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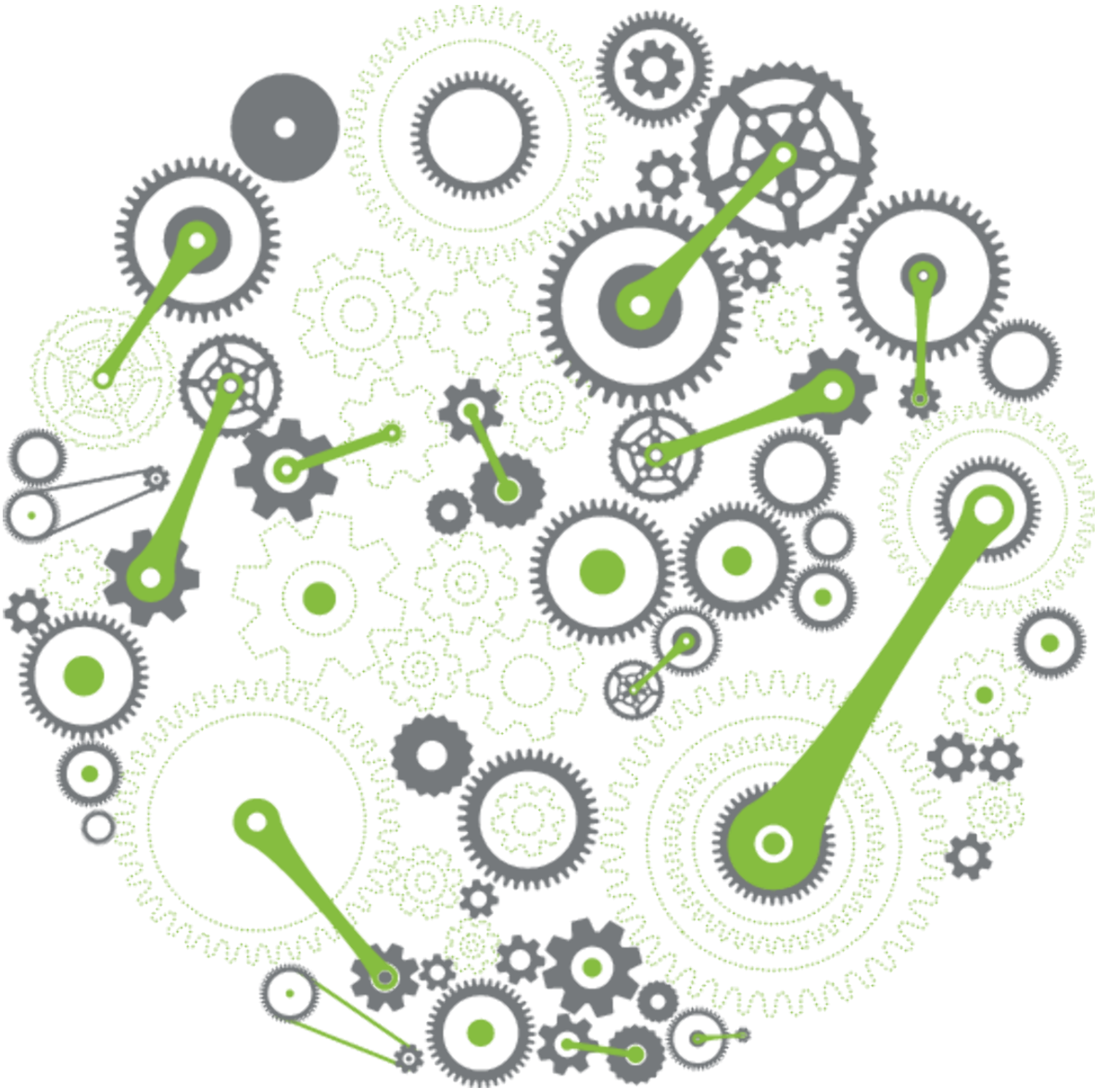

Pillar Two Minimum Tax Rate Implementation

Public Consultation Response

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Consultation on Pillar Two Proposal
Tax Division,
Department of Finance,
Government Buildings,
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Dublin 2.
D02 R583

VIA EMAIL: ctreview@finance.gov.ie

Dear Sirs/Mesdames:

We are pleased to submit comments on behalf of Deloitte in response to your Consultation paper on the Pillar Two Minimum Tax Rate Implementation. We appreciate this opportunity to share our views and trust that you will find our comments valuable to the discussion.

We look forward to continued collaboration with the Department of Finance on this and other tax initiatives, and are available to discuss anything in this document, as needed. In the meantime, if you have any queries, please do not hesitate to contact us at 01-417-2200.

Yours sincerely,

Lorraine Griffin

Tom Maguire

Lorraine Griffin	**Tom Maguire**
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Executive summary

As an overarching observation, Ireland has been a major beneficiary of globalisation in recent years. Given the significant tax contributions made by MNEs in Ireland, Pillar Two poses a risk to our finances. Accordingly, other areas of the Irish tax system and our economy in general must be adequately served to ensure that Ireland remains a competitive location in which to invest and grow businesses both from the perspective of inward investment and also domestic indigenous growth. Considerations such as high marginal personal tax rates in Ireland, the existing complexity of Irish tax legislation and incentives to drive innovation and growth in the knowledge economy are, in our view, crucial to securing our future competitiveness on the global stage. While further detail can be found in our responses to individual consultation questions, some of the key points raised are summarised below:

- A core consideration for many MNEs with a US footprint will likely be whether the GILTI ("Global Intangible Low Taxed Income") is considered a QIIR ("Qualified Income Inclusion Rule"). While uncertainties remain as to whether the proposed amendments to GILTI to align the US rules with Pillar Two principles, where GILTI is ultimately not regarded as a Qualified Income Inclusion Rule, we would argue that GILTI taxes should nevertheless be treated as Covered Taxes and allocated to the Irish constituent entities accordingly. Further consideration will need to be given as to how exactly GILTI should be apportioned across the various countries. For example, the GILTI taxes may be apportioned on the basis of profits.
- The attractiveness of the Knowledge Development Box ("KDB") may be eroded as a result of the Pillar Two rules, with a minimum effective tax rate of 15% resulting in a top up tax for companies availing of such reliefs. To preserve a benefit from the KDB, amendments should be considered to the form in which the relief is granted. Such amendments would give relief not as a deduction from taxable profits, but as a tax credit calculated as a percentage of qualifying profits.
- It is questionable whether the current R&D tax credit regime would fall to be regarded as a QRTC ("Qualified Refundable Tax Credit"). Adjustments will be necessary to the R&D credit in order to limit it being negatively affected by the proposed EU Directive.
- Further definition and clarity are required in a variety of areas including the meaning of "excluded entities" as they pertain to Irish real estate investment vehicles and in the meaning of "annual revenue" in determining whether an MNE is in scope for the rules.
- A similar comment can be made with respect to the meaning of "covered taxes", a core component in calculating the effective tax rate for a constituent entity, including bringing about greater clarity on the meaning of a "total deferred tax adjustment amount".
- The mechanism to address temporary differences contained in the proposed Directive (also referred to as the "recapture rule") may cause practical difficulties for companies claiming capital allowances for expenditure on certain intangible assets. Consideration should be given to whether the recapture rules are meant to apply to such cases.
- Overall, the introduction of a qualified domestic top up tax ("QDTUT") in Irish law as provided for by the Directive would provide for a measure of simplicity for foreign

parented groups. The QDTUT could reduce the compliance and administrative burdens on MNEs generally and should therefore be considered.

- Lastly, any top up tax (whether collected *via* the IIR, UTPR or QDTUT) should be collected separately from the corporation tax return for an entity (the Form CT1). We would also recommend against the introduction of preliminary tax payment obligations in respect of top up tax arising under Pillar Two.

Consultation Questions

General

1. Are there any specific features of the Rules that warrant particular attention with regard to their implications for Ireland's tax code and tax policy?

2. When implementing the Rules, are there any specific issues which should be considered with respect to implications for the Irish tax code arising from US corporate tax reform proposals, with particular reference to the significance of US MNEs operating in Ireland?

3. Are there other considerations of significance that should be taken into account when implementing the Rules in domestic legislation?

4. Are there any amendments needed to Ireland's existing tax code to ensure that existing legislation does not result in any unintended outcomes under the Rules when they are implemented in domestic legislation?

1. Are there any specific features of the Rules that warrant particular attention with regard to their implications for Ireland's tax code and tax policy?

Ireland has been a major beneficiary of globalisation and one of the drivers of that has been our corporate tax regime. While there are many reasons other than tax for Ireland's success (e.g., English speaking, educated workforce, GMT time zone, membership of the EU and favourable business conditions), we cannot ignore the reality that the 15% Pillar Two minimum tax will to some degree level the playing field with other competitor countries in terms of attracting MNEs. Given the significant tax contributions made by MNEs in Ireland, Pillar Two poses a significant risk to our finances. The Department of Finance has estimated that international tax reforms could reduce Ireland's corporation tax base by up to €2 billion. Accordingly, other areas of the Irish tax system and our economy in general must be adequately served to ensure that Ireland remains a competitive location in which to invest and grow businesses both from the perspective of inward investment and also domestic indigenous growth. A number of areas that should be considered in particular are our relatively high personal taxation, streamlining and simplifying our interest deductibility and double taxation rules, and improving our R&D and Knowledge Development Box regimes. We would suggest that in preparation for the introduction of the Pillar Two rules, these areas are addressed.

Our marginal personal tax rates of 52% and 55% are among the highest in the EU. It should also be noted that we have a low entry point for the higher marginal rate to apply. Ireland's high personal tax rate is a disincentive to businesses locating in Ireland, employees taking on additional work and foreign based talent (including Ireland's diaspora) relocating to Ireland. In light of the potential opportunities/risks arising out of Pillar Two, it is vital that Ireland is well positioned to attract and retain investment. We need to retain and attract talent to Ireland not only to sustain our income tax base but also our corporate tax base. People are increasingly mobile. One of the factors which will determine where such employees locate is personal tax rates. The marginal rate of tax should be reduced from its current level of 52%-55% and the entry point to the higher rate of tax should be significantly increased. We understand that a third middle rate is under consideration, and we welcome this. At the very least, a roadmap should be put in place to demonstrate to workers when this burden will be reduced. It should also be noted that personal tax rates will become a greater differentiator for the location of investment in a post BEPS world.

