Transfer Pricing & Tax Avoidance

Jurisdictional comparisons **First edition 2014**

General Editor: David W Chodikoff, Miller Thomson LLP

THE EUROPEAN LAWYER REFERENCE

As clients continue to expand beyond our borders, David Chodikoff once again provides us with a relevant and timely tax manual. Another great addition for any tax practitioner's reference library.

John Doma, Partner and Principal of Bateman MacKay LLP, Chartered Accountants

In the very complex and ever-changing world of international tax, David Chodikoff's Transfer Pricing and Tax Avoidance *is a "must have" resource for the professional advisor. David is a trusted authority who I can rely upon.*

N. Gregory McNally, LLB, MBA, JD, LLM (Int'l Tax), TEP, N. Gregory McNally & Associates Ltd.

Transfer Pricing and Tax Avoidance *is a splendid comprehensive one-of-a-kind reference source for businesses, accountants, lawyers, academics and judges. It provides descriptions of the transfer pricing and tax avoidance regimes operating in 33 countries, based on contributions from experts in each of the countries. Having done some international comparative work myself in the tax avoidance area, I understand that* Transfer Pricing and Tax Avoidance *is the product of an enormous amount of work. A resource of this kind at an earlier time would have substantially shortened the time I've spent researching tax avoidance laws in foreign jurisdictions. On this basis alone I have no hesitation in saying that* Transfer Pricing and Tax Avoidance *represents an outstanding advance in the global literature for these two areas.*

Dr. Robert McMechan, Ph.D., Robert McMechan Professional Corporation

With the boom in M&A activity and worldwide intercompany transactions, this is a valuable one-stop comprehensive resource to identify the legislation, case law, guidelines and methodologies governing transfer pricing in jurisdictions throughout the world. It is interesting to examine which transfer price methodologies have been accepted or rejected in each jurisdiction.

Bruce C. Roher, CPA, CA·IFA, CBV, CFE, Partner, Fuller Landau LLP, Chartered Professional Accountants

Transfer pricing and tax avoidance are the two most vexing topics facing tax practitioners, administrators, and policy makers the world over. This comparative volume provides current, incisive insights on the state of play and details the law and practice in over 33 countries.

Kim Brooks, Dean, Weldon Professor of Law, Schulich School of Law, Dalhousie University

This ambitious volume achieves a deep synthesis of the legislation, case law, and policy surrounding transfer pricing and tax avoidance in numerous jurisdictions. It will soon take a deserved place at the top of the reading list for all students of international transfer pricing.

Benjamin Alarie, Associate Professor & Associate Dean First Year Program, Faculty of Law, University of Toronto

As tax authorities worldwide continue to allocate greater resources to auditing related party transactions, Transfer Pricing and Tax Avoidance *explains clearly the current regulatory environment facing multinationals, the documentary requirements across jurisdictions, and the importance of well-reasoned real time analysis in the allocation of risk/return between non-arm's length entities.*

David Chodikoff has marshalled an impressive group of leading global tax practitioners from 33 countries and assembled a thoroughly comprehensive text explaining the evolving world of transfer pricing and tax avoidance.

Tim Dunham, CBV, CFA, Tax Valuations Partner, Kalex Valuations Inc., Toronto, Ontario

Increasing global trade and the increased complexities and ambiguities in establishing supportable transfer pricing requires careful and precise documentation to support pricing and precise documentation to satisfy the various taxing and regulatory authorities. This work is a wonderful resource for tax professionals and Corporations in international trade. David Chodikoff and associates are to be congratulated for compiling this invaluable work.

Gabriel Nachman FCPA, FCA, Retired Partner, PricewaterhouseCoopers, Chartered Professional Accountants

This comprehensive, all-inclusive, global review of transfer pricing and tax avoidance will save you countless hours of research, time and money. Well-structured and well-written, it is the "go-to resource" when working with clients and counsel in third party jurisdictions.

James E. Ross, B.A., LL.B., President, Stonegate Private Counsel & Senior Vice President, Assante Wealth Management

It is clear that Transfer Pricing and Tax Avoidance *have become two of the most important aspects of current tax laws in virtually all of the world's industrialized countries. Although these issues have become exceedingly complex, David Chodikoff, who is an experienced and highly regarded Canadian tax litigator, has once again managed to put together a template that organizes, compares and simplifies the treatment of* Transfer Pricing and Tax Avoidance *issues in 33 countries.*

David has an outstanding ability as an editor to organize, manage and provide guidelines for contributions to a multi-author book. This book will be of great practical assistance to anyone faced with the complexity of Transfer Pricing and Tax Avoidance *issues.*

Sheldon Silver, Q.C., Counsel, Fogler Rubinoff LLP

Transfer Pricing and Tax Avoidance *is a comprehensive, concisely written study of a wide range of relevant transfer pricing topics including current legislative and regulatory frameworks, issues, methodology and case law, organized by jurisdiction. I have no doubt that it will prove to be a popular resource for* *income tax executives conducting international business as well as income tax practitioners.*

Steven Hacker, CPA, CA, CBV, Partner, Valuation and Litigation Support, Meyers Norris Penny LLP

Transfer pricing is a quintessential global problem whose solution is primarily local. While purportedly adhering to the "universal" arm's length principle, countries adopt different transfer pricing rules and practices. Obtaining reliable information on various countries' rules and practices is not easy. This collection of papers authored by a large number of country experts should serve as a great resource to those involved in transfer pricing. It is indeed a great service to the community.

Jinyan Li, Professor of Law, Osgoode Hall Law School of York University

This book is a valuable resource for those in the corporate world who currently have business operations throughout the world. Congratulations to David Chodikoff and the many contributors for assembling this timely and well organized information. Transfer Pricing and Tax Avoidance *will be a welcome addition to our corporate tax library.*

James Grundy, CPA, CA, Chief Financial Officer, NRT Technology Group of Companies

Transfer Pricing and Tax Avoidance *is a comprehensive and insightful book for lawyers, administrators and business professionals who seek international perspectives on these topics in an increasingly globalized and connected world. The chapters present key policy issues within sound methodological frameworks, including numerous historical and contemporary case studies providing tremendous breadth and depth. The attention to detail in this book is noteworthy, the given examples are astute and interesting, and the discussions of current trends maintain the relevance of this book in relation to the rapidly changing global economy. While the contributors to this book showcase their topical expertise by critiquing the strengths and weaknesses of various legislative positionalities, the common rhetorical ground across chapters is the push towards sound taxation strategies amidst a collective prioritization of how these positionalities effect and respond to the forces of international relations. Although there are still many problems in the fields of transfer pricing and tax litigation, this book inspires solutions to these problems by bringing to the fore a multitude of issues that, up until now, have not been addressed in sufficient detail.*

Eli Swirsky, President, The Torgan Group

This book is a magnificent resource for anyone responsible for planning, implementing and defending a company's transfer pricing policies.

Brad Rolph, Partner, National Transfer Pricing Leader, Grant Thornton Consulting

Globalization has encouraged increasing cross-border ties among related companies along with a corresponding rise in transfer pricing headaches. This book provides *an essential comparative perspective of national transfer pricing laws and serves as an important contribution given the renewed enthusiasm governments have shown with respect to auditing transfer prices.*

Professor Arthur Cockfield, Queen's University Faculty of Law

Once again, David Chodikoff has hit the mark with a comprehensive analysis on Transfer Pricing and Tax Avoidance*, which is both readable and up to date. This book is an excellent resource for any company considering going global.*

Vincent Cosentino, CPA, CA, Johnvince Foods Group of Companies

Transfer Pricing and Tax Avoidance *brings to us straight forward to the point front-line perspectives on the dominant topics of international taxation. Nowhere will you find this level of current, relevant, ready to use insight in one place. Many thanks to David and his extraordinarily distinguished contributors for making this a must have not only for the experienced global tax professional, but for CFOs and Principals demanding a convenient way to become and stay informed.*

Jim Reitan, Chief Financial Officer, Dr. Bernstein Diet & Health Clinics

Globalization will continue to present complex transfer pricing issues for companies and their management team. Minimizing taxes when designing these transfer pricing strategies is one of the best ways of creating shareholder value.

Kin-Man Lee, Chief Financial Officer, St. Joseph Communications

Transfer Pricing and Tax Avoidance *is the latest book effort by David Chodikoff. As the General Editor, David has brought together leading expert contributors from 33 countries to outline and provide fundamental information on the subjects of transfer pricing and tax avoidance. Whether you are a veteran international business player or simply a student of these subjects, this book is an essential resource volume for everyone's tax library.*

Alon Ossip, Chief Executive Officer, The Stronach Group of Companies

With constantly changing tax regulations around the world, the need for corporations to ensure tax efficiency for their businesses this book provides an authoritative and thorough reference guide. It is a must have textbook for anyone dealing with international tax regulations.

Nick Barisheff, CEO Bullion Management Group Inc., Toronto, Ontario

Transfer Pricing & Tax Avoidance

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General Editor:

David W Chodikoff, Miller Thomson LLP

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General Editor:
David W Chodikoff

Commissioning Editor
Emily Kyriacou

Commercial Director
Katie Burrington

Publishing Assistant
Nicola Pender

Design and Production
Dawn McGovern

Typesetting
Forewords

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Foreword

The Honourable Mr Justice Marshall Rothstein, The Supreme Court of Canada

Over the past year, there has been a surge of interest in taxation issues with international aspects. The United States' *Foreign Account Tax Compliance Act*, or FATCA, enacted to address tax non-compliance, affects American citizens residing outside of the US. It subjects financial institutions in those countries to a new set of rules. The enactment of FATCA resulted in an aspect of international taxation unexpectedly becoming the subject of popular media attention and discussion than is usually the case because of its broad effect on individuals.

