IRELAND

Joe Duffy, John Ryan and Kathryn Stapleton, MATHESON

TRANSFER PRICING: GENERAL OVERVIEW

1. WHAT ARE THE MAIN CHARACTERISTICS OF TRANSFER PRICING LAW AND POLICY IN YOUR JURISDICTION?

Ireland introduced formal transfer pricing legislation for the first time in 2010. The Finance Act 2010 introduced a new transfer pricing regime in 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.

Broadly, the transfer pricing rules require domestic and international transactions between associated persons to be entered into at arm's length. Where an arrangement between associated entities is made otherwise than at arm's length, an adjustment can be made to the Irish company profits. An adjustment is only made where income is understated or expenses are overstated.

The transfer pricing rules only apply to trading activities. This is a key characteristic of the transfer pricing rules that is quite unusual. The meaning of "trading" in this context is discussed under *Question 3*.

The transfer pricing legislation specifically provides that the transfer pricing rules must be construed in accordance with the Organisation for Economic Co-operation and Development (OECD) Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010.

2. WHAT HAVE BEEN THE MAIN DEVELOPMENTS OF SIGNIFICANCE FOR TRANSFER PRICING LAW AND PRACTICE IN YOUR JURISDICTION IN THE PAST 12 MONTHS?

The Organisation for Economic Co-operation and Development (OECD) final reports on base erosion and profit shifting (BEPS) are having a significant impact on international tax policy in Ireland. A formal advance pricing agreement (APA) programme has been introduced by the Irish Revenue Commissioners (Irish Revenue) to enhance certainty and transparency for taxpayers with multi-jurisdictional operations. In addition, the legislative framework required to implement country-by-country reporting has been established and enacted, with effect from 1 January 2016. The updated OECD guidelines on transfer pricing have also been incorporated into Irish legislation. In June 2016, the Irish Revenue released guidance containing frequently asked questions and answers in connection with the interpretation of legislation and regulations on country-by-country reporting in Ireland. This guidance has been updated periodically, most recently in December 2016.

In July 2016, Ireland launched a formal regime in respect of bilateral and multilateral APAs. In the past, Ireland facilitated bilateral and multilateral APAs without having a formal regime in place. It will now be possible to initiate these agreements with the Irish tax authorities. However, entry into APAs is confined to complex transfer pricing transactions that could give rise to double taxation issues.

The Irish Revenue has confirmed that Ireland's spontaneous exchange of information regime will apply retroactively to certain tax rulings issued since 1 January 2010. The regime is based on a combination of:

- The framework proposed by the OECD under BEPS Action 5.
- Directive 2015/2376/EU amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation.

The regime typically applies to rulings relating to transactions with a cross-border impact. Exchange of information applies to relevant rulings issued or amended on or after 1 January 2010 under the OECD framework, and 1 January 2012 under EU rules, and which were still in effect on 1 January 2014. All relevant rulings issued or amended by the Irish Revenue since 1 January 2014 will be subject to exchange of information, regardless of whether they remain in effect.

TRANSFER PRICING LEGISLATION

FEDERAL OR NATIONAL LEGISLATION

3. WHAT IS THE MAIN FEDERAL (NATIONAL) LEGISLATION REGULATING TRANSFER PRICING IN YOUR JURISDICTION?

Part 35A of the Taxes Consolidation Act 1997 (TCA) sets out the transfer pricing regime. The following paragraphs outline the:

- Circumstances in which the transfer pricing rules apply.
- Arrangements that are specifically excluded from the scope of the transfer pricing rules.
- Consequences of the application of the transfer pricing rules.

Scope of application of the transfer pricing rules

The transfer pricing rules apply if all the following conditions are met:

- 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)".
- At the time of the supply and acquisition, the supplier and acquirer are associated. Two persons are associated if:
  - 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; or
  - the first person is participating in the management, control or capital of the other person, where that other person is a company controlled by the first person.
- The profits, gains or losses arising from the relevant activities are in respect of trading activities. "Trading" is defined in Irish legislation as including "every trade, manufacture, adventure or concern in the nature of a trade".

There is no definition of "trade" in Irish tax legislation. Generally, to be trading, the Irish company must:

- Be engaged in the key profit-making commercial activity.
- Have persons in Ireland with the requisite skills and expertise to perform that activity.