Existing tax legislation in Ireland is complex and multi layered. The introduction of Pillar Two rules into domestic law has the potential to add another layer of complexity. In the interests of taxpayer certainty and to ensure that the Irish tax regime remains workable and user friendly, we would recommend that serious consideration be given to streamlining and simplifying the Irish tax code. In particular, Ireland's interest deductibility rules are complex, cumbersome and are in need of urgent reform. As previously outlined in our pre-Budget 2023 submission,[1] tax relief for interest is subject to a range of conditions which has resulted in significant taxpayer uncertainty and additional compliance costs. Simplification measures such as allowing relief for interest expenses as incurred, streamlining S.247/S.249 TCA97 rules and reviewing the distribution rules in S130(2)(d) TCA97 would, in our view, be beneficial. In addition, the existing regime for the provision of double tax relief on foreign income contained in Schedule 24 TCA97 is overly complex and results in increased compliance and costs for taxpayers. The adoption of a territorial regime of taxation for foreign dividends and foreign branch income on an elective basis and the broad simplification of other areas of the Irish double tax regime would be a welcome step in reducing taxpayer compliance costs prior to the introduction of Pillar Two rules.

Many countries may change existing tax-based incentives to grants and other forms of subsidy, which are in certain circumstances treated favourably for GloBE purposes. The Government should closely monitor how other countries around the world are reacting to GloBE and in particular take steps to maintain our competitiveness.

The 15% minimum tax may not result in existing MNEs leaving Ireland, but this is a key issue to be monitored going forward. However, a question that does arise is whether Ireland will be an MNE hub for the next new technology. Given the significant contribution made by MNEs to Ireland's tax revenues, this is a critical area for consideration. In order to ensure Ireland's tax base is sustainable, we should build a first class productive and innovative SME sector which produces high value jobs (in addition to our continued efforts in the MNE sector). While Ireland has a significant number of reliefs etc. aimed at SMEs, many need to be refreshed and streamlined and should be revisited. In particular, our current SME tax system needs to be reformed to not only facilitate start–ups but also to incentivise entrepreneurs to remain and scale up their businesses. The taxation of entrepreneurs in a broad context should be addressed both in the context of personal taxation, taxation of funding/financing returns, as well as capital events. We need to ensure that our SMEs have access to capital and talent and that such companies receive the necessary support to drive research, development, and innovation. While taxation is not

[1] Deloitte Pre-Budget 2023 Submission made to the Minister for Finance on 18 July 2022.

the only factor in this, taxation can play a part. In particular, in our view, there are a number of reliefs that need to be reviewed and amended such as the Special Assignee Relief Programme (“SARP”), the Foreign Earnings Deduction (“FED”), Employment Investment Incentive (EII), Start Up Relief for Entrepreneurs (SURE), CGT Entrepreneur Relief and Key Employee Engagement Programme (“KEEP”). These reliefs have in general not met their policy objectives or there is limited uptake. A strategic review of the taxation system pertaining to SMEs should be carried out in order to create a competitive tax system.

In summary, in light of Pillar Two, Ireland should update its tax strategy to retain and attract multinationals businesses as well as developing the SME sector. This updated strategy should include: -

- A competitive corporation tax regime;
- A competitive personal tax system with a focus on lower marginal rates and targeted measures to attract key talent; and
- A tax system which is fair, certain and relatively straightforward.

2. When implementing the Rules, are there any specific issues which should be considered with respect to implications for the Irish tax code arising from US corporate tax reform proposals, with particular reference to the significance of US MNEs operating in Ireland?

US law already includes a minimum tax in the form of the GILTI (“Global Intangible Low-Taxed Income”). GILTI is not currently considered a Qualified Income Inclusion Rule, in particular as GILTI applies on a global basis rather than a jurisdictional basis. As a result, low tax profits from one jurisdiction can be blended with high tax profits of another jurisdiction to bring the overall effective tax rate down for GILTI purposes. The Build Back Better Act (“BBBA”) includes proposed changes to amend GILTI so that the minimum tax applies on a jurisdiction-by-jurisdiction basis. BBBA also increases the GILTI tax rate to 15%. However, the progress of BBBA has stalled in the US Senate, with Republicans unanimously opposed and one Democratic senator, Joe Manchin holding out his vote due to the scope of the BBBA. Whether the BBBA will pass is currently uncertain. Given the uncertainty in the US developments, retaining a flexible approach to the Irish implementation would in our view be advisable.

In the event that the expected amendments to GILTI are not passed, greater complications will no doubt arise in applying Pillar Two to multinational groups involving the US. In particular, if the US does not amend GILTI, then Irish subsidiaries of US MNEs may need to apply the IIR or the UTPR to some or all of profits of a US group .e.g., the IIR/UTPR may need to be applied by the Irish group entities to Irish profits, US profits and rest of world profits. At the same time, the US will also possibly tax the same profits under GILTI. The questions then are firstly whether any GILTI taxes are Covered Taxes for the purposes of Pillar Two and secondly, if such GILTI taxes are Covered Taxes, can they be allocated to other jurisdictions for the purposes of GloBE. In the absence of GILTI being treated as a Covered Tax allocable to other jurisdictions for the purposes of GloBE, then double taxation is likely to arise (unless the US allows any top up tax as a credit against GILTI).

In respect of the first question, in our view, there are arguments that GILTI taxes should be considered Covered Taxes for the purposes of the Directive. Article 19.1 of the Directive states that *"The covered taxes of a constituent entity shall include: (a) taxes recorded in the financial accounts of a constituent entity with respect to its income or profits, or its share of the income or profits of a constituent entity in which it owns an ownership interest*". GILTI tax paid by a US parent in respect of a non-US subsidiary should be considered a tax on the US parents share of the profits of a constituent entity. Also, Para 38 of the OECD commentary states that "*[o]n the other hand, an ordinary domestic minimum tax that is not a Qualified Domestic Minimum Top-up Tax is a Covered Tax if it otherwise meets the definition of a Covered Tax".*

The second question is whether such GILTI taxes can be allocated to non-US jurisdictions for the purposes of the GloBE rules. In order to allocate the GILTI taxes, the GILTI taxes must be considered Covered Taxes under a controlled foreign company tax regime. In particular, Article 23.3 states that "*a constituent entity shall be allocated the amount of any covered taxes included in the financial accounts of its direct or indirect constituent entity-owners under a controlled foreign company tax regime,* on their share of the controlled foreign company's income*"* Article 3.14 of the Directive states that *"controlled foreign company tax regime means a set of tax rules, other than a qualified IIR, under which a direct or indirect shareholder of a foreign entity ….., is subject to taxation on its share of part or all of the income earned by that foreign constituent entity, irrespective of whether that income is distributed to the shareholder.*" Broadly, a qualified IIR is an IIR that adheres to the Directive or the OECD Pillar Two agreement. Thus, it would seem that GILTI is not currently a qualified IIR and thus arguably is a controlled foreign company tax regime. As such in computing the top up tax for each jurisdiction (.i.e., jurisdictions other than the US or Ireland), it is arguable that GILTI taxes should be taken into account as a Covered Tax when computing the ETR for GloBE purposes.

Also, it should be noted that current Revenue practice in respect of anti-hybrid rules is to treat GILTI as a CFC charge. Therefore, we would be of the view that in the interests of consistency, GILTI should also be treated as a CFC tax regime.

Further consideration will need to be given as to how exactly GILTI should be apportioned across the various countries. For example, the GILTI taxes may be apportioned on the basis of profits.

BEAT

The BEAT targets large US corporations that make deductible payments, such as interest, royalties, and certain service payments (Includes depreciation or amortization on the acquisition of property from related parties and reinsurance payments), to related foreign parties thus eroding the US tax base. BEAT operates as follows: -

(i) A US corporation calculates its regular US tax, at a 21% rate,
(ii) The US corporation then recalculates its tax at a lower BEAT Rate after adding back the deductible payments (the modified taxable income); and
(iii) If the regular tax is lower than the BEAT, then the corporation must pay the regular tax plus the amount by which the BEAT exceeds the regular tax.

The BEAT Rate is 10% through to 2025, and 12.5% in 2026 and beyond. Effectively, BEAT imposes an alternative minimum corporate tax liability.

Consideration will need to be given to whether BEAT is a Covered Tax for the purposes of the GloBE rules. As mentioned, Article 19.1 of the Directive states that *"The covered taxes of a constituent entity shall include: (a) taxes recorded in the financial accounts of a constituent entity with respect to its income or profits, or its share of the income or profits of a constituent entity in which it owns an ownership interest*". Arguably, BEAT is not in respect of an entity's "income or profits" as BEAT is calculated by reference to a higher amount .i.e., the income or profits for BEAT purposes is calculated after disallowing (adding back) interest/royalties etc. However, para 27 of the OECD Commentary states that *"Accordingly, the definition of Covered Taxes includes Taxes that allow for a simplified estimate of net profit. For example, a Tax that allows deductions for some but not all expenses related to the relevant income would be considered an income tax, provided the deductible expenses can reasonably be considered to have been incurred in connection with deriving that income."* In addition, para 38 of the OECD commentary states that "*[o]n the other hand, an ordinary domestic minimum tax that is not a Qualified Domestic Minimum Top-up Tax is a Covered Tax if it otherwise meets the definition of a Covered Tax".* It is arguable that BEAT is an *"ordinary domestic minimum tax."* In summary, we would be of the view that BEAT should be a Covered Tax. Consideration should be given to making it explicit in Irish legislation that BEAT and similar alternative minimum taxes are Covered Taxes, thereby providing groups with certainty.

The inclusion of BEAT within the definition of Covered Taxes would have the effect of properly reflecting all taxes on not only the entity's income or profits but on simplified estimates of net profits. Such an inclusion would take into account the greater range of taxes that can be levied on a constituent entity and would provide greater certainty for MNEs with a US footprint.

<u>Interaction with QDTUT</u>

In the event that GILTI is amended with the effect that GILTI is a qualifying IIR, then it should be noted that a US group will have to two sets of calculations being GILTI and a QDTUT. Consideration should be given to flexibility in the application of such provisions.

3. Are there other considerations of significance that should be taken into account when implementing the Rules in domestic legislation?

We would recommend that the Pillar Two rules are introduced as a standalone part of TCA97 (.e.g., Part 35E) and include a section to the effect that the GloBE rules are applied after the calculation of domestic corporate/income tax .i.e. a section similar to 835AAO TCA 1997 which states "*this Part shall apply after all provisions of the Tax Acts and the Capital Gains Tax Acts.".*

To the extent possible, the Irish legislation should follow the wording of the Directive and use the same terminology. Where terms are undefined in the Directive, Irish legislation should to the extent possible define such terms drawing on the OECD commentary and accounting standards. Such an approach has the advantage of familiarity, in particular for foreign investors and should provide groups with a level of certainty as to how the Irish rules will operate.