For those practitioners, taxpayers and financial institutions who deal with cross-border tax issues, familiarity with international and anti-avoidance tax rules in different countries is essential. Each country's tax system is complicated enough in its own right to keep stables of lawyers and accountants busy as they attempt to navigate the inevitable complexities. These complexities are exponentially greater when a tax issue arises that involves more than one tax system. Understanding the ongoing trends of reducing tax avoidance and harmonizing tax rules between jurisdictions is vital for taxpayers, for lawyers and accountants, for governments, and for judges trying to make sense of it all.

Transfer pricing and tax avoidance rules in jurisdictions around the world demonstrate both of these trends. Transfer pricing rules, which affect where profits (and losses) are recognized, target cross-border transactions in which taxpayers seek to minimize their tax liability based on the differences between tax systems and tax rates. Tax avoidance rules, even if they are not designed to specifically address cross-border issues, are often applicable to cross-border transactions. The purpose of both types of rules is to limit tax base erosion made possible by the complexities of, and variations between, tax systems.

However, these rules come at a price: loss of clarity and predictability; being able to know and understand the tax outcome of complicated transactions and situations. International efforts such as the OECD Guidelines and Model Tax Conventions, along with regional efforts such as those effected through the European Union, attempt to achieve some clarification and predictability by establishing common practices and providing for dispute resolution mechanisms. The success of these efforts can be seen in the influence of the OECD Guidelines and Model Tax Conventions on the domestic laws, bilateral agreements, and case law of jurisdictions around the world. But in the end, tax laws are devised and imposed by individual countries (and even subdivisions within countries), meaning there is no end in sight to these issues.

Transfer Pricing and Tax Avoidance is an invaluable resource for assisting readers in understanding these issues and envisioning possible reforms. It brings together the rules, case-law (both current and historical) and trends regarding transfer pricing and tax avoidance of 33 jurisdictions in an accessible and convenient manner. The sections in each chapter regarding the international forums and relations at play in the featured jurisdictions provide valuable insight into the manner in which those jurisdictions may interact.

The cross-jurisdictional analysis made possible by this book will assist practitioners and tax authorities in dealing with specific cases. But I also anticipate that it will permit substantive examination of the principles and long-term trends underlying both domestic and international tax law, allowing interested parties and governments the ability to look ahead to the future of tax law.

This project, which brings together tax experts from around the world, will make an important contribution to this area of the law. It is noteworthy not only for its timeliness, but also for its comprehensive inclusion of numerous jurisdictions. Information regarding the tax rules in foreign jurisdiction can be hard to come by due to both lack of experience and language barriers. *Transfer Pricing and Tax Avoidance* eases those difficulties by setting out the essential concepts and serving as a launching point for more in-depth study.

I want to express my thanks to those who participated in this project. Its General Editor, David Chodikoff, has provided yet another important contribution to the literature of taxation. All contributors should be commended for the expertise and time they have brought to *Transfer Pricing and Tax Avoidance*. I have no doubt that their efforts will prove to have been well worthwhile.

Justice Marshall Rothstein
Ottawa
July 2014

Acknowledgements

David W Chodikoff, Miller Thomson LLP

This was an immense project and there are lots of people to thank for making this book a published reality. As anyone that has worked on an intense project knows, it is always one's family that hears about it or suffers, either directly or indirectly, from the demands of such a project. This explains why so many writers, editors and others in all sorts of fields thank their families first for their tolerance, patience and support. I am no different. This is my sixth edited book and I owe a great deal to my lovely and talented wife, Tanya, and my beautiful and smart son, Daniel. Thank you both!

Once again, I had the great pleasure of working with Katie Burrington. Katie, as the Commercial Director of Sweet & Maxwell's European Lawyer Reference Series, was directly involved in the recruitment of the participating law firms. Katie is also responsible for heading up the UK publishing team. The UK team consists of Emily Kyriacou, Dawn McGovern and Nicola Pender, as well as Chris Myers and Nick Allen (from Forewords). These are exceptional people that worked very hard to bring about the publication of this work in a timely fashion. I would be remiss in not singling out Nicola Pender. Over the course of the last year, Nicola and I became 'e-mail pals'. Nicola was always cheery, helpful and coordinated the proofing and publishing efforts in England. Thank you, Nicola!

In Canada, I had the pleasure of working with Jamie Walker. If the name sounds familiar, it is due to the fact that Jamie was the senior assistant editor for *Tax Litigation*, another book belonging to the family of the European Lawyer Reference Series. At the time of the first book, Jamie was still a law student but now having completed his education he is commencing his legal career by articling at Miller Thomson LLP. We are delighted to have him here. And I could not be more pleased that Jamie agreed to take on the role as senior assistant editor for the second time. Thank you, Jamie! Also returning as an assistant editor is Victoria Rodrigues. Victoria worked as an assistant editor on *Tax Litigation*. Victoria will also be commencing her legal career by articling with Miller Thomson LLP. I should also add that Victoria was a Senior Editor of the *Osgoode Hall Review of Law and Policy* (a publication of Osgoode Hall Law School, York University). Two new members of the Canadian editorial team included: Emma Nicholl (assistant editor) and Kristen Vandenberg (assistant editor). Both Emma and Kristen are second year law school students that are working at Miller Thomson LLP this summer. Both women eagerly accepted the position as assistant editors and I am very happy that they did! Their respective editing efforts have been stellar!

The co-author of the Canadian chapter of this book is Laura Etherington. If that name sounds familiar to some, it is because Laura co-wrote the Canadian chapter in *Tax Litigation*. I can hardly put into words my gratitude for Laura's hard work and gift for writing. It has made my job as co-author of the Canadian chapter exceptionally easy. Laura articled with Miller Thomson LLP last year and she has returned as an associate in the business law group. Watch for her in the years to come, Laura will undoubtedly be a superstar in the practice of law.

In the area of research, my thanks go to Kate Genest who was a student-at-law at Miller Thomson LLP. Kate, a ray of sunshine always, was a diligent worker and made a difference.

At Miller Thomson LLP, we are fortunate to have an absolutely brilliant library staff. I should know as I call upon them often and my office is literally right across from our Toronto library. The staff are always available to assist me and I thank them. They are led by Ines Freeman, the National Director of Library Services, and include: Jennifer Bonomo, Dian-Marie Galita, Julia Luke, Arlene Mazur and Erin Murphy.

It is hard to believe, but my executive assistant, Filomena Mendonca ('Fil'), has now been involved in four of these types of book projects. I cannot say enough good things about Fil. She has been my 'Chief of Staff' since May 2005 and as anyone knows – if you are on Fil's good side, you are likely to be on mine! Fil not only looks after the coordination of special projects like this one, but she is my point person in my private practice. As I have openly admitted, if I am successful in private practice, it is in no small measure a result of Fil's dedication, professionalism and hard work. Thank you, Fil. I am sincerely grateful.

A number of my partners at Miller Thomson LLP were highly supportive of my efforts and I would be remiss in not naming my biggest boosters (or those that listened to my rants and never complained!): James ('Jim') Hutchinson, Martin ('Marty') Rochwerg, Peter Auvinen, Thomas ('Tom') Whitby, Mark Frederick, William ('Bill') Fowlis, Robert Hayhoe, John Campbell, Susan Manwaring, Amanda Stacey, Tamara Farber, Michael Kerr, Emily Cole, Susan Metzler, James ('Jim') Klotz, Greg Shannon, Crystal Taylor, Sandra Gogal, Lyne Gaulin, Hugh Dyer, Kent Davidson, Barbara ('Barb') Doherty, Shashi Malik and last but not least, Andy Chan.

I would also like to thank The Honourable Mr Justice Marshall Rothstein for his wonderful Foreword. Mr Justice Rothstein is an extraordinary jurist and it is truly an honour to have him grace these pages with his words of insight and praise. Thank you, Mr Justice Rothstein!

As readers will note, there are a number of endorsements from business leaders, chief financial officers, chartered accountants, transfer pricing experts and academics. I am sincerely thankful for this incredible and generous support. On behalf of all of the contributors, we thank you!

Finally, my thanks to each and every contributor. This was an extraordinary effort taken on by dozens of people from *33* different countries. Every single contributor truly displayed a great sense of responsibility by meeting tight deadlines and by producing chapters of true value. Thank you, contributors!

David W Chodikoff
General Editor, August 2014

Preface

David W Chodikoff, Miller Thomson LLP

It was in the fall of 2013 that Thomson Reuters, Sweet & Maxwell held a successful launch of the publication of *Tax Litigation* at the annual International Bar Association conference in Boston, Massachusetts; *Tax Litigation* is yet another hardcover volume to be added to the growing stable of titles that make up The European Lawyer Reference Series. I was fortunate to be the General Editor of *Tax Litigation*. I had the very good luck of working with some incredibly talented and devoted people.

As a result of that experience, I thought that two key tax subjects that would benefit from the same type of treatment as *Tax Litigation* were Transfer Pricing and Tax Avoidance. Obviously, the people at The European Lawyer Reference Series, agreed. More to the point, so, too, did the contributors from 32 other participating jurisdictions.

In your hand, you are holding a resource book that has the same template for every chapter. The chapters are broken down into two parts. The first part deals with transfer pricing and covers the following subjects: an overview, the legislative framework, national policy issues, case law, penalties and dispute resolution mechanisms. The second half of each chapter focuses upon tax avoidance. The subjects include: acceptable tax planning areas/subjects, defining abusive tax avoidance, the legislative framework, key areas of interest, penalties and current trends.