Certain activities can 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 the Irish courts. The badges of trade, and matters to be considered in determining whether a particular activity constitutes a trade, include the following:

- Subject matter.
- Length of ownership of the relevant subject matter.
- Frequency of transactions.
- Supplementary work done on the relevant subject matter.
- Circumstances of sale.
- Motive for transaction.

These issues have been considered extensively in the courts. In *IRC v Fraser (24 TC 498)*, the taxpayer had 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 (40 TC 585)*, over the course of four years, the taxpayer had set up and disposed of 29 driving schools and was held to be trading. In *IRC v Livingston (11 TC 538)*, the taxpayers had 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 had been undertaken with a view to a subsequent disposal. In the UK High Court case of *Noddy Subsidiary Rights Company Limited v CIR (43 TC 458)*, a company had been 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 in 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.

The Irish Revenue issued a guidance note on the classification of activities as trading, which provides that the Revenue may be prepared to express a view as to whether a particular transaction or operation amounts to a trade or qualifies for the 12.5% corporation tax rate. In arriving at a decision, the Irish Revenue endorses the *Noddy* case and has stated that the key considerations are whether:

- There is any commercial rationale for the type of transaction proposed.
- There is any real value added in Ireland.
- There are employees in Ireland with sufficient levels of skills to indicate that the company is actively carrying on a trade.

The Irish Revenue also published details of cases submitted, and opinions issued, in the period from December 2002 to December 2015 on the classification of activities as trading activities. The Irish Revenue stated that opinions on the classification of activities as trading are made by 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.

Transactions undertaken otherwise than 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 at arm's length, and are therefore deemed to be for a consideration equal to the market value.

Exclusions from the transfer pricing rules

The transfer pricing rules are excluded in any of the following circumstances:

- The arrangement is concluded within a small or medium-sized enterprise. A small or medium-sized enterprise means an enterprise that falls within the category of micro, small and medium-sized enterprise as defined in the Annex to the European Commission Recommendation concerning the definition of micro, small and medium-sized enterprises *(OJ 2003 L124/36)* (broadly, less than 250 employees and either a turnover of less than EUR50 million or assets of less than EUR43 million on a group basis).
- The arrangement was agreed before 1 July 2010. The transfer pricing legislation includes a grandfathering clause, 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, but the arrangement itself remains in place, as to whether the arrangement remains grandfathered. The view of the Irish Revenue, although not published officially, is that to remain grandfathered the arrangement existing at 1 July 2010 should be able to "deliver the terms" of the ongoing arrangement.
- The arrangement relates to a section 110 securitisation special purpose vehicle. Section 110 of the Taxes Consolidation Act 1997 requires transactions entered into by certain qualifying companies to be by way of bargain at arm's length, except in respect of profit participating loan notes issued by a qualifying company.

Consequences of application of the transfer pricing rules

The consequences of the application of the transfer pricing rules are as follows:

- Where an arrangement between associated entities is made otherwise than at arm's length, an adjustment can be made where the Irish company has understated income or overstated expenses. The arm's length amount is defined as the amount of the consideration that independent parties would have agreed in relation to that arrangement.
- The relevant person to which the transfer pricing rules apply must have records available as may be reasonably required for the purpose of determining whether the trading profits have been calculated on an arm's length basis.

STATE OR LOCAL TRANSFER PRICING LEGISLATION

4. WHAT ADDITIONAL REGIONAL (LOCAL STATE) LEGISLATION AND REVENUE AUTHORITIES ARE RELEVANT TO TRANSFER PRICING IN YOUR JURISDICTION?

Ireland does not have applicable state or local transfer pricing legislation.

INTERNATIONAL TRANSFER PRICING TREATIES AND AGREEMENTS

5. WHAT ARE THE MAIN INTERNATIONAL TREATIES AND AGREEMENTS THAT APPLY IN YOUR JURISDICTION?

The primary sources of international law that have an impact on 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. The transfer pricing rules must be construed in accordance with the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010.