Drafting Irish legislation in such a way to cover every potential scenario addressed in the OECD Commentary and elsewhere will ultimately lead to long overly prescriptive legislation. While the intention of such an approach may be to add clarity, in our view such an approach will not achieve that objective. We would urge that long overly prescriptive legislation is avoided. Instead, consideration should be given to including a provision similar to that used in S.835D (2) TCA 1997[2], to the effect that Irish domestic Pillar Two rules should be "construed, as far as practicable", consistently with the OECD Pillar Two commentary. It should be noted that recital 19a of the draft Directive states that "…*in implementing this Directive, Member States should use the 'Tax Challenges Arising from the Digitalisation of the Economy Global Anti-Base Erosion Model Rules (Pillar Two)' agreed by the OECD/G20 Inclusive Framework on BEPS and the explanations and examples in the OECD Commentary on the GloBE Rules under Pillar Two , ….as a source of illustration or interpretation in order to ensure consistency in application across Member States to the extent that they are consistent with the provisions of this Directive and with Union law…".* It should be remembered that these rules will need to be drafted not only to interact with Irish tax law, but also with foreign tax law.

Ultimately, the Pillar Two rules should provide simplicity (so far as possible) and clarity, so businesses can understand how much tax they should be paying, and also to provide certainty so that businesses can plan ahead. It should be noted that while the complexity of tax legislation may not be a primary reason driving where an MNE locates its operations, it nonetheless is a relevant factor. Many potential investors into Ireland cite the complexity of Irelands Double Taxation Relief regime and interest deductibility rules as a negative when weighing up whether to locate to Ireland. Thus, Ireland should not add to this by introducing similarly overly complex Pillar Two rules.

While Ireland should faithfully implement the Directive, we would also recommend that Ireland does not go any further than is necessary to comply with the Directive. We are a small open economy, and we need to be cognisant that any provisions more onerous than those prescribed in the Directive will put us at a competitive disadvantage relative to our competitors.

We would recommend that the full text of the proposed draft legislation is circulated as early as possible as part of a Feedback Statement process in order that taxpayers, practitioners, and other stakeholders have an opportunity to provide feedback on same, thus ensuring matters are dealt with in a timely manner.

[2] "Principles for construing rules in accordance with OECD Guidelines" included in Part 35A Transfer Pricing

4. Are there any amendments needed to Ireland's existing tax code to ensure that existing legislation does not result in any unintended outcomes under the Rules when they are implemented in domestic legislation?

Knowledge Development Box

The KDB provides broadly that profits from patented inventions and copyrighted software (qualifying assets) earned by an Irish company can, to the extent it relates to Research and Development ("R&D") undertaken by that company, be effectively taxed at a rate of 6.25 per cent. The current KDB regime is an OECD-compliant intellectual property ("IP") regime as it is fully aligned with the Action 5 (Harmful Tax Practices) minimum standard.

Due to a number of factors the uptake of the KDB since its introduction has been limited. Nevertheless, we are of the view that it has a role to play and regardless of Pillar Two, steps should be taken to enhance the regime. With regard to Pillar Two, the attractiveness of the KDB regime will be further eroded as a result of the proposed rules. In particular, there is no specific carve out in the EU Directive on Pillar Two for patent boxes. While patent boxes are not restricted, if there is no carve-out, any income taxed at less than the 15% minimum rate by the country of the patent box could be subject to a GloBE tax liability. This potentially negates any benefit that a group within the Pillar Two rules (broadly, an MNE with €750m plus turnover) would obtain by using the Knowledge Development Box.

Further to that, in order to achieve the 6.25% effective rate, the KDB gives a downward adjustment to taxable profits. In a Pillar Two context, and in particular with regard to the ETR calculations, this reduces the "covered taxes", but the "GloBE income" taken from the financial statements stays the same. As top up tax is paid on the difference between the GloBE 15% rate and the KDB rate of 6.25%, this means the KDB company will receive no KDB relief when considered at a holistic level.

It should be noted that this is arguably at odds with the conclusions reached at para 26 of Action 5 of the BEPS project which states that a preferential tax regime, like the KDB has a role to play in the tax system. We understand that the business community has been lobbying the OECD to exclude patent box income from the requirements to meet a global minimum tax rate and that the OECD have indicated that this will be considered.

However, in the absence of a carve out consideration could be given to amending the Irish KDB regime. In particular, consideration could be given to changing the method of granting the relief from giving a downward adjustment to giving a taxpayer a tax credit ("IP Tax Credit") calculated as a percentage of qualifying profits. Such credit should be drafted consistently with the "*qualified refundable credit*" definition in the draft EU Directive on Pillar Two (see our recommendations related to the R&D Tax Credit amendments). We believe that such approach should make the relief more "Pillar Two neutral". Any changes to the existing regime would require its reassessment under Action 5 and this should be considered in due course. Prima facie, we would be of the view that there are good arguments that changing the KDB regime from a downward adjustment regime to a credit regime should not fall foul of Action 5. Separately, in our view, such an approach would not mean that the nominal rate for the STTR would be considered below the 12.5% rate.

Scope

> 5. Are there any aspects concerning the scope of the Rules, for example the definitions of a Group, a Constituent Entity or an Excluded Entity, that require further clarification in domestic legislation?

As a general comment and as already mentioned above, to the extent possible, the Irish legislation should follow the wording of the Directive and use the same terminology/definitions. Where terms are undefined in the Directive, Irish legislation should to the extent possible define such terms drawing on the OECD commentary and accounting standards. Such an approach has the advantage of familiarity, in particular for foreign investors and should provide groups with a level of certainty as to how the Irish rules will operate.

Article 2.3 and Excluded entities.

Article 2.3. states that "*This Directive shall not apply to the following entities ('excluded entities'):*

a. a governmental entity, an international organisation, a non-profit organisation, a pension fund, an investment fund that is an ultimate parent entity and a real estate investment vehicle that is an ultimate parent entity;

b. an entity where at least 95 % of the value of the entity is owned by one or more entities referred to in point (a), directly or through one or several excluded entities, except pension services entities, and that:

(i) operates exclusively, or almost exclusively, to hold assets or invest funds for the benefit of the entity or entities referred to in point (a); or

(ii) exclusively carries out activities ancillary to those performed by the entity or entities referred to in point (a);

c. *an entity where at least 85 % of the value of the entity is owned, directly or through one or several excluded entities, by one or more entities referred to in point (a), …..*"

It should be made clear in the legislation that the excluded entity referred to in the underlined above is not necessarily an entity described in sub para (a).

The reference to "almost exclusively" in Article 3.3 (b) (i) should be defined.

Real Estate Investment Vehicle

Article 3.26 of the draft Directive states that "*real estate investment vehicle' means a widely held entity that holds predominantly immovable property and that is subject to a single level of taxation, either in its hands or in the hands of its interest holders, with at most one year of deferral".* It should be noted that Irish REIT's may be subject to Irish tax on its residual income and therefore potentially subject to a second layer of tax .i.e., at REIT and shareholder level. This could affect an Irish REIT's ability to rely on the excluded entity definition. Thus, it may be necessary to exempt all of a REIT's income from tax. It should be noted that there are already provisions within the REIT rules, such as the 75% income and asset tests that would limit a taxpayer's ability to abuse the REIT regime by say using the REIT to carry on a property development trade.

In addition, under the Irish REIT regime, the 85% distribution requirement does not apply to reinvested capital gains. Thus, the distribution requirement can be deferred indefinitely. As such, *prima facie*, the one - year maximum deferral of the distribution requirement is not met unless, arguably the one-year deferral requirement applies to income only and not gains. Para 146 of Chapter 10 of the OECD commentary states that "*[o]ne of the conditions set out in the definition is that Real Estate Investment Vehicle achieves a single level of taxation (with at most one year of deferral). <u>The intention of this language is to deal with tax neutral vehicles which are designed to ensure that a single level of taxation is achieved</u> either in the hands of the vehicle or its equity interests holders. <u>This could be the case of an exempt entity provided that it distributes its income within a time period.</u>"* We would recommend that the definition of "real estate investment vehicle" in Irish legislation is defined accordingly. It should be noted that in an international context, similar to Ireland, many REIT regimes only apply the distribution requirement to rental profits (and not gains), for example the UK, the Netherlands, the US, and Belgium.

<u>Meaning of "Annual Revenue" in Article 2 (Scope)</u>

An in-scope group is one where constituent entities located in a Member State of the European Union are members of an MNE or a large-scale domestic group which has an annual revenue of EUR 750,000,000 or more, including the revenue of the excluded entities referred to in para 3, in its ultimate parent entity's consolidated financial statements in at least two of the four fiscal years immediately preceding the tested fiscal year. "Annual Revenue" should be defined. The OECD commentary on page 15 explains that "*The revenue threshold takes into account the consolidated revenue as reported in the Consolidated Financial Statements of the Group. … Where the income of an Entity is consolidated with that of an MNE Group, then the threshold in Article 1.1.1 is applied to the total amount of the Entity's revenue that is reflected in the Consolidated Financial Statements of the Group, even if a portion of the interests in that Group Entity is owned (directly or indirectly) by minority interest holders".* Such clarity should be included in the definition of same so that questions such as whether exceptional items to be included in revenue, or whether revenue is gross, or net of relevant rebates can be avoided.

Charging provisions

> 6. Do you have any views on how (i) the Income Inclusion Rule ('IIR') and (ii) the Undertaxed Profits Rule ('UTPR') provisions[5] should be reflected in domestic legislation?
>
> 7. In relation to the UTPR, should this take the form of either (i) a top-up tax or (ii) a denial of deduction against taxable income resulting in an amount of tax liability necessary to collect Ireland's portion of the UTPR top-up tax amount?

6. Do you have any views on how (i) the Income Inclusion Rule ('IIR') and (ii) the Undertaxed Profits Rule ('UTPR') provisions should be reflected in domestic legislation?

<u>Legislation and steps</u>

As noted earlier, we would recommend that the Pillar Two rules are introduced as a standalone part of TCA97 (.e.g., Part 35E) and include a section to the effect that the GloBE rules are applied after the calculation of domestic corporate/income tax .i.e. a section similar to 835AAO TCA 1997 which states *"this Part shall apply after all provisions of the Tax Acts and the Capital Gains Tax Acts."*

In respect of the IIR, the rules should be set out in the following order: -

- Step 1: Determine if group is within GloBE rules .e.g., has the €750m threshold been breached? (Article 2)
- Step 2:

  (i) Determine the jurisdictions in which the group operates.
  (ii) Determine which jurisdictions are (a) subject to a Qualifying Income Inclusion Rule (QIIR) (other than that operated by Ireland) or (b) are EU jurisdictions which compute a QDTUT under IFRS or the acceptable accounting standard used by the UPE (Article 10.2 (para 2)).