On behalf of all of those involved in this project, we hope that you, the reader, find this a useful and stimulating volume of work that will lead you to further reading, thinking and your own writings on the subjects of transfer pricing and tax avoidance.

David W Chodikoff
August 2014

Ireland

Matheson Joe Duffy & John Ryan

PART ONE: TRANSFER PRICING

1. GENERAL OVERVIEW

Ireland introduced formal transfer pricing legislation for the first time in 2010. The *Finance Act*, 2010 introduced a new transfer pricing regime to Ireland for accounting periods commencing on or after 1 January 2011, for transactions the terms of which were agreed on or after 1 July 2010 (the 'Transfer Pricing Rules').

Broadly, the Transfer Pricing Rules require domestic and international transactions between associated persons undertaken in the course of trading activities to be entered into at arm's length. Where an arrangement between associated entities is made otherwise than at arm's length, an adjustment may be made to the Irish profits. An adjustment is only made where income is understated or expenses are overstated.

The transfer pricing legislation specifically provides that the Transfer Pricing Rules should be construed in accordance with the 2010 OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (the 'OECD Guidelines').

2. IDENTIFICATION OF LEGISLATIVE FRAMEWORK

Part 35A of the Taxes Consolidation Act 1997 (the 'TCA') sets out the relevant transfer pricing legislation. We set out below the circumstances in which the Transfer Pricing Rules apply, the arrangements that are specifically excluded from the application of the Transfer Pricing Rules, and the consequences of the application of the Transfer Pricing Rules.

The Transfer Pricing Rules apply in the following circumstances:

(a) There is an 'arrangement' involving the supply and acquisition of goods, services, money or intangible assets. *'Arrangement'* is defined very broadly and means *'any agreement or arrangement of any kind (whether or not it is, or is intended to be, legally enforceable).'*[1]

(b) At the time of the supply and acquisition, the supplier and acquirer are 'associated'. Two persons are associated if (1) one person participates in the management, control or capital of the other, or the same person participates in the management, control or capital of each of the two persons, and (2) the first person is participating in the management, control or capital of the other person if that other person is a company controlled by the first person.[2]

1 Section 835C TCA.
2 Section 835B TCA.

(c) The profits or gains or losses arising from the relevant activities are in respect of 'trading' activities.[3] *'Trading'* is defined in Irish legislation as including *'every trade, manufacture, adventure or concern in the nature of a trade.'* This is a key characteristic of the Transfer Pricing Rules that is quite unusual.

There is no definition of 'trade' in Irish tax legislation. Generally, to be trading, the Irish company should be engaged in the key profit-making commercial activity and should have the persons in Ireland with the requisite skill and expertise to perform that activity.[4] Certain activities may be subcontracted to third parties; however, the directors must be involved in managing the commercial activity and strategic policy of the company.

In most cases, there will be little doubt about whether a company's activities constitute trading. Guidance as to what constitutes 'trading' is derived from case law and by reference to a set of rules known as the Badges of Trade. These rules were drawn up in 1955 by the UK Royal Commission on the Taxation of Profits and Income and have been approved by Irish courts. The Badges of Trade, and matters to be considered in determining whether a particular activity constitutes a trade, include the following: (i) subject matter; (ii) length of ownership; (iii) frequency of transactions; (iv) supplementary work; (v) circumstances for sale; (vi) motive for transaction.

These issues have been considered extensively in the courts. In *IRC v Fraser*,[5] the taxpayer bought and sold a large quantity of whiskey and was held to be trading on the basis that the whiskey acquired was more than he could personally use. In *Leach v Pogson*,[6] over the course of 4 years, the taxpayer set up and disposed of 29 driving schools and was held to be trading. In *IRC v Livingston*,[7] the taxpayers acquired a cargo vessel and sold it at a profit and were held to be trading on the basis that even though it was an isolated transaction, substantial work was undertaken with a view to a subsequent disposal. In the UK High Court case of *Noddy Subsidiary Rights Company Limited v CIR*,[8] a company was formed to exploit the name and image rights of a character from a children's book. It was held that, in certain circumstances, the exploitation of these rights could constitute a trade. In this case, considerable weight was placed on the evidence of a high degree of activity associated with trying to promote the brand in question, seeking out and evaluating licensees, and of dealing with third parties.

A guidance note on the classification of activities as trading has been issued by the Irish Revenue Commissioners ('Irish Revenue') and states that they may be prepared to express a view as to whether a particular

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3 Section 835C TCA.
4 This is based on relevant case law in the area as well as the Revenue Guidance on the Classification of Activities as Trading (19 August 2010); available at: *http://www.revenue.ie*.
5 24 TC 498.
6 40 TC 585.
7 11 TC 538.
8 43 TC 458.

transaction or operation amounts to a trade or will qualify for the 12.5 per cent rate. In arriving at a decision, Irish Revenue endorse the *Noddy* case and have stated that the key considerations in their view are:

(i) Is there any commercial rationale for the type of situation proposed?
(ii) Is there any real value added in Ireland?
(iii) Are there employees in Ireland with sufficient levels of skill to indicate that the company is actively carrying on a trade?

Irish Revenue have also published details of cases submitted and opinions issued in the period from December, 2002 to December, 2011 on the classification of activities as trading activities.[9] Irish Revenue have stated that opinions on the classification of activities as trading are arrived at with reference to the specific facts and circumstances of each case. The key issues in the decision-making process are the activity, authority and skill levels within the company.

(d) Transactions undertaken otherwise in the course of a trade are not subject to the Transfer Pricing Rules. However, for Irish capital gains tax purposes, transactions between connected persons are deemed to be otherwise than a bargain at arm’s length and are therefore deemed to be for a consideration equal to the market value[10].

The Transfer Pricing Rules are excluded in the following circumstances:

(a) The arrangement is concluded within a ‘small or medium-sized enterprise’. A small or medium-sized enterprise means an enterprise which would fall within the category of micro, small and medium-sized enterprise as defined in the Annex to the Commission Recommendation 2003/361/EC of 6 May 2003 (OJ L124, 20 May 2003, p. 36 (broadly, less than 250 employees and either a turnover of less than EUR 50 million or assets of less than EUR 43 million on a group basis).[11]
(b) The arrangement was agreed before 1 July 2010. The transfer pricing legislation includes a ‘grandfathering clause’,[12] which seeks to ensure that arrangements in place before 1 July 2010 are not subject to the Transfer Pricing Rules. This creates some uncertainty for taxpayers where a pre-1 July 2010 arrangement is varied, though the arrangement itself may remain in place as to whether the arrangement remains grandfathered. The view of Irish Revenue, although not published officially, is that for an arrangement to remain grandfathered, the arrangement existing as at 1 July 2010 should be able to ‘deliver the terms’ of the ongoing arrangement.
(c) The arrangement relates to a section 110 securitization special purpose vehicle. Section 110 of the TCA contains a specific legislative requirement that the transactions entered into by a qualifying company should be by way of bargain at arm’s length, except in respect of profit participating loan notes issued by a qualifying company.

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9 Revenue Guidance on the Classification of Activities as Trading (19 August 2010); available at: *http://www.revenue.ie*.
10 Section 547 TCA.
11 Section 835E TCA.
12 Section 42 Finance Act 2010.

The consequences of the application of the Transfer Pricing Rules are as follows:

(a) Where an arrangement between associated entities is made otherwise than at arm's length, an adjustment may be made where the Irish company has understated income or overstated expenses. 'Arm's length amount' is defined as the amount of the consideration that independent parties would have agreed to, had those independent parties entered into that arrangement.[13]

(b) The relevant person to which the Transfer Pricing Rules apply must have available such records as may be reasonably required for the purpose of determining whether the trading profits have been computed on an arm's length basis in accordance with the Transfer Pricing Rules.[14]

2.1 Federal legislation

Ireland does not have applicable federal and state/provincial legislation.

2.2 State or provincial legislation

Ireland does not have applicable federal and state/provincial legislation.

2.3 International treaties and agreements

The primary source of international law impacting transfer pricing in Ireland are the 70 double tax treaties entered into by Ireland. For Irish tax purposes the provisions of double tax treaties take precedence over domestic law.[15] In addition the transfer pricing legislation specifically provides that the Transfer Pricing Rules should be construed in accordance with the OECD Guidelines.[16]

(a) Double tax treaties

From a transfer pricing perspective, double tax treaties are typically most relevant where there is an allocation of profits to a permanent establishment in accordance with Article 9 of the OECD Model Tax Convention on Income and Capital Gains (the 'OECD Model Convention').[17]

In situations where there is a dispute about the profits allocable to a permanent establishment most Irish double tax treaties include a mutual agreement procedure article in accordance with Article 25 of the OECD Model Convention.

Almost all Ireland's double tax treaties contain an exchange of information provision. This is particularly important in the context of transfer pricing audits and it is important to note that Irish Revenue have wide information gathering powers and this information can be provided to tax treaty partner countries.

[13] Section 835C TCA.
[14] Section 835F TCA.
[15] Section 826 TCA.
[16] Section 835D TCA.
[17] 22 July 2010.

(b) OECD guidelines

The transfer pricing legislation specifically provides that the Transfer Pricing Rules should be construed in accordance with transfer pricing guidelines. The *'transfer pricing guidelines'* are defined quite broadly and includes *'such additional guidance, published by the OECD on or after the date of passing of the Finance Act 2010, as may be designated by the Minister for Finance … by order …'*

In effect this means that the Transfer Pricing Rules must be construed in accordance with all relevant, current and future OECD guidelines. Furthermore, it means that transfer pricing discussions with Irish Revenue are typically framed and discussed in the context of OECD guidelines.

