1.6 References to "*interest holders*" in the definition of *controlling interest* and *real estate investment vehicle*. We assume this refers to holders of ownership interests (as defined in the legislation) and suggest amending the draft to refer to "*holders of an ownership interest*". We presume (perhaps to be confirmed in guidance) that it is the beneficial owner of that interest, rather than legal owner (where different).

2 Draft Legislation – Chapter 2

2.1 *Intermediate parent entity in the State*

2.1.1 It should be possible to combine this section and the following section (*Intermediate parent entity located in the State and held by an excluded UPE*), which should make the legislation clearer to follow.

2.2 *Partially-owned parent entity in the State*

2.2.1 Where an entity that is a partially-owned parent entity (**POPE**) could also be liable as an intermediate parent entity (**IPE**) under the provisions applicable to IPEs, it should be clarified which provision will apply to the entity, i.e. will it be taxed as a POPE or an IPE.

2.3 *Effect of a qualified domestic top-up tax*

2.3.1 Subsection (1) provides that no top-up tax shall be computed in respect of any constituent entities to which a qualified domestic top-up tax (**QDTT**) has been computed in accordance with the UPE's acceptable accounting standard, or with IFRS.

2.3.2 However, subsection (3) provides that where a QDTT is applied by a Member State or third country territory, the financial accounting net income or loss of the CEs located in that Member State or territory may be determined in accordance with an acceptable financial accounting standard or an authorised financial accounting standard that is different that the financial accounting standard used in the consolidated financial statements, provided that such financial accounting net income or loss is adjusted to prevent any material competitive distortion.

2.3.3 While this is following the format laid out in the Directive, it could create unnecessary confusion in the legislation and, we believe, could be implemented in a more simplified manner which should give greater clarity to the legislation.

2.3.4 Subsection (1) could be read to suggest that a domestic top-up tax will not be a QDTT where it is based on the local acceptable financial accounting standards, which would not be in line with the OECD Model Rules.

2.3.5 We suggest amending (1) to add a third limb (c) as follows and deleting subsection (3) entirely:

(c) an acceptable financial accounting standard or an authorised financial accounting standard that is different that the financial accounting standard used in the consolidated financial statements, provided that such FANIL is adjusted to prevent any material competitive distortion

2.4 ***Application of a UTPR across the MNE group***

2.4.3 It should be possible to combine this section and the following section (*Application of the UTPR in the territory of an UPE*), which should make the legislation clearer to follow.

3 Chapter 3

3.1 ***Adjustments to determine the qualifying income or loss***

3.1.1 Subsection (4): this should be amended to clarify that this applies to transactions/transfers between CEs of the same Group.

3.1.2 Portfolio shareholdings: The effect of this provision would appear to negate the benefit of s.21B TCA (and, to some extent, the franked investment income exemption under s.129 TCA in respect of short-term portfolio shareholdings in Irish companies), as the exemption for portfolio shareholdings under the Directive and Model Rules is narrower than the exemption contained in Irish legislation. It would, therefore, be particularly useful for Revenue to issue specific guidance for affected businesses, for example, any guidance that can be offered as to appropriate methodologies that can be used to track the holding periods of portfolio shareholdings.

3.2 ***Allocation of the qualifying income or loss of a flow-through entity***

3.2.1 Subsection (5) refers to a "*reverse hybrid entity*". This term does not appear to be defined in the draft legislation, but is also used in relation to the description of a flow through entity. This term should be defined. Ideally, the definition for this purpose should be consistent with the definition of a reverse hybrid entity for the purposes of the hybrid rules under s.835AVA TCA.

4 Chapter 4: Computation of the adjusted covered taxes

4.1 ***Covered taxes***

4.1.1 (1)(c) and (d) – We request that Revenue, in its guidance, confirm what taxes it considers would fall within these descriptions / permit taxpayers to request confirmation whether a tax in another jurisdiction comes within these limbs.

5 Chapter 5: Computation of the effective tax rate and the top-up tax

5.1 *Determination of the effective tax rate*

5.1.1 Subsection (4): excludes from the computation "constituent entities, that are investment entities"; this should be "constituent entities that are excluded entities".

6 Chapter 6: Corporate restructuring and holding structures

6.1 *Application of consolidated revenue threshold to group mergers and demergers*

6.1.1 With regards to a "merger", Revenue guidance should confirm that the acquisition by a Group of a single entity, with no permanent establishments outside of the jurisdiction in which that entity is located, shall not constitute a merger, even where the Group is a large-scale domestic group (**LDG**). Such scenario should be dealt with by the section titled "*Constituent entities joining and leaving an MNE Group or LDG".*

6.1.2 Subsection (4): The drafting reflects an earlier version of the Directive. The Directive, as published, has deleted "and" at the end of (4)(a), clarifying that where a Demerged Group exceeds the €750m threshold in its first fiscal year following the demerger, it will be considered to have met the consolidated revenue threshold; rather than only where the threshold is exceed in at least two years. The Irish legislation should follow the published draft of the Directive.

6.1.3 We would also suggest that Revenue's published guidance confirms that following a demerger, all resulting groups are subject to the demerger provisions, including the group which continues to have the same UPE as before the demerger. This is, in our view, consistent with the approach set out in the OECD Commentary.

6.2 *Transfer of assets and liabilities*

6.2.1 Revenue guidance should confirm that a 'scheme of reconstruction' shall be considered a "reorganisation", provided it meets the conditions outlined at (a)-(c) of that definition, regardless of whether it effected as a merger, demerger or liquidation. Revenue should provide examples of any other transactions which it would consider similar to a merger, demerger or liquidation.

6.2.2 In the event of a reorganisation where the disposing CE's gain or loss is partially subject to tax, the part of the transaction which is not subject to tax should be treated as a reorganisation for the purposes of this Part.