- Step 3: Where the Irish QIIR applies to a jurisdiction or UTPR applies, determine the constituent entities that a group has in the relevant jurisdictions.
- Step 4: Determine: -

  (i) "Financial accounting net income or loss of each constituent entity"
  (ii) The "covered taxes" of each constituent entity

- Step 5: For each constituent entity, adjust "Financial accounting net income or loss of the constituent entity" in order to arrive at "Qualifying Income or Loss" (Article 15).
- Step 6: For each constituent entity, adjust "covered taxes" to determine "adjusted covered taxes" (including adjustments made in respect of deferred tax) (Article 20 & 21).
- Step 7: For each jurisdiction, aggregate the Qualifying Income or Losses and the "adjusted covered taxes" found in Steps 5 and 6 to determine the "Net Qualifying

Income" and the aggregate "adjusted covered taxes. (Note this is an aggregation as opposed to a consolidation).

- Step 8: Exclude jurisdictions to which the de–minimis rules apply (Article 29).
- Step 9: For each jurisdiction, calculate the jurisdictional ETR by dividing the adjusted covered taxes by the Net Qualifying Income (Article 25.1).
- Step 10:
    - If the jurisdictional ETR in Step 9 is 15% or more, then nothing further is required in respect of these jurisdictions.
    - If the jurisdictional ETR in Step 9 is less than 15%, calculate the group's 'top-up percentage' for the jurisdiction. The top up percentage is the minimum tax of 15% less the jurisdictional ETR (Article 26.2).
- Step 11: Calculate excess profit by taking the Qualifying Income and deducting the Substance – based income exclusion (Article 26.4 & 27).
- Step 12: Calculate the jurisdictional top up tax by taking the excess profit calculated in Step 11, multiplying same by the top up tax percentage per Step 10 (Article 26.3).
- Step 13: Subtract any taxes charged under a QDTUT. (Article 26.3) and add any additional top up tax calculated in respect of earlier years (In certain cases it may be necessary to recalculate the top up tax of an earlier period .e.g., where a deferred tax liability is recaptured or where gains on immovable property are spread in accordance with Article 15.7. In such a case, any additional top up tax will be payable in the current period).

The above steps would also require a placeholder for any safe harbour rules which may apply, where such rules are agreed upon and transposed into law.

Commencement

Article 55 states that the IIR and the UTPR shall apply in respect of the fiscal years beginning as from 31 December 2023 and 31 December 2024 respectively. The fiscal year referred to is the fiscal year of the taxpayer. Thus, the Irish domestic rules should only apply to accounting periods commencing after 31 December 2023 for the IIR or after 31 December 2024 for the UTPR. In particular, the rules should not apply on a split year basis.

7. In relation to the UTPR, should this take the form of either (i) a top-up tax or (ii) a denial of deduction against taxable income resulting in an amount of tax liability necessary to collect Ireland's portion of the UTPR top-up tax amount?

The mechanism for collecting any top up tax under the UTPR appears to be left open to jurisdictions as to whether to do this by disallowing expenses for GloBE purposes or simply imposing an additional tax. In our view, a taxpayer should be allowed elect between a (i) a top-up tax or (ii) a denial of deduction against taxable income.

Computation of GloBE Income or Loss

8. Do you have any comments on the Computation of GloBE Income or Loss provisions contained within the Rules[6] and how these could be implemented in domestic legislation? In particular, do you have any comments on:
    (i) the determination of the Financial Accounting Net Income or Loss, and
    (ii) the adjustments to determine the GloBE Income or Loss?

9. Are there any aspects of the Computation of GloBE Income or Loss provisions that require further clarification in domestic legislation?

10. Do you have any views on the rules regarding the allocation of Income or Loss to entities/jurisdictions as they could apply to domestic legislation?

8. Do you have any comments on the Computation of GloBE Income or Loss provisions contained within the Rules and how these could be implemented in domestic legislation? In particular, do you have any comments on:
(i) the determination of the Financial Accounting Net Income or Loss, and
(ii) the adjustments to determine the GloBE Income or Loss?

<u>Financial Accounting Net Income or Loss</u>

"Financial accounting net income or loss" is used throughout the Directive but the term is not defined. We understand the term refers to accounting profits after tax. However, there is uncertainty as to what accounting profits it refers to. Some commentators have suggested that "Financial accounting net income or loss" refers to the after-tax accounting profits/loss as calculated for inclusion in the groups consolidated accounts. This may not be an ideal approach as group accounting numbers are typically prepared using a high level of materiality and thus subject to change.

Typically, consolidated financial statements are prepared in a short timeframe post the financial year-end. While the consolidated accounts are audited, group level materiality has to be taken into consideration. Following group reporting, a group will generally prepare statutory financial statements for each entity which may be based on a different materiality standard (in most cases a lower materiality threshold). Another issue with using group reporting numbers is that for materiality reasons, smaller entities may not be consolidated as part of the group accounts.

Further to above, if the entity figures used for consolidation purposes are used for GloBE purpose, there is a likelihood that adjustments would be required in the following year. Adjustments for changes under the GloBE rules is not however a straightforward process and may in certain cases result in additional tax costs for a taxpayer.

Further to that, an increase to a constituent entity's covered taxes for a prior year is treated as an increase in covered taxes in the current year (i.e., in the fiscal year in which the adjustment is made) (Article 24.1). If the taxpayer was allowed to adjust the prior year, then such adjustment could increase the ETR in that year thereby in certain cases reducing the top up tax associated with prior years (resulting in a refund of tax).

In contrast, a material (defined as an aggregate decrease of less than EUR 1 million in the adjusted covered taxes for the jurisdiction for a fiscal year) decrease in covered taxes for a prior year requires the MNE to adjust both the taxes and the GloBE Income for the prior year. The ETR and top-up tax for the prior year must then be re-determined based on the revised Covered Taxes and GloBE Income in order to determine if there is any additional top-up tax for the jurisdiction.

As such, groups would likely prefer to avoid having to regularly amend earlier periods. This is not only because of the additional administration burden of having to recalculate earlier periods but also the risk that such post filing adjustments may result in a higher top up tax being paid, than would have been the case if a top up tax return had been prepared with the results of the statutory financial statements.

Article 14.1 states that "*The qualifying income or loss of a constituent entity shall be computed by making the adjustments set out in Articles 15 to 18 to the financial accounting net income or loss of the constituent entity for the fiscal year before any consolidation adjustments for eliminating intra-group transactions, as determined under the accounting standard used in the preparation of the consolidated financial statements of the ultimate parent entity".* In our view, this does not necessarily require a group to use for GloBE purposes, the entity results included in the consolidated accounts. The key requirement is that such results are "*determined under the accounting standard used in the preparation of the consolidated financial statements of the ultimate parent entity*" Some might argue that the reference to *"before any consolidation adjustments for eliminating intra-group transactions"* requires the use of the numbers as they stand pre–consolidation. However, "before" could also be interpreted as meaning without elimination of intra group transactions.

We would recommend that taxpayers have the option of using the numbers in the final statutory accounts as adjusted to the group accounting standard for the purposes of the GloBE return. This approach would also align the GloBE tax basis with the starting point for corporate tax returns and provide greater certainty for both the Revenue and the taxpayer.

<u>Adjustments to determine GloBE income</u>

Article 15.4. para 1 states that "*Any transaction between constituent entities located <u>in different jurisdictions</u> that is not recorded in the same amount in the financial accounts of both constituent entities or that is not consistent with the arm's length principle must be adjusted so as to be in the same amount and consistent with the arm's length principle* [emphasis added]*."* Provisions should be included to the effect that if the arm's length adjustment is subsequently reflected in the "financial accounting net income or loss" in a later period, then such adjustment can be ignored and does not need to be adjusted for under the post filing adjustments in Article 24. For example, say a group when preparing its GLoBE return notices that a transaction in the financial statements (now closed) was not at arm's length. In that case, the group will adjust the qualifying income or loss for FY1 to reflect the arm's length amount. The financial statements in FY2 may also reflect the same arm's length adjustment (.i.e., such adjustment may not necessarily be adjusted through opening reserves) which could be reflected in FY2's qualifying income or loss. Accordingly, provision should be included to adjust the FY2 arms - length adjustment.

Article 15.4. para 2 deals with certain domestic to domestic transactions and reads *"[a] loss from a sale or other transfer of an asset between two constituent entities located <u>in</u>*

the same jurisdiction that is not recorded consistently with the arm's length principle shall be adjusted based on the arm's length principle if that loss is included in the computation of the qualifying income or loss. [emphasis added]". It can be seen that this provision is only invoked where a loss arises in the disponer constituent entity; given that the loss must be included in the computation of the qualifying income or loss then presumably this means an accounting loss based on the carrying value of the respective asset. Ireland currently has an exception from the application of transfer pricing rules for certain domestic to domestic transactions, but this would be obviated for GloBE rules. The matter will arguably be of little consequence if the asset concerned is accounted for as an expense in the acquirer's profit and loss account given that the two results of the two entities will be aggregated in computing the jurisdiction's qualifying income. However, the adjustment will be necessary where the acquirer capitalises the asset and depreciates it over time its profit and loss account. The abovementioned Article 15.4. para 2 applies only to the loss being recorded consistently with the arm's length provisions and is silent on the deferred tax implications of same. Clarity would be welcome regarding whether the accounting deferred tax included in covered taxes is to be adjusted or otherwise.

In cases where a foreign audit results in a revision to the figures contained in the financial accounts on which GloBE income or loss has previously been based, clarity would be welcome as to how taxpayers are expected to proceed.

9. Are there any aspects of the Computation of GloBE Income or Loss provisions that require further clarification in domestic legislation?

See our responses to Question 8.

10. Do you have any views on the rules regarding the allocation of Income or Loss to entities/jurisdictions as they could apply to domestic legislation?

We have no comments in this regard.

Computation of Adjusted Covered Taxes

11. Do you have any comments on the Computation of Adjusted Covered Taxes provisions[7] and how these could be implemented in domestic legislation?

12. Are there any aspects of the Computation of Adjusted Covered Taxes provisions that require further clarification in domestic legislation?

13. Do you have any views on the rules on (i) the allocation of covered taxed between entities, (ii) the mechanism to address temporary differences, and (iii) post-filing adjustments as they could apply to domestic legislation?

11. Do you have any comments on the Computation of Adjusted Covered Taxes provisions and how these could be implemented in domestic legislation?

We have no comments in this regard.

12. Are there any aspects of the Computation of Adjusted Covered Taxes provisions that require further clarification in domestic legislation?

Similar to our points in respect of "financial accounting net income or loss", clarification is needed in respect of whether it is the deferred tax used for group reporting purposes or deferred tax used for statutory accounts that should be used.