3. NATIONAL POLICY ISSUES

Ireland's overarching policy with respect to transfer pricing is that it should be construed in a manner that is consistent with the OECD guidelines. Furthermore Ireland has sought to link the application of the Transfer Pricing Rules to the availability of the 12.5 per cent tax rate on trading income.

3.1 Overall national policy announcements

In recent years the key national policy announcement was the introduction of transfer pricing legislation taking effect from accounting periods commencing on or after 1 January 2011. Irish Revenue has since stated that they intend to apply a collaborative approach to transfer pricing audits.

3.2 National revenue authority initiatives

In November 2012, in the context of a collaborative approach to transfer pricing, Irish Revenue announced that Transfer Pricing Compliance Reviews ('TPCRs') would form the cornerstone of monitoring compliance with the transfer pricing legislation.[18] The TPCR process was seen as an appropriate mechanism to optimize the use of resources in Irish Revenue's transfer pricing intervention program having regard to the complex and time-consuming nature of transfer pricing audits. It is hoped that the TPCR would represent a collaborative approach to monitoring compliance with the transfer pricing rules. The TPCR program is discussed in more detail in section 6 below.

3.3 Administrative statements

In conjunction with the publication of the relevant transfer pricing legislation in the *Finance Bill*, 2010 Irish Revenue published a Q&A paper providing background to the introduction to the Transfer Pricing Rules,[19] what is meant by transfer pricing and the arm's length principle, how it would apply and what it would mean in practice for businesses operating in Ireland.

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18 *www.revenue.ie/en/about/foi/s16/income-tax.../35a-01-01.pdf.*
19 *www.revenue.ie/en/practitioner/law/bills/archive/.../transfer-pricing.pdf.*

3.4 Administrative guidelines

(a) Notes for guidance on legislation

Irish Revenue have published the Notes for Guidance on Part 35A of the TCA which summarises the relevant legislative provisions and Irish Revenue's interpretation of the legislation in an easy-to-read format.[20]

(b) Freedom of information material published

Irish Revenue's operations manual contains an overview of the approach to transfer pricing and includes information regarding the overall structure of the legislation, the TPCR process and documentation requirements.[21]

(c) Transfer pricing documentation

Section 835F of the TCA imposes an obligation on companies to have available records as may reasonably be required for the purposes of determining whether the trading income of the company has been computed on an arm's length basis; however, Irish tax legislation is not prescriptive as to the form of that documentation. Irish Revenue have provided some guidance on documentation requirements.[22] The following is an overview of Irish transfer pricing documentation guidance:

(i) There is no standard or required form of transfer pricing documentation. However, the EU Council code of conduct, EU Transfer Pricing Documentation,[23] and Chapter V of the OECD Guidelines are considered good practice.

(ii) Documentation should be available at the time the relevant tax return is made although it is best practice that the documentation is prepared at the time of the transaction in question.

(iii) Suitable documentation may already be held by another group company.

(iv) The extent of documentation depends on the facts. The cost and administrative burden of preparing documentation should be commensurate with the risk involved. For example, it would be expected that complex and high-value transactions would generally require more detailed analysis and related documentation than simple, easily understood and comparable, high-volume transactions.

(v) The quality of the documentation will be a key factor in determining whether an adjustment on audit should be regarded as correcting an innocent error or a technical adjustment. The quality of the documentation will depend on its suitability for purpose. Again, for complex high-value transactions the benchmark for what represents quality documentation will be higher.

(vi) At a minimum, the transfer pricing documentation should identify:
   (1) the associated persons for the purposes of the legislation;

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20 *www.revenue.ie/en/practitioner/law/notes-for-guidance/tca/part35a.pdf.*
21 *www.revenue.ie/en/about/foi/s16/income-tax.../35a-01-01.pdf.*
22 Tax Briefing 07/2010.
23 OJ No. C176, 28.07.2006, p.1.

(2) the nature and terms of transactions within the scope of the legislation;
(3) the method or methods by which the pricing of transactions were arrived at, including any study of comparables and any functional analysis undertaken;
(4) how that method has resulted in arm's length pricing (this will usually include an analysis of market data or other information on third-party comparables);
(5) any budgets, forecasts or other papers containing information relied on in arriving at arm's length terms; and
(6) the terms of relevant transactions with both third parties and associates.

4. CASE LAW

As Ireland has only recently introduced the Transfer Pricing Rules there are no litigated Irish transfer pricing cases. Furthermore, Irish Revenue are currently trying to position transfer pricing as a collaborative rather than confrontational matter and therefore transfer pricing litigation is not seen as a policy priority right now.

4.1 Current cases

There are no transfer pricing cases currently before the Irish courts.

4.2 Historical cases of note

Ireland only introduced transfer pricing legislation with effect from accounting periods commencing on or after 1 January 2011. However, *Belville Holdings v Cronin*,[24] a High Court case that predates the introduction of the transfer pricing legislation, is often quoted as supporting the proposition of a general transfer pricing rule in Irish law outside the transfer pricing legislation. In this case the taxpayer was a holding company that also carried on the trade of managing and financing its subsidiaries. The holding company recharged only a part of its operating expenses to the subsidiaries thereby generating a trading loss which it sought to set off against dividends received by its subsidiaries. The High Court held that, effectively, a charge should be made by the holding company for the service it provided and the charge should be an amount to bring the transaction within the realm of being a bona fide transaction in the ordinary course of business. However the court did not give any view as to what the appropriate charge should be and it is not certain how widely the *Belville* case can be interpreted. It is not certain that *Belville* requires an 'arm's length charge' (rather it requires a charge to bring it 'within the realm of being a bona fide transaction').

[24] III ITR 340.

5. PENALTIES

The Transfer Pricing Rules do not prescribe a separate penalty regime and therefore general tax legislation[25] and the Code of Practice for Revenue Audit[26] will be applicable.

5.1 Types of penalties

In a case where a penalty arises, the amount of the penalty due is generally computed by the Irish Revenue auditor, agreed with the taxpayer and paid. Where there is no agreement between Irish Revenue and the taxpayer on the amount of the penalty, or where an agreed penalty is not paid, the penalty due will be determined by a court.

The applicable penalty is a tax-geared penalty, as set out in the TCA,[27] and can vary depending on (i) the category of default giving rise to the penalty, (ii) whether the taxpayer has made voluntary qualifying disclosure of the underpayment of tax and (iii) whether the taxpayer co-operates during the course of the audit.

The relevant categories of default are (a) deliberate behaviour; and (b) careless behaviour, (i) with significant consequences; or (ii) without significant consequences.

(a) Deliberate behaviour penalties

Deliberate behaviour is not defined in the TCA and is, therefore, given its normal meaning. In general, deliberate behaviour involves either a breach of a tax obligation with indicators consistent with intent on the part of the taxpayer or a breach that cannot be explained solely by carelessness. For deliberate behaviour penalties to apply, the auditor must be satisfied (i) that the facts of the case are consistent with intent to default, or (ii) that the taxpayer's actions or omissions were likely to result in a tax default and those actions or omissions cannot be explained solely by carelessness.

(b) Careless behaviour penalties

Taxpayers must exercise care in fulfilling their tax obligations. Careless behaviour means a lack of due care rendering tax liabilities returned by the taxpayer, or repayment claims made, incorrect. Careless behaviour is distinguished from deliberate behaviour by the absence of indicators, in the facts and circumstances of the default, consistent with intent.

'Carelessly' is defined in the Acts as meaning the *'failure to take reasonable care.'* The test of reasonable care is *'whether a taxpayer of ordinary skill and knowledge, properly advised, would have foreseen as a reasonable probability or likelihood the prospect that an act (or omission) would cause a tax underpayment, having regard to all the circumstances.'* The taxpayer cannot devolve the responsibility of making a correct return to an agent. If all relevant matters have not been brought to the attention of the agent, the taxpayer has not taken due care.

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25 Part 47 TCA.
26 *www.revenue.ie/en/practitioner/code-of-practice-revenue-audit.pdf*.
27 Section 1077E TCA.

Where there is careless behaviour, the appropriate penalty depends on whether that careless behaviour gave rise to significant consequences.

(i) Careless behaviour with significant consequences is distinguished from careless behaviour without significant consequences by reference to the size of the shortfall relative to the correct tax liability concerned.

(ii) Significant consequences: this phrase is not defined in the TCA but is used to describe the statutory penalty applicable where the tax underpaid exceeds 15 per cent of the tax correctly payable. The 15 per cent test is to be applied separately to each tax type and period in respect of which a return or statement of liability is required to be made by the taxpayer. In the case of a reduction in a repayment made, if any, compared with the repayment claimed, if the reduction exceeds 15 per cent of the amount of the repayment claimed by the taxpayer, a penalty in the category of careless behaviour with significant consequences will apply if the incorrect claim arose from a lack of due care by the taxpayer.

Penalty Mitigation Table in respect of penalties imposed after 24 December 2008.

Qualifying disclosure	Category of default	Co-operation	
		Prompted	Unprompted
All qualifying disclosures in this category	Careless behaviour without significant consequences	10 per cent	3 per cent
First qualifying disclosure in these categories	Careless behaviour with significant consequences	20 per cent	5 per cent
	Deliberate behaviour	50 per cent	10 per cent
Second qualifying disclosure in these categories	Careless behaviour with significant consequences	30 per cent	20 per cent
	Deliberate behaviour	75 per cent	55 per cent
Third or subsequent qualifying disclosure in these categories	Careless behaviour with significant consequences	40 per cent	40 per cent
	Deliberate behaviour	100 per cent	100 per cent
No qualifying disclosure	**Category of default**	**No co-operation**	**Co-operation only**
All defaults where there is no qualifying disclosure	Careless behaviour without significant consequences	20 per cent	15 per cent
	Careless behaviour with significant consequences	40 per cent	30 per cent
	Deliberate behaviour	100 per cent	75 per cent

5.2 Special or notable cases

There are no Irish court cases that discuss the imposition of penalties. However the imposition of penalties and the opportunities to mitigate are discussed in detail in the Code of Practice for Revenue Audit published by Irish Revenue.