6. WHAT IMPACT DO INTERNATIONAL TREATIES AND AGREEMENTS HAVE IN YOUR JURISDICTION?

From a transfer pricing perspective, double tax treaties are typically most relevant where there is either:

- An adjustment of profits in accordance with Article 9 of the OECD Model Tax Convention on Income and on Capital (OECD Model Convention).
- An allocation of profits to a permanent establishment in accordance with Article 7 of the OECD Model Convention.

Where there is a dispute about the profits allocable to a taxpayer, 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 exchange of information provisions. This is particularly important in the context of transfer pricing audits. The Irish Revenue has wide information-gathering powers, and this information can be provided to tax treaty partner countries.

TRANSFER PRICING POLICY

7. WHAT IS THE OVERALL NATIONAL TRANSFER PRICING POLICY IN YOUR JURISDICTION?

Ireland's overarching policy with respect to transfer pricing is that it must be construed in a manner that is consistent with the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010. The adoption of a principled approach has been emphasised in this regard.

In November 2012, in the context of a collaborative approach to transfer pricing, the Irish Revenue announced that transfer pricing compliance reviews (TPCRs) would form the cornerstone of monitoring compliance with the transfer pricing rules. TPCRs involve taxpayers being selected on a risk assessment basis to conduct a self-review on their transfer pricing policy for a specified period. Taxpayers have three months to conduct the self-review and to provide a report to the Irish Revenue. If the Irish Revenue is satisfied with the results of the TPCR, a letter confirming that it has no further enquiries will be issued, giving taxpayers comfort that their transfer pricing policy for that period has been accepted. Where the Irish Revenue is not satisfied with the level of information received, or with the transfer pricing policy, TPCRs can be escalated to more formal audits (with the related risk of penalties). A transfer pricing audit is conducted in the same manner as a regular corporation tax audit.

However, as experience of transfer pricing matters has grown within the Irish Revenue, more transfer pricing audits are in progress, particularly in respect of transactions that are identified as higher-risk. In recent years, the Irish Revenue has increased resources within its internal transfer pricing function. In particular, the transfer pricing unit within the Irish Revenue's Large Cases Division has been expanded to enhance the Irish Revenue's audit functionality in a transfer pricing context. It is likely that the Irish Revenue's increased audit activity will result in greater instances of double taxation in practice, leading to an increased need for mutual agreement procedures under the relevant double tax treaty.

8. WHAT ARE THE MAIN TRANSFER PRICING METHODOLOGIES THAT ARE USED TO DETERMINE AN ARM'S LENGTH PRICE IN YOUR JURISDICTION?

The Irish transfer pricing rules do not specify acceptable or preferred transfer pricing methods. However, the legislation requires the transfer pricing rules to be construed in such as way so as to ensure, as far as practicable, consistency with the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010 (OECD Transfer Pricing Guidelines).

Therefore, any transfer pricing method that is selected and applied in accordance with the OECD Transfer Pricing Guidelines should be acceptable from an Irish transfer pricing perspective. Under the OECD Transfer Pricing Guidelines, the taxpayer should select the methodology that is most appropriate for the particular transaction.

9. TO WHAT EXTENT, IF ANY, DOES YOUR JURISDICTION FOLLOW THE OECD TRANSFER PRICING GUIDELINES?

The transfer pricing legislation specifically provides that the transfer pricing rules must be construed in accordance with "transfer pricing guidelines". The "transfer pricing guidelines" are defined quite broadly and include 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 Irish transfer pricing rules must be construed in accordance with all relevant current and future OECD guidelines.
- Transfer pricing discussions with the Irish Revenue are typically framed and discussed in the context of OECD guidelines.

The updated OECD guidelines contained in the final BEPS report on Actions 8 to 10 have not been implemented into Irish domestic law to date. Therefore, the updated guidelines are technically not applicable to wholly domestic disputes or arrangements involving non-treaty partner countries. However, the updated guidelines will apply to pricing disputes that arise under any of Ireland's double tax treaties in accordance with general OECD principles. It is expected that the updated OECD guidelines will be incorporated into Irish law in the near future.

10. IS IT POSSIBLE TO OBTAIN ANY CLEARANCES OR ADVANCE PRICING AGREEMENTS FROM THE REVENUE AUTHORITIES IN RESPECT OF TRANSACTIONS?