Article 19.1 – Definition of covered taxes

Article 19.1. states *"[t]he covered taxes of a constituent entity shall include: (a) taxes recorded in the financial accounts of a constituent entity with respect to its income or profits, … ."* We understand this definition includes cash tax charged on the profits of the company, tax on dividends from an investee company imposed by the country of the investee company (e.g., withholding tax operated by the country of an investee company) and accruals in respect of uncertain tax positions (albeit reduced by Article 20(3)(d)). This should be clarified in the Irish domestic definition.

Article 19.1. states "*[t]he covered taxes of a constituent entity shall include…(c) taxes imposed in lieu of a generally applicable corporate income tax."* The OECD commentary to the GloBE rules explains at para 31 to Ch4 "*this includes taxes that are not described in the generally applicable income tax definition but which operate as substitutes for such taxes. This test, … would generally include withholding taxes on interest, rents and royalties, and other taxes on other categories of gross payments such as insurance premiums, provided such taxes are imposed in substitution for a generally applicable income tax. Taxes imposed in lieu of a generally applicable CIT would also include taxes arising from the Subject to tax Rule*" This should be made clear in Irish domestic legislation.

In construing article 19 of the Directive, it would appear that Covered Taxes does not include deferred tax by virtue of the implication arising from articles 20 and 21. This is not explicit in the Directive. We would suggest that the Irish domestic definition of "Covered Taxes" should explicitly state that it does not include deferred taxes.

Article 20 - Adjusted covered taxes

"Uncertain tax positions" should be defined, possibly in line with the definitions used in accounting standards.

Article 21

There is no definition of "total deferred tax adjustment amount". This should be defined in Irish domestic law. Prima facie, in the first instance the "total deferred tax adjustment amount" is the net deferred tax movement in the tax line in the Income Statement. It should also be noted that the Directive uses the term "total deferred tax adjustment amount" to refer to amounts pre and post the adjustments in Article 21.3 to 21.5. The amounts pre and post the adjustments in Article 21.3 to 21.5 should be distinguished for the purposes of clarity in Irish domestic legislation.

Article 21.2 states that *"[w]here the tax rate applied for purposes of computing the <u>deferred tax expense</u> is above the minimum tax rate, the total deferred tax adjustment amount to be added to the adjusted covered taxes of a constituent entity for a fiscal year pursuant to point (b) of Article 20(1) shall be the deferred tax expense accrued in its financial accounts with respect to covered taxes recast at the minimum tax rate, subject to the adjustments under paragraphs 3 to 6."* It is not clear whether "deferred tax expense" refers to a net deferred tax movement that is an expense only or whether it can extend to a net deferred tax movement that is a credit also. The OECD commentary on the matter states: -

> ***"Article 4.4.1***
> *70. The starting point for the Total Deferred Tax Adjustment Amount is the amount of deferred tax expense accrued in the financial accounts of a Constituent Entity if the applicable tax rate is below the Minimum Rate or, in any other case, such deferred tax expense recast at the Minimum Rate. Deferred tax expense for the Fiscal Year is comprised of the net movement in deferred tax assets and liabilities between the beginning and end of the Fiscal Year. When established, deferred tax assets are recorded as negative tax expense (i.e., income tax benefit) whereas deferred tax liabilities are recorded as tax expense. Note that the recast of deferred tax expense may either be performed on an item-by-item basis or in the aggregate for all items recorded at the same rate, as the result should remain unchanged. When a deferred tax asset or deferred tax liability reverses it will reverse at the same amount and rate at which it has been recorded. A reversal of a deferred tax liability is negative deferred tax expense, whereas the reversal of a deferred tax asset equates to deferred tax expense. The applicable tax rate is the tax rate at which the deferred tax item is recorded. For example, if a deferred tax liability of 20 is recorded with respect to income of 100, the applicable tax rate is 20% (i.e., the tax imposed on an item of income divided by that item of income). This rate is higher than the Minimum Rate and would thus be recast at the Minimum Rate. For example, if the CIT rate in Country Z in the example in the introduction to the Article 4.4 Commentary was 30%, then the rules in Article 4.4.1 would still only recognise a deferred tax liability of 12 (i.e., 80 of additional income multiplied by the 15% Minimum Rate) in the first Fiscal Year. When such deferred tax liability reverses, the amount of the reversal will be 12.*
> *71. To the extent deferred tax assets exceed deferred tax liabilities, deferred tax expense will be negative (i.e., an asset in lieu of a liability). This amount is typically accrued with respect to the applicable domestic tax rate (i.e., the tax rate in a jurisdiction which applies to the item of income with respect to which the deferred tax item is recorded) in a jurisdiction in order to adjust for timing differences between financial accounting recognition and domestic tax recognition. In order to use the accounts to adjust for timing differences under the GloBE Rules, the deferred tax assets and liabilities must be recast with reference to the Minimum Rate to the extent they have been recorded at a rate in excess of the Minimum Rate"*

While not entirely clear, it would seem that where the applicable rate is in excess of the minimum rate, the aggregate deferred tax movement, whether such movement is positive or negative in the income statement should be recast at the minimum rate. If that is the case, for Irish domestic tax, we would suggest that using terminology such as "aggregate deferred tax movement" instead of "deferred tax expense" may be a more appropriate description.

13. Do you have any views on the rules on (i) the allocation of covered taxed between entities, (ii) the mechanism to address temporary differences, and (iii) post-filing adjustments as they could apply to domestic legislation?

<u>Allocation of covered taxed between entities</u>

We have no comments in this regard.

<u>The mechanism to address temporary differences</u>

Article 21 (7) states that "*[a] deferred tax liability that is not reversed and whose amount is not paid within the five subsequent fiscal years shall be recaptured to the extent it was taken into account in the total deferred tax adjustment amount of a constituent entity"* Article 21.7 also states that *"the amount of the recaptured deferred tax liability determined for the current fiscal year shall be treated as a reduction to the covered taxes in the fifth preceding the current fiscal year and the effective tax rate and top-up tax of such fiscal year shall be recomputed*". Basically, if a deferred tax liability has not been reversed and paid by the end of Year 6, then Year 1 must be recalculated excluding the deferred tax liability (the Recapture Rule).

An example of what the Recapture Rule targets is a remittance basis regime. Under a remittance regime, the taxpayer would not be taxed on accrued income. Instead, the taxpayer would only be taxed when it actually received the cash in respect of the income. Giving the timing difference, a tax expense in respect of a deferred tax liability would be recognised in the Income Statement. For example, say in Year 1 there was accrued income of 100. At the end of Year 1, no monies had been received by the taxpayer. The tax rate in the taxpayer's country is 30%. In such a case, no cash tax is paid in respect of Year 1. However, a deferred tax liability is recognised of 30 (100 @ 30%). The deferred tax liability would result in an ETR of 30% .i.e., 30/100. Without the recapture rule, it would be possible to frustrate the GloBE rules as the 15% ETR would be met even through no actual cash tax had been paid to the tax authorities. Further to that, if the deferred tax liability recognised in Year 1 is not reversed by the end of Year 6 and is not paid by the end of Year 6, then the Year 1 ETR is recalculated excluding the deferred tax liability expense. On recalculation, the ETR for GloBE purposes would be 0%.

A critical point to note is that the test is an "and" test .i.e., "a deferred tax liability that is not reversed <u>and</u> whose amount is not paid within the five subsequent fiscal years shall be recaptured." If for example, the deferred tax liability was for some reason reversed in Year 2, on a strict technical reading, this in itself would not be sufficient to avoid the recapture rule at the end of Year 6, if the tax of 30 had not been paid at some point during Years 2 – 6. This could result in taxation in excess of commercial profits. Further consideration should be given to this.

S.291A TCA 1997 provides capital allowances for expenditure on certain intangible assets. Generally, under S.291A the timing of the deduction for such capital allowances follows the accounting treatment .i.e., broadly, an allowance is allowed for the amount of amortisation charged to the income statement in the accounting period. In such a case, no deferred tax would normally arise. However, under S.291A (4) TCA 1997, a company may elect to have the allowances spread over 15 years. A company would typically make this election if for accounting purposes an intangible asset is not amortised or is amortised over a period in excess of 15 years.

Where a company makes such an election, then a deferred tax liability may be recognised in Year 1 with the deferred tax liability increasing in each of the Years 2 – 15 .i.e., as in each of the years 1 – 15, the Net Book Value for accounting purposes would be in excess of the Tax Written Down Value. In the case of an intangible asset that is been amortised over a period in excess of 15 years, the deferred tax liability will be reversed over the remaining useful life of the intangible asset .e.g., an intangible asset that is being amortised over 20 years for accounting purposes, then the deferred tax liability will be reversed in years 16 – 20. For an intangible asset that is not amortised, the deferred tax liability will not reverse until sale. For the purposes of Pillar Two, prima facie, for each year beginning in Year 6 and in some cases right out to Year 25, it will be necessary to recapture the deferred tax expense and recompute the ETR for the tax year that is five years earlier .i.e., broadly, the ETR of the earlier period is recalculated ignoring the deferred tax expense.

Consideration should be given to whether the Recapture Rules are meant to apply to a S.291A TCA 1997 situation as discussed above. As mentioned, Article 21 (7) states that "[a] deferred tax liability that is not reversed and whose amount is not paid within the five subsequent fiscal years shall be recaptured…" Thus, for the Recapture Rule not to apply, the deferred tax liability must be paid within 5 years following the tax year in which the deferred tax expense was charged to the income statement (regardless of whether such amount has been reversed or not). This is arguably a condition that can never be met in the context of S.291A TCA 1997 as such a deferred tax liability could never be "paid". That is, a company may recognise a deferred tax liability where the net book value exceeds the tax written down value. However, such deferred tax liability would never represent a tax liability. Such deferred tax liability merely represents the fact that the tax life of the intangible asset is shorter than the accounting life of the intangible asset. This may indicate that Article 21.7 is not intended to target the S.291A TCA 1997 situations described above. Instead, Article 21.7 is more likely intended to target remittance type regimes as discussed earlier.

Further support may be found for this position in the OECD Pillar Two commentary discussing "cost recovery allowances on tangible assets". By way of background, the recapture rule in Article 21.8 does not apply to certain expenses such as "cost recovery allowances on tangible assets" .e.g., capital allowances on tangible assets. While this exception does not apply to the capital allowances on intangible assets provided by S.291A TCA 1997, some of the reasons given for excepting tangible assets from the Recapture Rule are equally relevant to the S.291A TCA 1997 situation described above. In that regard, Article 4.4 & 4.4.5 of the March 2022 OECD Commentary on Pillar Two states: - [emphasis added by Deloitte]

"68. While Article 4.4 uses existing deferred tax accounts maintained by MNE Groups to the greatest extent possible to simplify compliance, certain adjustments are required to protect the integrity of the GloBE Rules. These adjustments include using the lower of the Minimum Rate or the applicable tax rate to calculate deferred tax assets and liabilities in order to prevent deferred tax amounts from sheltering unrelated GloBE Income. The rules also require the recapture of certain amounts claimed as deferred tax liabilities that are not paid within five years. Exceptions are provided for the most common and material book to tax differences when they relate to substance in a jurisdiction or are not prone to taxpayer manipulation. These amounts do not require monitoring for recapture.