6. DISPUTE RESOLUTION MECHANISMS

In the first instance Irish Revenue prefers to handle transfer pricing investigations by way of TPCR. Cases may escalate from TPCR to full transfer pricing audit. International transfer pricing matters (eg, seeking correlative relief in Ireland for transfer pricing adjustment made in another jurisdiction) may be resolved either unilaterally, through the mutual agreement procedure under the relevant double tax treaty or under the European Arbitration Convention. Transfer pricing matters may be agreed in advance by way of bilateral Advance Pricing Agreements ('APAs'). Current policy is that Irish Revenue will not provide a unilateral APA.

6.1 Preferred national options

(a) TPCR

Taxpayers are selected on a risk assessment basis to conduct a self-review on their transfer pricing for a specified period. Taxpayers have three months to conduct the self-review and to provide a report to Irish Revenue.

TPCRs are not formal audits and adjustments may be agreed upon under the TPCR without the imposition of any penalties. If Irish Revenue is satisfied with the results of the TPCR, a letter confirming that they have no further enquiries will be issued, giving taxpayers comfort that their transfer pricing policy for that period has been accepted by Irish Revenue. Where Irish Revenue is not satisfied with the level of information received, or with the transfer pricing, TPCRs may be escalated to more formal audits (with the related risk of penalties). However, Irish Revenue considers the TPCR to be a substantial compliance check in its own right and not normally a precursor to a transfer pricing audit. While the TPCR process is in its infancy, the approach to date, in respect of the TPCRs, has been cooperative and open.

The report to Irish Revenue under the TPCR should provide the following information:

(i) The group structure
(ii) Details of transactions by type and associated companies involved
(iii) Pricing and transfer pricing methodology for each type of transaction
(iv) The functions, assets and risks of parties
(v) A list of documentation available/reviewed
(vi) The basis for establishing how the arm's-length standard is satisfied

The information does not have to be provided in a particular format and Irish Revenue has confirmed that where a transfer pricing study or report already exists, that study will suffice, provided it contains the information listed above.

(b) Full transfer pricing audit

A transfer pricing audit is conducted in the same manner as a regular corporation tax audit. The tax audit and appeal procedure can be summarised as follows:

(i) Cases are selected for audit by Irish Revenue primarily on a risk assessment basis though some random audits are conducted. In addition a full audit may escalate from the conduct of a TPCR.
(ii) Typically Irish Revenue will provide 21 days' notice of an audit setting out the scope and nature of the audit.
(iii) Following notification of the audit, the taxpayer is still entitled to file a prompted qualifying disclosure of any underpayment of taxes which can ultimately result in a mitigation of penalties.
(iv) Following the audit Irish Revenue may issue a notice of assessment to corporation tax setting out the underpayment of tax together with interest and penalties payable by the taxpayer.
(v) The taxpayer must lodge an appeal to an assessment within 30 days. Appeals are heard by the Appeal Commissioners.
(vi) If the Appeal Commissioners determine the appeal the matter may be reheard before the Circuit Court and ultimately appealed to the High Court and Supreme Court.
(vii) If the Appeal Commissioners dismiss the appeal the taxpayer can only appeal to the High Court or Supreme Court if he considers that having regard to the available evidence, the dismissal of the appeal was unreasonable.

6.2 International options

(a) Unilateral Relief

From a transfer pricing perspective, double tax treaties are typically most relevant where there is an allocation of profits to a permanent establishment in accordance with Article 9 of the OECD Model Convention. Irish Revenue may accept a transfer pricing adjustment under Article 9(2) without formally engaging in a MAP.

Many of Ireland's double tax treaties do not include an equivalent to Article 9(2) of the OECD Model Convention. This means that there is potentially double taxation where an adjustment is made to profits in accordance with such double tax treaties, because Irish domestic law requires that a corresponding adjustment can only be taken in such instances where the adjustment is taken in accordance with a double taxation agreement. However, although not legally obliged to allow a corresponding adjustment where there is no equivalent to Article 9(2) of the OECD Model, Irish Revenue generally allow for relief from double taxation on the basis of a claim under the MAP article of the relevant double tax treaty or EU Arbitration Convention.

(b) Mutual agreement procedure

There is no formal procedure for undertaking a MAP under Irish law however the MAP request should (i) quote the legal basis for the MAP ie, the relevant Article in Ireland's double taxation treaties/agreements or EU Arbitration Convention; (ii) explain why a MAP is considered necessary; (iii) explain the issues involved (attaching relevant background documentation); and (iv) set out what the requester considers to be the correct outcome (attaching any documents, case law, etc, backing up the requester's view). Furthermore if the MAP request(s) is being made to more than one Competent Authority, the Irish Competent Authority should receive the same information as the other Competent Authority(ies).

(c) EU Arbitration Convention

In the MAP Article 25, there is typically no obligation on the respective Competent Authorities to reach a binding decision. They are typically only required to endeavour to resolve the case and find a solution. As such, binding arbitration procedures are useful in coming to a final solution for the taxpayer where the MAP process has proved unsuccessful.

The EU Arbitration Convention[28] currently applies in all EU Member States and provides for a process to resolve disputes arising in connection with the adjustment of profits between associated enterprises (ie, transfer pricing adjustments).

Where a taxpayer believes that there is double taxation as a result of a transfer pricing adjustment, a claim must be presented to the Competent Authority of the country in which it is resident (eg, Ireland) within 3 years of adjustment being made. If Irish Revenue consider that the claim is well-founded and if Irish Revenue cannot solve the issue unilaterally, it will be obliged to attempt to resolve it by mutual agreement with the Competent Authority of the other EU Member State.

Where no agreement has been reached between the two Competent Authorities within two years, the matter is sent to an arbitration commission for an opinion regarding how to eliminate the double tax. The arbitration commission board usually consists of two independent 'persons of standing' from the arbitration panel, a chairperson and the representatives of the Competent Authorities. The decision of the arbitration commission shall be reached within a six month period; however, this decision is not binding on the parties involved. The Arbitration Convention merely requires the Competent Authorities to reach a final binding decision within a further six months after the conclusion of the proceedings of the arbitration panel.

(d) Advance pricing agreement

Irish Revenue will consider bilateral or multilateral APAs. However, as a policy matter, they will generally not consider unilateral APAs. The APA process is similar to the MAP process described above.

PART TWO: TAX AVOIDANCE

7. ACCEPTABLE TAX PLANNING AREAS/SUBJECTS

The scope of acceptable tax planning in Ireland has narrowed over the last number of years. Most recently the Irish Supreme Court has held in *O'Flynn*

[28] Convention 90/436/EEC

Construction Limited v Revenue Commissioners[29] that the Irish general anti-avoidance rule ('GAAR') should be broadly interpreted.

There is no comprehensive list of transactions which Irish Revenue consider to be abusive. However the *Finance Act*, 2010 introduced a mandatory disclosure regime for certain transactions.[30] Irish Revenue emphasise in published guidance notes that, just because a transaction falls within the mandatory disclosure regime, does not mean that it falls afoul of the GAAR. However the type of transactions which are identified as being subject to mandatory disclosure are indicative of the type of transaction that Irish Revenue regard as undesirable and may fall afoul of the GAAR.

A disclosable transaction is a transaction or a proposal for a transaction which gives rise to a tax advantage (being the main or one of the main benefits expected from the transaction) and which also falls within one of the following specified descriptions:

(a) There is a desire to keep the scheme confidential from other promoters or from Irish Revenue.
(b) It would be reasonable to expect a premium fee to be charged on the basis of how it gives rise to the expected tax advantage.
(c) The scheme is a standardised tax product that does not require tailoring to client's specific circumstances to any material extent.
(d) The scheme creates a tax loss that can be used by more than one individual client and the main outcome of the transaction, to an informed observer, is the provision of tax losses.
(e) A transaction structured so as to create a loss buying scheme for corporates.
(f) Employment schemes that generate a tax advantage for an employer, employee or any other person. This does not include routine schemes that already involve Irish Revenue oversight (eg, retirement benefit schemes).
(g) Schemes that convert income (taxable at a higher rate) into capital gains (taxable at a lower rate). This does not include routine schemes that already involve Irish Revenue oversight (eg, share ownership trusts).
(h) Schemes that convert income (taxable at a higher rate) into a gift (taxable at a lower rate).

It is important to note that Irish Revenue do not consider that routine day to day tax advice and the routine use of statutory exemptions and reliefs for bona fide purposes should be regarded as disclosable transactions.

8. DEFINING ABUSIVE TAX AVOIDANCE

(a) GAAR

Section 811 TCA contains Ireland's GAAR for tax purposes. It is intended to defeat the effect of transactions which have little or no commercial reality but are intended to reduce or avoid a tax charge or to artificially create a tax deduction or a tax refund.

[29] 14 December 2011.
[30] Part 33, Chapter 3 TCA and related regulations.

The GAAR applies where Irish Revenue form the opinion that a transaction is a 'tax avoidance transaction'. A tax avoidance transaction is a transaction that gives rise to a tax advantage and was not undertaken or arranged primarily for purposes other than to give rise to a tax advantage. In considering whether a transaction is a tax avoidance transaction Irish Revenue should consider the results of the transaction, its use as a means of achieving those results and any other means by which the results or part of the results could have been achieved.