Ireland recently introduced a formal bilateral advance pricing agreement (APA) programme, took effect on 1 July 2016. The APA programme replaces Irish Revenue's ad hoc approach to agreeing APAs and provides for the initiation of APAs by taxpayers. Ireland actively participates in bilateral APAs, but will not generally conclude unilateral APAs. Where the relevant issues involve more than two tax jurisdictions, the Irish Revenue will consider entering into a series of bilateral APAs to deal with multilateral situations.

A company's access to the APA programme is subject to the terms of the mutual agreement procedure provision of the relevant double tax treaty. An application for an APA can be made by:

- A company that is tax resident in Ireland.
- A permanent establishment of a non-resident company.

The Irish Revenue adheres to the detailed guidelines for concluding APAs that are contained in "Annex to Chapter IV: Advance Pricing Arrangements" of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2010. All bilateral APAs are negotiated on the basis of identifying an arm's-length remuneration for the transactions covered by the APA. The transfer pricing method applied will be one of the methodologies contained in the OECD Transfer Pricing Guidelines.

In addition, when negotiating a bilateral APA with an EU member state, the Irish Revenue will adhere to the best practices for the conduct of APA procedures that are set out in the Guidelines for Advance Pricing Agreements within the EU, which have been published by the EU Joint Transfer Pricing Forum.

11. WHERE THE REVENUE AUTHORITIES MAKE A TRANSFER PRICING ADJUSTMENT, WHAT IS THE EFFECT OF THAT ADJUSTMENT ON THE OTHER PARTY TO THE TRANSACTION?

In circumstances where the Irish Revenue makes a transfer pricing adjustment, there is no automatic direct effect on the other party to the transaction. However, all double tax treaties concluded by Ireland currently contain a mutual agreement procedure article. The Irish Revenue is willing to support requests for double taxation relief on application by Irish resident taxpayers, provided that the facts and circumstances of each case fall within the provisions of the relevant double tax treaty.

12. WHAT ARE THE REPORTING AND OTHER ADMINISTRATIVE OBLIGATIONS THAT APPLY TO HELP THE AUTHORITIES EVALUATE TRANSFER PRICES?

Taxpayers are not required to submit transfer pricing documentation for evaluation to the Irish Revenue, unless requested to do so. However, a taxpayer must retain and have available for inspection sufficient documentation and records to demonstrate compliance with the transfer pricing rules. The Irish Revenue has provided some guidance on documentation requirements in Tax Briefing 07/2010.

Transfer pricing documentation must be prepared in a timely manner and must demonstrate that the taxpayer's relevant income has been calculated in accordance with the transfer pricing rules. The records must be retained for a period of at least six years after the completion of the relevant transaction to which they relate.

A taxpayer who fails to submit documentation when requested by the Irish Revenue may be liable to a penalty. The Irish Revenue can apply to the High Court of Ireland for a court order to compel a taxpayer to submit records or documentation.

TRANSFER PRICING COURTS AND DISPUTE RESOLUTION

NATIONAL COURTS AND TRANSFER PRICING DISPUTE RESOLUTION

13. WHAT ARE THE RELEVANT NATIONAL COURTS AND WHAT DISPUTE RESOLUTION MECHANISMS EXIST FOR TRANSFER PRICING ISSUES IN YOUR JURISDICTION?

The Irish Revenue generally adopts a pragmatic approach to resolving transfer pricing disputes, and a taxpayer can engage in discussion and negotiation with the Irish Revenue throughout the course of an audit and appeals process. Once an assessment is raised, the taxpayer must accept the assessment or appeal within 30 days.

A taxpayer can appeal a transfer pricing assessment to the Tax Appeals Commission at first instance. The decision of an Appeal Commissioner can be appealed on a point of law to the High Court and the Supreme Court. Procedural defects in the Irish Revenue's conduct can be challenged by way of judicial review.

INTERNATIONAL COURTS AND TRANSFER PRICING DISPUTE RESOLUTION

14. WHAT INTERNATIONAL DISPUTE RESOLUTION METHODS ARE AVAILABLE IN YOUR JURISDICTION, AND WHICH ARE PREFERRED FOR TRANSFER PRICING ISSUES?