91. The Recapture Exception Accrual rule, which provides categories of deferred tax liabilities that do not need to be monitored for recapture under Article 4.4.4, is set forth in Article 4.4.5. The list of Recapture Exception Accruals sets out the temporary differences that are both common in Inclusive Framework jurisdictions and that are generally material to MNE Groups. Such temporary differences are typically tied to substantive activities in a jurisdiction or are differences that are not prone to taxpayer manipulation. Accordingly, to reduce compliance burdens, these low-risk items that are certain to reverse over time are not required to be monitored under the rules in Article 4.4.4 for recapture.

Paragraph (a)

92. The inclusion of cost recovery allowances in paragraph (a) of Article 4.4.5 with respect to tangible assets reflects the principle that accelerated depreciation and immediate expensing regimes are common in Inclusive Framework jurisdictions and that such timing differences are certain to reverse over the life of an asset. Absent the rule in paragraph (a) of Article 4.4.5, the recapture mechanism in Article 4.4.4 could serve to disgorge the benefit of such regimes and result in the distortion of jurisdictional ETRs for assets that have a lifespan longer than the time period set forth in Article 4.4.4"

Also, there has been some concern that the recapture rule could serve to recapture deferred tax liabilities created prior to the transition date. Article 21.7 states "*A deferred tax liability that is not reversed and whose amount is not paid within the five subsequent fiscal years shall be recaptured to the extent it was taken into account in the total deferred tax adjustment amount of a constituent entity".* In our view, a deferred tax liability recognised before the transition date would not have been taken into account in a "total deferred tax adjustment amount" .i.e. an expense posted to the income statement before the transition date is a deferred tax expense but it is not a "deferred tax adjustment amount". A "deferred tax adjustment amount" is a GLoBE term and as GLoBE was not applicable prior to the transition date the deferred tax expense is not a "deferred tax adjustment amount". Thus, the recapture rules should not apply to deferred tax liabilities recognised before the transition date.

Post-filing adjustments as they could apply to domestic legislation?

Post filing adjustments – See earlier comments in Q8.

Qualified Refundable Tax Credits

> 14. Do you have any comments on the potential interaction of tax credit provisions, as currently set out in the corporation tax code, with the definition of "Qualified Refundable Tax Credit"[8]?

Article 3 of the Directive states "(32)(a) 'qualified refundable tax credit' means:

> *"(a) a refundable tax credit designed in such a way that it must be paid as a cash payment or a cash equivalent to a constituent entity within four years from the date when the constituent entity is entitled to receive the refundable tax credit under the laws of the jurisdiction granting the credit; or*
>
> *(b) if the tax credit is refundable in part, the portion of the refundable tax credit that is payable as a cash payment or a cash equivalent to a constituent entity within four years from the date when the constituent entity is entitled to receive the partial refundable tax credit"*

It is questionable whether the current R&D credit would fall to be regarded as a "qualified refundable tax credit" ("QRTC"). As currently written S.766 (2) TCA 1997 provides that the claimant's corporation tax liability must in the first instance be reduced by the amount of the R&D credit. Then, broadly, S.766 (4A) and (4B) TCA 1997 allow for a refund of any excess of the credit over the claimant's corporation tax liability within 3 years. However, S.766B TCA 1997 puts a limit on such refund by reference to certain corporate and payroll liabilities. As such, in certain circumstances it may be the case that not all of the R&D credit is refundable within 4 years. Thus, any amount in excess of this limit may not be a qualifying refundable tax credit.

Recitals 19a of the draft Directive allows Member States implementing the Directive to have regard to the OECD Pillar Two documentation. In that regard, para 135 of the OECD commentary makes the points: -

> *"… Refundable means that the amount of the credit that has not been applied already to reduce Covered Taxes is either payable as cash or cash equivalent. For this purpose, cash equivalent includes checks, short-term government debt instruments… as well as the ability to use the credit to discharge liabilities other than a Covered Tax liability. If the credit is only available to reduce Covered Taxes, i.e., it cannot be refunded in cash or credited against another tax, it is not refundable for this purpose. If the tax credit regime provides for an election by the taxpayer to receive the credit in a manner that is refundable, the tax credit regime is considered refundable to the extent of the refundable portion, regardless of whether any particular taxpayer elects refundability."*

As a result, we would suggest that the Irish domestic law be amended to ensure it can be refundable in total without any limits within 4 years. This could involve allowing the taxpayer to set the R&D credits against other non-covered taxes of the taxpayer concerned at the discretion of the taxpayer and for refunds to be payable with no restriction or cap imposed by reference to corporate and payroll liabilities.

Further, para 136 notes that "*[t]he assessment of whether a credit is refundable in the sense contemplated by the GloBE Rules must be made based on the conditions under which the credit is granted and on the information that was available at the time the credit was introduced into domestic law*." It is unclear as to whether that requires looking back to the R&D credit status as at 2004.

As a separate point, while the digital games credit relief provided for in Finance Act 2021 has not yet been made effective in law we would nevertheless be of the view that such a credit should also be reviewed to ensure that it will be treated as a "Qualified Refundable Tax Credit" for the purposes of Pillar Two.

Computation of ETR and Top – up Tax

> 15. Do you have any views on the Computation of Effective Tax Rate (ETR) and Top-up Tax provisions[9]? In particular, do you have any views on the process to calculate ETR and Top-up Tax and how these could be implemented in domestic legislation?
>
> 16. Are there any aspects of the calculation of the ETR and Top-up Tax of investment entities, joint ventures or minority-owned constituent entities that require further clarification in domestic legislation?

15. Do you have any views on the Computation of Effective Tax Rate (ETR) and Top-up Tax provisions? In particular, do you have any views on the process to calculate ETR and Top-up Tax and how these could be implemented in domestic legislation?

See our responses to Question 6.

Based on Articles 25, 26.2 - 26.4 & 27, it would seem that the top up tax is to be computed on a jurisdictional basis and not on an entity-by-entity basis. The second sentence in Article 26.1 also states that the *"[t]he top-up tax shall be computed on a jurisdictional basis"*. Article 26.5 then apportions the jurisdictional top up tax between the different constituent entities in the jurisdiction based on each constituent entity's share of "qualifying income".

However, the first sentence of Article 26.1 states that *"… the MNE group or a large-scale domestic group shall compute the top-up tax separately for each of its constituent entities that has qualifying income included in the computation of net qualifying income of that jurisdiction."* This would seem to indicate that the top up tax is to be calculated on an entity-by-entity basis. As such, this would seem to contradict Articles 25, 26.2 - 26.4 & 27 and the second sentence in Article 26.1.

In our view, the jurisdictional basis is the correct basis. As such, we would recommend that in order to avoid interpretative difficulties, similar language as used in the first sentence of Article 26.1 is not used in Irish legislation.

16. Are there any aspects of the calculation of the ETR and Top-up Tax of investment entities, joint ventures or minority-owned constituent entities that require further clarification in domestic legislation?

We have no comments in this regard.

Qualified Domestic Top-up Tax ("QDTUT")

> 17. In your view, should a QDTUT be implemented by Ireland? If so, what should be the features of such a QDTUT and how should it operate? In particular, please provide your view on the charging and administrative rules that should apply.
>
> For example, could a QDTUT form part of the corporation tax liability of a company and be returned as part of the corporation tax return? How should the jurisdictional calculation of the QDTUT be addressed in return filings, particularly where entities in an MNE group in scope in Ireland might have different intermediate parents?

<u>Should it be implemented?</u>

There would be two policy rationales for the introduction of an Irish QDTUT (i) Revenue protection and (ii) Simplification.

The first reflects the fact that absent a domestic minimum tax, the GloBE rules will mean that Irish profits will be subject to a top up tax in foreign jurisdictions (even though the activities generating the profits are carried on in Ireland). A QDTUT therefore secures additional tax revenue for the Irish exchequer without increasing the overall tax burden of the group. We would recommend that consideration is given to using any additional top up taxes collected to support reductions in personal taxation and the enhancement of reliefs such as R&D credits and KDB.

On the second point, a QDTUT could reduce the compliance and administrative burdens on MNEs generally given that "top up tax" would be calculated by the jurisdiction at issue. However, an EU parent would still need to compute the top up tax in its home country if the Irish company did not compute its QDTUT under IFRS or the acceptable accounting standard used by the UPE (Article 10.2).

Article 10(4) requires Member States who elect to apply a QDTUT to notify the Commission within four months following the adoption of national laws to provide for such a tax. Para (13) of the preamble to the Directive states "… Member States should notify to the European Commission when they elect to apply a qualified domestic top-up tax, with the objective of providing tax authorities of other Member States and third country jurisdictions as well as MNE groups with sufficient certainty as regards the applicability of the qualified domestic top-up tax to low-taxed constituent entities in that Member State". Where feasible, we would welcome early notice from the Department of Finance as to whether the QDTUT is to be transposed into Irish law. An early clear statement as to Government policy on this point would be welcomed by the business community and assist in scope groups in assessing and modelling the impact of Pillar Two in advance of its enactment.

<u>Potential features of the QDTUT</u>

The calculation of the QDTUT should operate in the same manner as the calculation of the Qualified IIR for a particular jurisdiction. Recital (13) to the Directive states:

“Constituent entities of an MNE group that are located in a Member State which has elected to implement such a system in its own domestic tax system should pay the top-up tax to this Member State. Such system should ensure that the minimum effective taxation of the qualifying income or loss of the constituent entities is computed in the same way, as the calculation of the top-up tax in accordance with this Directive.”

Under the qualified domestic top-up tax rules in Article 10, the domestic excess profits of the low-taxed constituent entities may be computed based on an acceptable financial accounting standard or an authorised financial accounting standard permitted by the authorised accounting body and adjusted to prevent any material competitive distortions, rather than the financial accounting standard used in the consolidated financial statements. While an “acceptable financial accounting standard” is defined in Article 3(22) of the Directive, neither “authorised financial accounting standard” nor “authorised accounting body” is defined for the purposes of Article 10. An “authorised accounting body” is defined for the purposes of Article 14, but the Directive is silent as to whether the definition contained therein may be used elsewhere and in particular in applying Article 10 (the QDTUT).