The GAAR directs that a transaction should not be a tax avoidance transaction where either (a) it was undertaken with a view to the realisation of profits in the course of the business and was not undertaken primarily to give rise to a tax advantage, or (b) it was undertaken to obtain the benefit of a relief/allowance/abatement provided in the TCA and was not a misuse or abuse of that provision.

In determining whether a transaction is a genuine commercial transaction or the legitimate use of a tax relief, Irish Revenue can give regard to the substance of a transaction and related transactions so as to get behind the mere form of the transaction. The GAAR is considered in more detail below.

(b) Case law

The GAAR was introduced in 1987. However, there has only been one material case decided by the Irish courts in respect of its meaning, namely the *O'Flynn* case. This case was recently decided by the Irish Supreme Court, which delivered an instructive majority judgment on the way in which section 811 of the TCA should be applied. The facts in question involved a series of pre-planned steps designed to permit a building and construction business access to a tax relief intended to promote export sales. The Supreme Court held against the taxpayer, and the majority judgment offered some trenchant criticism of aggressive tax planning. The *O'Flynn* case is considered in more detail below.

(c) Mandatory disclosure regime

As outlined above a mandatory disclosure regime was introduced in the *Finance Act*, 2010 as part of an attempt to identify and shut down unacceptable tax planning.

9. THE LEGISLATIVE FRAMEWORK

(a) Tax Avoidance Transaction

The concept of a 'tax avoidance transaction' is the key concept in the GAAR. It is defined as a transaction which meets two conditions:

(i) The transaction must give rise to (or but for section 811 of the TCA would give rise to) a 'tax advantage'.

(ii) The transaction must not have been undertaken or arranged primarily for purposes other than to give rise to a 'tax advantage'.

It was observed by the Supreme Court in the *O'Flynn* case that this test is directed towards 'making the difficult distinction between a commercial transaction which has been legitimately structured in such a way as to mitigate the tax due on the one hand, and a purely tax-driven transaction designed to give rise to a tax advantage on the other'. The Supreme Court acknowledged that this is a distinction 'more easily described than applied'.

There are two initial points to address. First, the matter in question must constitute a 'transaction'. A *'transaction'* is defined to include any *'course of action'* or *'course of conduct'*. Second, the transaction must give rise to a 'tax advantage'. A *'tax advantage'* includes a *'reduction or avoidance or deferral'* of any charge to Irish tax or to any *'potential or prospective'* charge to Irish tax.

(c) Matters which must be considered

In determining whether a transaction is a 'tax avoidance transaction', there are various features of the transaction required by section 811 of the TCA to be considered by Irish Revenue.

First, Irish Revenue must have regard to 'any one or more' of the following:

(i) The results of the transaction.
(ii) The use of the transaction as a means of achieving those results.
(iii) Any other means by which the results (or any part of the results) could have been achieved.

Second, Irish Revenue must have regard to all of the following:

(i) The form of the transaction.
(ii) The substance of the transaction.
(iii) The substance of any other transaction or transactions with which that transaction may reasonably be regarded as being directly or indirectly related to or connected.
(iv) The final outcome and result of that transaction and any combination of those other transactions which are so related or connected.

In considering the 'substance' of a transaction, the Supreme Court in the *O'Flynn* case took a very broad approach. In that case, the Supreme Court reviewed the 40-plus steps involved and then considered, analysed and concluded on them in the whole. The Supreme Court looked at the starting point and the end point, and drew conclusions with respect to the overall effect of the arrangement. The Supreme Court did not focus on any particular step, nor did the Supreme Court identify any single step as the transaction in respect of which the desired relief could be dis-applied.

(c) Safe-harbours

The legislation also provides for two safe-harbours, where a transaction will not be a 'tax avoidance transaction':

(i) The first safe-harbour is for 'business profits'. This applies where a transaction was undertaken with a view (directly or indirectly) to the realisation of profits in the course of the business activities of a business carried on by a person. The transaction in question must not have been undertaken or arranged primarily to give rise to a tax advantage. This safe-harbour applies even if the purpose or purposes of the transaction could have been achieved by some other transaction which would have given rise to a greater amount of tax being payable.

(ii) The second safe-harbour is for the 'proper use' of a tax relief. This applies where the transaction was undertaken or arranged for the purpose of obtaining the benefit or any relief, allowance or other abatement and that transaction would not result (directly or indirectly) in a *'misuse of the provision or an abuse of the provision, having regard to the purposes for which it was provided.'*

10. KEY CASES OF INTEREST

The GAAR was introduced in 1987. However, there has only been one material case decided by the Irish courts in respect of its meaning, namely the *O'Flynn* case.

The *O'Flynn* case is analysed in detail below. However, at this stage it is worth highlighting that the Supreme Court held that the purpose of section 811 of the TCA was to reverse the *Duke of Westminster* case[31] in Ireland. The *Duke of Westminster* case was a United Kingdom House of Lords case decided in 1936, which had (broadly) supported a 'form over substance' approach to the application of tax legislation. In the leading judgment of the Duke of Westminster, it was held that *'[e]very man is entitled if he can to order his affairs so as that the tax attaching … is less than it would otherwise be. If he succeeds in ordering them so as to secure this result, then, however unappreciative the Commissioners of Inland Revenue or his fellow taxpayers may be of his ingenuity, he cannot be compelled to pay an increased tax.'* This decision had effectively been overturned by the United Kingdom courts in 1982 but had been endorsed by the Irish courts in the decision of *O'Sullivan v P Ltd*. The *O'Flynn* case now effectively marks the end of such a taxpayer-friendly approach in Ireland.

(a) Current cases

Following the successful outcome for Irish Revenue in the *O'Flynn* case, they have been actively issuing notices to taxpayers where they form the opinion that a transaction is a tax avoidance transaction. These cases have not yet been litigated through the Irish courts on the substantive point of whether or not they constitute tax avoidance. However, it is safe to say that even though it took 25 years for the first GAAR case to be heard in the Irish Supreme Court, we will not have to wait 25 years for the next case.

The High Court case of *Ronan McNamee v Revenue Commissioners*[32] involved a judicial review of the process Irish Revenue deployed in challenging transactions under the GAAR. The judge found in favour of Irish Revenue and found the Applicant was not entitled to any of the reliefs sought. The Applicant had sought an order quashing Irish Revenue's notice of opinion, issued by a nominated officer of Irish Revenue, that a number of transactions entered into by the Applicant and his wife together constituted a tax avoidance transaction for the purposes of the GAAR. The issuing of the

[31] 19 TC 490.
[32] 27 November 2012.

notice of opinion had the consequence of the withdrawal of a tax advantage of over EUR 6 million.

The judge found that the notice of opinion issued by the nominated officer of Irish Revenue concerning these series of transactions complied with the procedural requirements of section 811 of the TCA. He further found that there was no evidence that the officer who had formed the opinion was tainted by pre-judgment or bias and there was no breach of natural or constitutional justice.

(b) Key historical cases

The *O'Flynn* case focused on whether a claim for a particular tax relief should be denied by virtue of section 811 of the TCA, notwithstanding that the technical conditions for the relief itself were satisfied. Much of the case related to the second safe-harbour, and whether the claim for the tax relief in question was a 'misuse or abuse' of the tax relief.

The majority judgment in the Supreme Court indicated that this safe-harbour must be considered in light of the general purpose of section 811 of the TCA namely to reverse the *Duke of Westminster* case in Ireland. The Supreme Court offered two (somewhat informal) tests of whether section 811 of the TCA should deny a claim for a tax relief:

(i) was the claim a 'proper and intended use' of the relevant tax relief?
(ii) was the claim an 'appropriate use' of the relevant tax relief?

In ascertaining the 'intention' or 'appropriate use' of any particular tax relief, the Supreme Court indicated that this was to be derived from the legislative words used in their context ('deploying all the aids to construction which are available, in an attempt to understand what the Oireachtas intended.').

The Supreme Court gave examples of situations where section 811 of the TCA may not be applied:

(i) where the Irish parliament has not contemplated at all the scheme subsequently constructed;
(ii) where there was a gap that the Irish Parliament had neglected;
(iii) where an intended scheme was not foreseen;
(iv) where the tax relief is 'so technical and detailed so that no broad or general purpose can be detected'; and
(v) where a tax relief has its own explicit anti-avoidance provision.

In respect of the first three bullet points, the Supreme Court held that the courts would *'not [be] empowered to disallow a relief … since to do so would be to exceed the proper function of the courts in the constitutional scheme.'*

In respect of the last two bullet points, the Supreme Court held that *'there may be no room for the application of section [811] since it may not be possible to detect a purpose for the provision other than the basic one that the Oireachtas intended that any transaction which met requirements of the section should receive the relief.'*

To contrast these situations, the Supreme Court held that section 811 of the TCA should be applied where it could be said *'with some confidence'* that the result is *'not the sort of relief'* that the legislation intended to result.

The Supreme Court acknowledged that such an evaluation *'may be difficult and can create some uncertainty.'* However, that was not a reason *'to avoid the task.'* The Supreme Court held that *'the desire to provide certainty to those who wish to avoid a taxation regime which applies to others similarly situated to them, is something which ranks low in the objectives which statutory interpretation seeks to achieve.'* Certainty could be achieved, the Supreme Court observed, by paying tax.