<u>Charging & administration</u>

Article 10.1 of the Directive states that *“if a Member State where constituent entities of an MNE group or a large-scale domestic group are located elects to apply a qualified domestic top-up tax, <u>all low-taxed constituent entities of the MNE group or a large-scale domestic group in that Member State shall be subject to that domestic top-up tax</u> for the fiscal year.”* This would seem to indicate that each entity is separately subject to QDTUT and therefore presumably would be liable for its own QDTUT.

Equally, in line with our later comments on Questions 18 and 19, we would advise against the introduction of preliminary tax payment obligations with respect to the QDTUT.

<u>Part of corporate tax return?</u>

We would not recommend that the QDTUT forms parts of the corporation tax liability of a company and be returned as part of a corporation tax return. In addition, a corporation tax return is due within 8 months and 23 days of the period end. The deadline for filing a top up tax return is 15 months (18 months in the transition year). We would recommend that QDTUT have a user-friendly form of return to be completed by the constituent entity in question.

Article 10.2

From the perspective of an MNE group with an Irish parent, Article 10(2) of the Directive provides that where a parent entity is located in a Member State and its directly or indirectly held low taxed constituent entities located in another Member State or in a third country jurisdiction are subject to a QDTUT, the amount of any top up tax to be levied on the parent is to be reduced by the amount of the QDTUT due by the constituent entities. Therefore, from the perspective of an Irish parent entity (whether the UPE or the intermediate parent), the computation of any top up tax under the IIR is likely to involve a consideration of the quantum of relief or reduction to be given for the QDTUT where this option is adopted by the Member States in which the subsidiaries are located or resident.

Article 26.2 para 1 states:

"Where a parent entity [either a UPE or an IPE] of an MNE group or a large-scale domestic group is located in a Member State, and its directly or indirectly held constituent entities located, either in this Member State or in another jurisdiction, are subject to a qualified domestic top-up tax for the fiscal year in those jurisdictions, the amount of any top-up tax computed in accordance with Article 26 due by the [Irish] parent entity pursuant to Articles 5 to 7 shall be reduced, up to zero, by the amount of qualified domestic top-up tax due either by itself or by those constituent entities."

Basically, where an Irish parent entity (either a UPE or an IPE) operates a IIR, then such parent entity must calculate the top up tax for each jurisdiction and then credit against such top up tax any QDTUT paid either by itself or at lower levels. However, under Article 26.2 para 2, there is no need for the parent to calculate the top up tax for jurisdictions that compute their QDTUT using IFRS or the acceptable accounting standard of the Irish parent. Thus, where jurisdictions compute their QDTUT using accounting standard other than IFRS or the Irish parent's acceptable accounting standard, then the Irish parent will need to compute the top up tax and then provide credit for same. The top up tax payable by the parent could be in excess of the QDTUT credit and the parent will therefore have a liability. Where however the QDTUT exceeds the top up tax calculated by the parent, then there does not seem to be a mechanism to claim a refund. Consideration should be given as to whether Article 26.2 is wide enough to allow the parent to carry forward the overpayment and credit such payment against a top up tax liability of a later year.

Article 10.1

Article 10.1 states*:*

"Under a qualified domestic top-up tax, the domestic excess profits of the low-taxed constituent entities may be computed based on an acceptable financial accounting standard or an authorised financial accounting standard permitted by the authorised accounting body and adjusted to prevent any material competitive distortions, rather than the financial accounting standard used in the consolidated financial statements."

It could be read as not binding on a Member State .i.e. a Member State could choose whether to legislate for Article 10.1 in its domestic legislation. In our view, the option in Article 10.1 to apply acceptable or authorised accounting standards instead of the group accounting standard is an option of the taxpayers and the Irish legislation must provide for such an option.

This is important in that under US GAAP certain intra group transfers of IP are booked at cost at the entity level. This may result in reduced amortisation and therefore increased accounting profits being recorded. Applying the QDTUT to an entity preparing its accounts under US GAAP may result in a higher amount of top up tax than would be payable under IFRS. If a group decided to use US GAAP for the purposes of its QDTUT calculation, subject to the transition rules in Article 45.4, then the provisions of Article 15.4 should be utilised to the effect that the Irish entity applies amortisation to the asset's arm's length price.

18. Do you have any views on how the reporting obligations of entities that are in scope of the Rules, should be satisfied?

19. How should liabilities arising under the IIR or UTPR be reported and paid/collected? Do you have any views on the frequency of such payments and the deadlines that should apply?

18. Do you have any views on how the reporting obligations of entities that are in scope of the Rules, should be satisfied?

Recital (18) of the OECD Commentary states "… *The primary responsibility of filing the information return should lie on the constituent entity itself.* [Article 42.2] *A waiver of such responsibility should however apply where the MNE group has designated another entity to file and share the information return.* [Article 42.2 & 42.3] *It could be either a local entity or an entity from another jurisdiction that has a competent authority agreement in place with the Member State of the constituent entity"* [Article 42.2 & 42.3].

It would be expected that in most cases, groups will be able to avail of the derogation in Article 42.3. As such, the group will file one single GloBE return (subject to Article 42.6 discussed below) in the jurisdiction of its Ultimate Parent Entity. This jurisdiction will then exchange the GloBE return with other tax administrations. The obligation to file in other jurisdictions will then be treated as discharged when those jurisdictions have received the return through the exchange mechanism. This is intended to reduce the compliance burdens on businesses by reducing the number of returns it is required to submit.

The derogation in Article 42.3 may apply even if the jurisdiction of the UPE does not operate a Qualified IIR. Broadly, a Qualified IIR' means a set of rules that is equivalent to the rules laid down in this Directive or, as regards third country jurisdictions, the OECD Model Rules. The key requirement for the purposes of the derogation in Article 42.3 is that there is a qualifying competent authority agreement with the country where the top up return is filed. A ‘qualifying competent authority agreement’ means a bilateral or multilateral agreement or arrangement between two or more competent authorities that provides for the automatic exchange of annual top-up tax information returns. (Article 42.1(b)) However, where a constituent entity is located in a Member State with an ultimate parent entity located in a third country jurisdiction that applies equivalent IIR rules, the constituent entity or the designated local entity shall nonetheless file a top-up tax information return containing certain information in respect of (i) a Partially Owned Parent Entity (ii) all details that are necessary for the application of the UTPR or (iii) all information that is necessary for the application of a qualified domestic top- up tax by any Member State. (Article 42.6) Article 51.1 provides that “The legal framework implemented in the domestic law of a third country jurisdiction shall be considered as equivalent to a qualified IIR … if it fulfils certain conditions .i.e., broadly it imposes a 15% minimum top up tax on a jurisdiction-by-jurisdiction basis. For the avoidance of any doubt, it should be noted that while a regime equivalent to Qualified IIR is akin to a Qualified IIR, it is still not a Qualified IIR.

Article 54 then provides that “*[t]he Union may conclude agreements with third country jurisdictions whose legal frameworks have been assessed as equivalent to a qualified IIR in accordance with Article 51 with a view to arrange a framework for simplifying the reporting procedures laid down in Article 42(6).”* A consideration which arises in particular in the context of Irish subsidiaries of US groups (assuming GILTI is treated as IIR compliant) is the possibility of double filings for such entities.

For the avoidance of doubt, where a constituent entity is located in a Member State (“MS Sub”) with an ultimate parent entity located in another Member State (“MS Top”), the constituent entity in MS Sub will not need to file a top up tax return in MS Sub even if MS Sub operates a Qualified Domestic Top up tax.

Where constituent entities are unable to take advantage of the single filing entity model in Article 42.3, such constituent entity or a designated local entity will need to file a top up tax return. (Article 42.2) In these circumstances, the group may have to file multiple top up returns in multiple jurisdictions.

Deadline for return

Article 48 states that *“[n]otwithstanding Article 42(7), the top-up tax information return, and the notifications referred to in Article 42 shall be filed with the tax administration of the Member States no later than 18 months after the last day of the reporting fiscal year that is the transition year referred to in Article 45*”. In that regard, recital 18 to the Directive states *“… Considering the compliance adjustments that this system requires, groups that fall within the scope of this Directive for the first time should be granted a period of 18 months to comply with the information requirements.”* Thus, in can be seen from the preamble that the 18 month period for submitting a top up tax information return is a requirement and it is not open to a Member State to mandate a shorting period for filing.

Article 42.7 states that "*<u>[t]he top-up tax information return</u> referred to in paragraphs 5 and 6 <u>and</u> any relevant <u>notifications shall be filed with the tax administration of the Member State</u> in which the constituent entity is located <u>no later than 15 months after the last day of the reporting fiscal year"</u>.* It can be seen that the language used in Article 42.7 and Article 48 is very similar. Thus, in our view, the 15-month period for submitting a top up tax information return is also a requirement and it is not open to a Member State to mandate a shorting period for filing.

In any event, regardless of interpretation, due to the complexities involved, we would be of the view that the deadline should not be set earlier than 18/15 months after the last day of the reporting fiscal year.

Any elections under the GloBE rules should form part of the GloBE Information Return .i.e., there should not be separate procedures for making elections.

We would recommend that to the extent that where there is overlap between the information provided under CBCR and the information required by Article 42.5, that information disclosure requirement should be deemed met when filing the top tax return.

19. How should liabilities arising under the IIR or UTPR be reported and paid/collected? Do you have any views on the frequency of such payments and the deadlines that should apply?

<u>Frequency of payments</u>

We would be of the view that there should be one payment date and that payment date should be 15 months after the last day of the reporting fiscal year .i.e., the same date for filing the top-up tax information return. (18 months in respect of the transition year)

We would recommend against introducing preliminary tax deadlines. Currently, for the purposes of corporation tax, in order to calculate preliminary tax, in many cases a company would have to forecast future profits. This is a difficult exercise and not an exact science, leaving a company open to interest for underpayments of preliminary tax. In the case of GloBE the difficulties associated with a preliminary tax payment regime is magnified. A significant amount of information would be required to calculate GloBE liabilities and it would be challenging to forecast these liabilities during the Fiscal year. It is our understanding that the UK does not intend to introduce preliminary tax rules and intends to collect the tax in one single payment. We would recommend that Ireland pursues a similar approach.

20. Do you have any views on whether Irish constituent entities should be made joint and severally liable for any Irish GloBE liabilities of the Irish constituent entities of the same MNE Group? In this regard, would you differentiate between IIR liabilities and UTPR liabilities?

21. Do you have any views on whether Irish constituent entities should be made joint and severally liable for the QDTUT (if Ireland were to adopt such a provision) of the Irish constituent entities of the same MNE Group?

22. What group entity should be made initially liable for paying UTPR tax? Is your answer dependent on whether UTPR tax is collected by way of denial of deduction or direct charge?

20. Do you have any views on whether Irish constituent entities should be made joint and severally liable for any Irish GloBE liabilities of the Irish constituent entities of the same MNE Group? In this regard, would you differentiate between IIR liabilities and UTPR liabilities?