To ascertain the 'purpose' of a tax relief, the Supreme Court was quite clear that it was not sufficient to simply consider the 'general purpose' of the tax relief provision. Instead, it was necessary to ascertain the purpose of the 'particular scheme'. In other words, the focus should not be on an attempt to define the overall parameters of tax relief in question (which could descend into 'rhetoric'), but should instead be on an attempt to conclude whether the transaction in question fell within the tax relief.

The Supreme Court held that *'the important guides'* in determining whether there was a *'misuse or abuse'* of a tax relief in the context of a particular transaction were the matters set out in section 811 of the TCA itself, namely:

(i) The form and substance of the transaction.
(ii) Whether the transaction was undertaken for the realisation of profit in the course of business activities carried out by any person.
(iii) Whether it was undertaken primarily for purposes other than to give rise to a tax advantage.

The Supreme Court emphasised that, in ascertaining whether a tax relief was being *'misused or abused',* Irish Revenue should have regard to all these matters to which attention is directed under section 811 of the TCA itself.

Nevertheless, the Supreme Court did also review some technical aspects of the tax relief in question in the *O'Flynn* case, namely:

(i) its interaction with company law;
(ii) its requirement for profits (as opposed to revenues);
(iii) its requirement for the company's capacity to declare a dividend; and
(iv) its silence on the ability to sell or transfer these tax-free reserves.

11. PENALTIES

The penalties provided for in general tax legislation and the Code of Practice for Revenue Audit outlined in section 6 above apply equally to tax avoidance transactions. However an additional 20 per cent surcharge can apply to tax avoidance transactions. Furthermore, the most serious tax offences can be punished by a fine or imprisonment or both (in addition to paying tax, interest and penalties).

(a) Legislative provisions

Section 811A of the TCA provides that, where the opinion of Irish Revenue that a transaction is a tax avoidance transaction (within the meaning of the GAAR) becomes final, interest and a 20 per cent surcharge will be payable on the tax that the taxpayer unsuccessfully attempted to avoid paying.

The section also provides that, by making a protective notification to Irish Revenue in respect of a transaction within 90 days of beginning a transaction, the taxpayer can, on a wholly non-prejudicial basis, obtain protection from the possibility of such interest or surcharge arising in the event of Irish Revenue successfully challenging the transaction. In addition, where a full protective notification has been made, the time period within which Irish Revenue must form an opinion that a transaction is a tax avoidance transaction under section 811 of the TCA is limited to a period of two years from the date of the notification. A notice of opinion under section 811 of the TCA can otherwise be made at any time.

Criminal proceedings can be initiated where serious tax evasion is suspected.[33] The types of offences that are most likely to be prosecuted include (i) deliberate omissions from tax returns; (ii) false claims for repayment; (iii) use of forged or falsified documents; (iv) facilitating fraudulent evasion of tax; (v) systematic schemes to evade tax; (vi) use of offshore bank accounts to evade tax; (vii) insidious schemes of tax evasion; (viii) failure (as distinct from minor delays) in remitting fiduciary taxes.

(b) Examples of penalties imposed

As part of any audit settlement Irish Revenue will insist that full tax and interest is paid. Tax geared penalties may be mitigated in accordance with the discussion at section 6 above. Although Irish Revenue publishes a list of tax defaulters on a quarterly basis, the settlement amount disclosed does not distinguish between tax, interest and penalties. Tax defaulters who make a qualifying disclosure are not published in the list of tax defaulters.

12. CURRENT TRENDS

12.1 National policy and law

Current Irish policy is to very firmly target and narrow the scope of aggressive tax planning and abusive tax avoidance. Irish Revenue have wide powers of investigation, a GAAR that is only recently being utilised to full effect, a broad based mandatory disclosure regime and a judiciary that are prepared to look at substance over form.

The reaction of the Revenue Chairman, Josephine Feehily, following the judgment in the *McNamee* Case is instructive: *'The judgment of the High Court, delivered this morning, is an important one in confirming the efficacy of Revenue's procedures around section 811. Challenging transactions which we believe have little or no commercial reality is an important part of our strategy. At the end of last year, 50 avoidance schemes were being challenged by Revenue. Aggressive tax planning and abusive avoidance schemes are very damaging to the Exchequer and to the fairness of the tax system. We will continue to challenge taxpayers, and the promoters/advisers who market these schemes, where we can, and will recommend legislative changes to the Minister for Finance where we consider that is the best course of action.'*

33 Section 1078 TCA; s. 531 TCA; s. 1056 TCA.

As part of Budget 2013, the Irish Department of Finance published a document entitled 'Ireland's International Tax Strategy'. Included within this tax strategy paper was a statement that *'Aggressive tax planning by companies is a major issue across the world and it needs to be addressed. Ireland is very much involved in the process of addressing the issue.'*

In May 2014 the Department of Finance launched a public consultation paper entitled 'OECD Base Erosion and Profit Shifting Project in an Irish Context'. This consultation paper was issued in the context of the on-going OECD BEPS process, as a basis for encouraging debate on the options for Ireland's tax system in responding to a changing international tax environment.

Recent domestic legislation enacted to target perceived aggressive tax planning included the introduction of a change to the corporate tax residency rule under Irish law, which essentially means that an Irish incorporated company would be tax resident in Ireland if it was not otherwise resident anywhere else. This was an effort to remove the so-called 'stateless companies' ie, Irish incorporated companies that were tax resident nowhere. It is important to note that domestic Irish legislation still permits Irish incorporated companies in certain circumstances to be tax resident in another jurisdiction (even a so-called tax haven) where they are managed and controlled in that jurisdiction.

12.2 Impact and role of the OECD and other international relations

As well as highlighting Ireland's domestic response to countering aggressive tax planning, the Tax Strategy Paper commits Ireland to the international effort. Ireland's activities in countering aggressive tax planning can be summarised as follows:

(a) Through the OECD

Ireland is an active participant in the OECD/G20 Base Erosion and Profit Shifting (BEPS) project.

From Ireland's perspective, the key purpose of the project is to better align the right to tax with real economic activity. Ireland already does this (profits charged in Ireland reflect substantive operations here), and in this regard Ireland is fully supportive of solutions that would extend the alignment of tax and real economic activity internationally. Ireland does view BEPS as a project to be addressed collectively and as such it requires a co-ordinated effort and should not necessarily require immediate unilateral action on the part of any particular country.

(b) Through the EU

On 30 June 2013 Ireland finished its seventh Presidency of the Council of the European Union. Ireland's Presidency coincided with tax policy issues taking centre stage in the international arena. Against this elevated profile for taxation, the Irish Presidency's plan to focus on tackling tax fraud and tax evasion was very much in line with international developments. At a practical level our Presidency prioritised work in the following areas: tackling tax fraud and tax evasion, achieving a mandate to negotiate with third countries on the Savings Taxation agreements, tackling hybrid mismatches and enhancing administrative cooperation on tax. In addition Ireland carried forward the work on the Financial Transaction Tax (FTT), Energy Tax Directive and the Common Consolidated Corporate Tax Base (CCCTB).

Contact details

GENERAL EDITOR

David W Chodikoff
Miller Thomson LLP
Scotia Plaza
40 King Street West
Suite 5800
Toronto, ON
M5H 3S1
Canada
T: +416 595 8500
F: +416 595 8695
E: dchodikoff@millerthomson.com
W: www.millerthomson.com

ALBANIA

Endri Mykaj & Sokol Nako
Wolf Theiss
Eurocol Business Center
Murat Toptani Street
4th Floor, 1001 Tirana
Albania
T: +355 4 227 4521
+ 355 4 2274521
F: +355 4 227 4521
+ 355 2 2274521
E: endri.mykaj@wolftheiss.com
sokol.nako@wolftheiss.com
W: www.wolftheiss.com

AUSTRALIA

Stewart Grieve & Reynah Tang
Corrs Chambers Westgarth
Level 36, Bourke Place
600 Bourke Street
Melbourne VIC 3000
Australia
T: +61 3 9672 3000
F: +61 3 9672 3010
E: stewart.grieve@corrs.com.au
reynah.tang@corrs.com.au
W: www.corrs.com.au

AUSTRIA

Dr Jürgen Brandstätter & Victoria Rosengren, LLM
BMA Brandstätter Rechtsanwälte GmbH
Wallnerstrasse 3
1010 Vienna
Austria
T: +43 1 535 16 30
F: +43 1 535 16 30 40
E: juergen.brandstaetter@bma-law.com
victoria.rosengren@bma-law.com
W: www.bma-law.com

BELGIUM

Natalie Reypens & Aldo Engels
Loyens & Loeff
Woluwe Atrium
Neerveldstraat 101–103
B-1200 Brussels
T: +32 2 743 43 43
F: +32 2 743 43 10
E: natalie.reypens@loyensloeff.com
aldo.engels@loyensloeff.com
W: www.loyensloeff.com

BRAZIL

Henrique Lopes
KLA–Koury Lopes Advogados
Av. Brigadeiro Faria Lima, 1355 18°
São Paulo SP 01452-919
T: + 55 11 3799 8100
F: + 55 11 3799 8200
E: hlopes@klalaw.com.br
W: www.klalaw.com.br

CANADA

David W Chodikoff & Laura Etherington
Miller Thomson LLP
Scotia Plaza
40 King Street West
Suite 5800
Toronto, ON
M5H 3S1
Canada
T: +416 595 8500
F: +416 595 8695
E: dchodikoff@millerthomson.com
letherington@millerthomson.com
W: www.millerthomson.com

CHINA
Tony Dong & Daisy Duan
King & Wood Mallesons
20th Floor, East Tower
World Financial Center
1 Dongsanhuan Zhonglu
Chaoyang District
Beijing 100020
P. R. China
T: +86 10 5878 5588
F: +86 10 5878 5599
E: tony.dong@cn.kwm.com
duantao@cn.kwm.com
W: www.kwm.com

CYPRUS
Dr Chrysthia N Papacleovoulou & Evi N Papacleovoulou
Law Chambers Nicos Papacleovoulou LLC
Alkiviades 3, Floor 1
Paphos 8011
Cyprus
T: +357 26933218/+26937674
F: +357 26 944129
E: chrysthia@papacleovoulou.com
n.papacleovoulou@cytanet.com.cy
W: www.papacleovoulou.com

FINLAND
Henri Becker, Tero Ahonen & Petteri Rapo
Alder & Sound
Mannerheimintie 16 A (5th floor)
00100 Helsinki
Finland
T: +358 10 219 3890
E: henri.becker@aldersound.fi
tero.ahonen@aldersound.fi
petteri.rapo@aldersound.fi
W: www.aldersound.fi

FRANCE
Jean-Marc Tirard
Tirard Naudin
9 rue Boissy d'Anglas
75008 Paris
France
T: +33 01 53 57 36 00
F: +33 01 47 23 63 31
E: tirard.naudin@online.fr
W: www.tirard-naudin.com

GERMANY
Dr Axel Bödefeld & Gunnar Knorr
Oppenhoff & Partner
Konrad-Adenauer-Ufer 23
50668 Cologne
Germany
T: +49 0221 2091 0
F: +49 0221 2091 333
E: axel.boedefeld@oppenhoff.eu
gunnar.knorr@oppenhoff.eu
W: www.oppenhoff.eu

GREECE
Aspasia Malliou & Ifigeneia Efthimiou
Potamitisvekris Law firm
9 Neofytou Vamva str. 10674
Athens
Greece
T: +30 210 3380000
F: +30 210 3380020
E: aspasia.malliou@potamitisvekris.com
ifigeneia.efthimiou@potamitisvekris.com
W: www.potamitisvekris.com

INDIA
Manoj K Singh
Singh & Associates, Advocates and Solicitors
N-30, Malviya Nagar
New Delhi – 110017
India
T: +91 11 46665000
F: +91 11 46665001
E: newdelhi@singhassociates.in
W: www.singhassociates.in

INDONESIA
Freddy Karyadi & Anastasia Irawati
ABNR – Ali Budiardjo, Nugroho, Reksodiputro
Graha CIMB Niaga
24th Floor
Jl. Jend. Sudirman Kav. 58
Jakarta 12190
T: +62 21 250 5125/5136

F: +62 21 250 5001/5121/5122/5392
E: fkaryadi@abnrlaw.com
airawati@abnrlaw.com
W: www.abnrlaw.com

IRELAND

Joe Duffy
Matheson
70 Sir John Rogerson's Quay
Dublin 2
Ireland
T: +353 1 232 2688
F: +353 1 232 3333
E: joseph.duffy@matheson.com
W: www.matheson.com

John Ryan
Matheson
200 Park Avenue
New York
NY 10016
T: +1 646 354 6583 (direct)
+1 646 354 6582
E: john.ryan@matheson.com
W: www.matheson.com

ISRAEL

Henriette Fuchs
Barnea & Co, Attorneys at Law
Life Plaza
6, Ha Choshlim Street
Herzliya Pituach 46724
Israel
T: +972 99 600 700
F: +972 99 516 002
E: hfuchs@barlaw.co.il
W: www.barlaw.co.il

ITALY

Massimo Antonini & Paolo Giacometti
Chiomenti Studio Legale
Via Verdi, 2
20121 Milano – Italy
T: +39 02 72157436
F: +39 02 72157227
E: massimo.antonini@chiomenti.net
paolo.giacometti@chiomenti.net
W: www.chiomenti.net

JAPAN

Kenji Hashidate
Hashidate Law Office
The Imperial Hotel Tower, 7th Floor
1-1, Uchisaiwai-cho 1-chome
Chiyoda-ku, Tokyo 100-0011
Japan
T: +81 3 3504 3800
F: +81 3 3504 1009
E: kenjihashidate@hashidatelaw.com
W: www.hashidatelaw.com

LUXEMBOURG

Raquel Guevara
MNKS
Vertigo Polaris Building
2-4 rue Eugène Ruppert (2nd floor)
L-2453 Luxembourg
T: +352 26 48 42 1
F: +352 26 48 42 35 00
E: guevara@mnks.com
W: www.mnks.com

MALAYSIA

S Saravana Kumar, Siti Fatimah Mohd Shahrom & Kho Chin Chau
Lee Hishammuddin Allen & Gledhill
Level 16 Menara Tokio Marine Life
189 Jalan Tun Razak
50400 Kuala Lumpur
Malaysia.
T: +603 2161 2330
F: +603 2161 3933
E: sks@lh-ag.com
sfs@lh-ag.com
kcc@lh-ag.com
W: www.lh-ag.com

MEXICO

Mario Barrera- Vázquez, ESQ.
Basham, Ringe y Correa, S.C.
Paseo de los Tamarindos<br
No. 400-A, 9 Floor
Col. Bosques de las Lomas
05120 Mexico City
Mexico
T: +52 55 52 61 05 07
F: +52 55 52 61 04 96
E: mbarrera@basham.com.mx
W: www.basham.com.mx

NETHERLANDS

Lucia Sahin
Loyens & Loeff N.V.
Blaak 31
3011 GA Rotterdam
The Netherlands
T: +31 10 224 63 01
F: +31 10 224 64 56
E: lucia.sahin@loyensloeff.com
W: www.loyensloeff.com

NEW ZEALAND

Leslie Prescott-Haar
TP Equilibrium AustralAsia
3/150 Moewai Road
Whitianga 3591
New Zealand
T: +64 274 516 646
E: leslie.prescotthaar@duffandphelps.com
W: www.duffandphelps.com

Jarrod Walker & Hugh Magee
Bell Gully
Vero Centre
48 Shortland Street
PO Box 4199
Auckland 1140
T: +64 9 916 8800
F: +64 9 916 8801
E: Jarrod.Walker@bellgully.com
Hugh.Magee@bellgully.com
W: www.bellgully.com

NIGERIA

Oluwatoyin Bashorun
Churchfields Solicitors
Suite 201-203, West Wing City Hall
23/25 Catholic Mission
Lagos Island
Lagos
Nigeria
T: +080 2328 7054
F: +01 8042134
E: churchfields_solicitors@yahoo.co.uk
tbashorun@churchfields-solicitors.com
W: www.churchfields-solicitors.com

NORWAY

Cecilie Amdahl
Advokatfirmaet Schjødt AS
Ruseløkkveien 14
P.O.Box 2444 Solli
NO-0201 Oslo
Norway
T: +47 22 01 88 00
F: +47 22 83 17 12
E: ceam@schjodt.no
W: www.schjodt.com

RUSSIA

Maxim Rovinskiy & Ekaterina Boldinova
YUST Law Firm
43, Sivtsev Vrazhek Lane
119002 Moscow
Russia
T: +7 495 795 0845
+7 495 795 3272
+7 495 795 0842
F: +7 499 241 1948
E: rovinskiy@yust.ru
boldinova@yust.ru
W: www.yust.ru

SERBIA

Anastasia Sagianni
Eurofast
31 Beogradska
Belgrade 11000
Serbia
T: +381 11 3241 484
F: +381 11 3038 848
E: anastasia.sagianni@eurofast.eu
info@eurofast.eu
W: www.eurofast.eu/global

SPAIN

José Oltra
Swan Partners
Grabador Esteve Street 15 – 2ª
46004 Valencia
Spain
T: +34 96 334 89 83
E: jose.oltra@swanpartners.es
W: www.swanpartners.es

SWITZERLAND

Marco Greter, Mathias Häni &
Fabian Streule
ADB Altorfer Duss & Beilstein AG
Walchestrasse 15
CH-8006 Zurich
Switzerland
T: +41 44 267 63 00
F: +41 44 267 63 90
E: marco.greter@adbtax.ch
mathias.haeni@adbtax.ch
fabian.streule@adbtax.ch
W: www.adbtax.ch

TURKEY

Dr Z Ertunç Şirin, MA & E Benan
Arseven
Moroğlu Arseven
Odakule Kat:12
İstiklal Caddesi No:142
Beyoğlu 34430
İstanbul
Turkey
T: +90 212 377 47 00
F: +90 212 377 47 99
E: zesirin@morogluarseven.com
barseven@morogluarseven.com
W: www.morogluarseven.com

UGANDA

Cephas K Birungyi
Birungyi, Barata & Associates
3 Portal Avenue
3rd Floor Crusader House
P.O. Box 21086
Kampala
Uganda
T: +256 414 348 669
F: +256 414 230 026
E: cbirungyi@taxconsultants.co.ug
W: www.taxconsultants.co.ug

UNITED KINGDOM

Richard Palmer & Nicholas Gardner
Ashurst
Broadwalk House
5 Appold Street
London
EC2A 2HA
United Kingdom
T: +44 020 7638 1111
F: +44 020 7638 1112
E: nicholas.gardner@ashurst.com
richard.palmer@ashurst.com
W: www.ashurst.com

UNITED STATES OF AMERICA

L Frank Cordero, Osmel L Cuan,
Michael J Bowen & Peter O Larsen
Akerman LLP
One Southeast Third Avenue
25th Floor
Miami
FL 33131
USA
T: +1 305 374 5600
F: +1 305 374 5095
E: frank.cordero@akerman.com
osmel.cuan@akerman.com
michael.bowen@akerman.com
peter.larsen@akerman.com
W: www.akerman.com