While the top up tax is calculated by reference to the profits of the UPE and its domestic and overseas subsidiaries, the top up tax liability is ultimately a liability of the UPE (or IPE where relevant). Article 1.1 states that "*[t]his Directive establishes common measures for the minimum effective taxation of MNE and large-scale domestic groups in the form of: (a) an income inclusion rule (IIR) in accordance with which a parent entity of an MNE group or a large-scale domestic group computes and pays its allocable share of top-up tax in respect of the low-taxed constituent entities of the group… ."* Therefore, we do not think it is necessary for other members to be held joint and severally liable for any Irish GloBE liabilities.

The Directive does not expressly state which entity in a jurisdiction should be liable for paying the top–up tax under the UTPR. Article 1 of the Directive states that "*[t]his Directive establishes common measures for the minimum effective taxation of MNE and large-scale domestic groups in the form of…(b) an undertaxed profit rule (UTPR) in accordance with which a constituent entity of an MNE group has an additional cash tax expense equal to its share of top-up tax that was not charged under the IIR in respect of the low-taxed constituent entities of the group."* Article 11.1 and 12.1 states that"*… Member States shall ensure that the constituent entities located in the Union are subject, in the Member State in which they are located, to an adjustment which shall be equal to the UTPR top-up tax amount allocated to that Member State for the fiscal year in accordance with Article 13".* A combination of Article 26, 13.1, 13.2 and 13.5 calculates the amount of top up tax that shall be allocated to a particular jurisdiction. However, there does not seem to be any provisions within the Directive that allocate the UTPR to various entities within that jurisdiction. We would be of the view that the group should have an option of designating which entity should be liable for the UTPR Tax. Again, we do not think it is necessary for other members to be held joint and severally liable for any Irish GloBE liabilities.

Having entities joint and severally liable for the liabilities of other groups and/or entities may also cause complications and increase the due diligence burden on an acquisition or disposal of an entity.

21. Do you have any views on whether Irish constituent entities should be made joint and severally liable for the QDTUT (if Ireland were to adopt such a provision) of the Irish constituent entities of the same MNE Group?

Article 10.1 of the Directive states that *"if a Member State where constituent entities of an MNE group or a large-scale domestic group are located elects to apply a qualified domestic top-up tax, <u>all low-taxed constituent entities of the MNE group or a large-scale domestic group in that Member State shall be subject to that domestic top-up tax</u> for the fiscal year."* This would seem to indicate that each entity is separately subject to QDTUT and therefore presumably would be liable for its own QDTUT. Thus, in our view, it is not necessary for entities to be joint and severally liable for the QDTUT. We would further reiterate our view that having entities joint and severally liable for the liabilities of other parties may result in complications and increased due diligence on the acquisition or disposal of an entity.

22. What group entity should be made initially liable for paying UTPR tax? Is your answer dependent on whether UTPR tax is collected by way of denial of deduction or direct charge?

The Directive does not expressly state which entity in a jurisdiction should be liable for paying the top-up tax under the UTPR. Article 1 of the Directive states that "*[t]his Directive establishes common measures for the minimum effective taxation of MNE and large-scale domestic groups in the form of…(b) an undertaxed profit rule (UTPR) in accordance with <u>which a constituent entity of an MNE group has an additional cash tax expense</u> equal to its share of top-up tax that was not charged under the IIR in respect of the low-taxed constituent entities of the group."* Article 11.1 and 12.1 states that "…Member States shall ensure that <u>the constituent entities located in the Union are subject,</u> in the Member State in which they are located, <u>to an adjustment which shall be equal to the UTPR top-up tax amount</u> allocated to that Member State for the fiscal year in accordance with Article 13.

A combination of Article 26, 13.1, 13.2 and 13.5 calculates the amount of top up tax that shall be allocated to a particular jurisdiction. However, there does not seem to be any provisions within the Directive that allocate the UTPR to various entities within that jurisdiction.

We would be of the view that the group should have an option of designating which entity should be liable for the UTPR Tax.

Transition Rules

> 23. Are there any aspects of the Transition Rules[11] that require further clarification in domestic legislation?

Pre entry deferred tax balances

Pre entry into the GloBE regime, a company may have either recognised or unrecognised deferred tax balances. A recognised deferred tax balance is a balance that is included as an asset or liability on the balance sheet. An unrecognised deferred tax balance is a balance that is not included as an asset or liability on the balance sheet. For example, a company may have a deferred tax asset but does not recognise it on its balance sheet because there is a question over recoverability .e.g., a company that has a history of losses may not recognise a deferred tax asset on its balance sheet as there may be a question mark over whether the losses will ever be used.

Article 45.2, para 1 states that "*when determining the effective tax rate for a jurisdiction ………the MNE group or a large-scale domestic group shall take into account all the deferred tax assets and deferred tax liabilities reflected or disclosed in the financial accounts of all the constituent entities in a jurisdiction for the transition year.*" Article 45.2 para 3 states "*the impact of any valuation adjustment or accounting recognition adjustment with respect to a deferred tax asset shall be disregarded.*"

In respect of recognised deferred tax balance, the effect of Article 45.2, para 1 is that the unwinding of opening deferred tax balance to the income statements in the periods after entry into the GloBE regime should be taken into account when computing the ETR.

In respect of unrecognised opening deferred tax balances, para 1 & 3 of Article 45.2 would seem to treat the unrecognised deferred tax balances as recognised for GloBE purposes. Such amounts would then be unwound after entry into the GloBE regime and therefore taken into account when computing the ETR.

We would recommend that Irish legislation clarifies that the deferred tax asset/deferred tax liability that should be taken "into account" is the opening deferred tax asset/deferred tax liability at the beginning of the transition year (as defined in Article 45.1) or what would be the opening deferred tax asset or liability if such deferred tax asset/liability had been recognised. We would also recommend that the phrase in Article 45.2 "reflected or disclosed in the financial accounts" is defined in Irish legislation to clarify that this effectively means recognised and unrecognised balances.

Transfers Post 30 November 2021 and pre - Model rules

In order to prevent certain restructuring in response to the publication of the draft Directive, there is a special rule (Article 45.4) to deal with asset transfers between constituent entities taking place after 30 November 2021 and pre the commencement of the GloBE rules. In particular, Article 45.4 states that "*in the case of a transfer of assets between constituent entities after 30 November 2021 and before the commencement of a transition year, the basis in the acquired assets, other than inventory, shall be based upon the transferring* *entity's carrying value of the transferred assets upon disposal with a deferred tax assets and liabilities determined on that basis."*

The OECD commentary states ***"****10. Article 9.1.3 provides a limitation on intragroup asset transfers before applicability of the GloBE Rules. If an asset is transferred between entities after 30 November 2021 and before the Transition Year* *of a MNE Group, and such entities would have been Constituent Entities of that MNE Group had the GloBE Rules been in effect with respect to that MNE Group,* *such asset must be recorded at its historic carrying value for GloBE purposes to limit the ability to step-up the basis in such assets without including the resulting gain in the computation of GloBE Income or Loss. It follows that when this rule applies, because there is no change in asset basis, items of deferred tax expense with respect to such transaction will be recorded for GloBE purposes with respect to the historic carrying value of the assets transferred. The historic carrying value of the asset can easily be determined because the gain on the intra-group transfer and corresponding increased depreciation or amortization must be eliminated in the Consolidated Financial Statements. …"* [emphasis added]

Article 45.4 of the Directive and the OECD commentary would seem to indicate that a deemed deferred tax adjustment is required for the purposes of the GloBE calculation in these circumstances .i.e., "*the basis in the acquired assets, …, shall be based upon the transferring entity's carrying value of the transferred assets upon disposal with a deferred tax assets and liabilities determined on that basis.* However, consideration would need to be given as to how this provision is entered into and drafted for Irish law.

Subject to Tax Rule ("STTR")

24. Should amendments to any domestic legislation be considered to address potential application of, or interactions with, the STTR?

The Subject to Tax Rule ("STTR") is designed to allow certain jurisdictions to impose a top-up withholding tax on certain types of outbound payments that are made between related parties and which are taxed at a nominal rate of less than 9%. The October 2021 OECD Statement states that *"if members that apply nominal corporate income tax rates below the STTR minimum rate to interest, royalties and a defined set of other payments would implement the STTR into their bilateral treaties with developing IF members when requested to do so"* The October 2021 OECD Statement also states *that "[a] model treaty provision to give effect to the STTR will be developed …..A multilateral instrument (MLI) will be developed by the IF … to facilitate the swift and consistent implementation of the STTR in relevant bilateral treaties."*

The definition of Covered Taxes should include any amounts payable in respect of top up taxes under the STTR. Article 19.1. states that "*[t]he covered taxes of a constituent entity shall include………(c) taxes imposed in lieu of a generally applicable corporate income tax*.." Para 31 of the OECD Commentary states *"31. Paragraph (c) provides that Taxes imposed in lieu of a generally applicable CIT are Covered Taxes. …The "in lieu of" test* *includes Taxes that are not described in the generally applicable income tax definition, but which operate as substitutes for such taxes. This test, …, would generally include withholding taxes on interest, rents and royalties, and other taxes on other categories of gross payments such as insurance premiums, provided such taxes are imposed in substitution for a generally applicable income tax. Taxes imposed in lieu of a generally applicable CIT would also include taxes arising from the Subject to Tax Rule."*

While not a feature of Irish tax law currently, a key consideration associated with the STTR is its interaction with any potential territorial system of taxation. Specifically, we would have concerns that the STTR according to the October 2020 blueprint[3] may have unintended consequences with respect to payments made which are subsequently allocated to an exempt foreign branch of an Irish company .i.e., payments which are allocated to a taxable branch but are exempt in Ireland could trigger the STTR. We would refer the Department of Finance to our previous comments in our response to the consultation on the introduction of a territorial system of taxation of March 2022.

Large Scale Domestic Groups

25. The proposed Directive on Pillar Two will also apply to large-scale domestic groups[12]. Are there any aspects of the application of the Rules to large-scale domestic groups that require further clarification in domestic legislation?

The top up tax for a Large-Scale Domestic group should be computed in the same manner as any other MNE .i.e., per Article 26. Thus, the rules applicable to MNEs should equally apply to Large Scale Domestic Groups.

Where Ireland adopts a QDTUT, then it will be each constituent entity that is liable for the top up tax rather than the UPE (Article 10.1, para 1). Under Article 26, the top up tax is calculated by reference to the jurisdiction. While it is not clear presumably the top up tax is allocated to each constituent entity per Article 26.5.

[3] Refer to Part 9.2.3 of the OECD Pillar Two blueprint of October 2020, accessible here.