International transfer pricing matters (for example, seeking correlative relief in Ireland for transfer pricing adjustment made in another jurisdiction) can be resolved unilaterally, through the mutual agreement procedure under the relevant double tax treaty or under the European Arbitration Convention.

Transfer pricing matters can be agreed in advance by way of bilateral advance pricing agreements (APAs). Irish Revenue does not provide unilateral APAs. See *Question 10*.

Unilateral relief

Double tax treaties are typically most relevant where there is either:

- An adjustment of profits in accordance with Article 9 of the OECD Model Tax Convention on Income and on Capital (OECD Model Convention).
- An allocation of profits to a permanent establishment in accordance with Article 7 of the OECD Model Convention.

Irish Revenue may accept a transfer pricing adjustment under Article 9(2) of the OECD Model Convention 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 these double tax treaties. This is because Irish domestic law provides that a corresponding adjustment can only be made in instances where the double tax treaty provides for such adjustment. However, although not legally obliged to allow a corresponding adjustment where there is no equivalent to Article 9(2), the Irish Revenue generally allows for relief from double taxation on the basis of a claim under the MAP article of the relevant double tax treaty or the EU Arbitration Convention.

MAP

There is no formal procedure for undertaking a MAP under Irish law. However, the MAP request must:

- Quote the legal basis for the MAP (that is, the relevant article in Ireland's double tax treaties or the EU Arbitration Convention).
- Explain why a MAP is considered necessary.
- Explain the issues involved (attaching relevant background documentation).
- Set out what the requester considers to be the correct outcome (attaching any documents and case law supporting the requester's view).

Additionally, if the MAP request is made to more than one competent authority, the Irish competent authority should receive the same information as the other competent authority(ies).

EU Arbitration Convention

Typically, the respective competent authorities have no obligation to reach a binding decision under the MAP article of a double tax treaty. They are typically only required to endeavour to resolve the case and find a solution. Therefore, binding arbitration procedures are useful to obtain a final solution where the MAP process has proved unsuccessful.

The EU Arbitration Convention 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 (that is, transfer pricing adjustments).

A taxpayer that believes that there is double taxation as a result of a transfer pricing adjustment must present a claim to the competent authority of the country in which it is resident (for example, Ireland) within three years of the transfer pricing adjustment. The Irish Revenue will be obliged to attempt to resolve a claim by mutual agreement with the competent authority of the other EU member state if it both:

- Considers that the claim is well founded.
- Cannot solve the issue unilaterally.

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 arbitration commission must reach a decision within a six-month period. However, this decision is not binding on the parties involved. The EU 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.

TRANSFER PRICING CASE LAW

15. WHAT ARE THE MOST SIGNIFICANT CASE LAW DEVELOPMENTS ON TRANSFER PRICING IN YOUR JURISDICTION?

As Ireland has only recently introduced transfer pricing rules, there are no litigated Irish transfer pricing cases. Ireland introduced transfer pricing legislation with effect from accounting periods commencing on or after 1 January 2011. However, *Belville Holdings v Cronin (III ITR 340)*, 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 that 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 that brings the transaction within the realm of a bona fide transaction in the ordinary course of business. However, the High 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 therefore not certain that Belville requires an arm's length charge.

TRANSFER PRICING ADJUSTMENTS

ADJUSTMENTS AND PENALTIES

16. WHERE THE REVENUE AUTHORITIES MAKE AN ADJUSTMENT OF TRANSFER PRICES FOR TAX PURPOSES, CAN ANY OTHER PENALTIES ALSO BE IMPOSED IN ADDITION TO THAT ADJUSTMENT?

The Irish tax legislation does not provide for specific penalties in transfer pricing and double taxation cases. In the absence of specific penalties, the Irish tax authorities have indicated that the general corporate tax penalty provisions and the Irish Tax Authority's Code of Practice for Tax Audits will apply to assessments raised due to transfer pricing adjustments.

The amount of a penalty due is generally calculated by the Irish Revenue auditor, agreed with the taxpayer and paid. Where there is no agreement between the 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 Taxes Consolidation Act 1997 (TCA) and can vary depending on:

- The category of default giving rise to the penalty.
- Whether the taxpayer has made voluntary qualifying disclosure of the underpayment of tax.
- Whether the taxpayer co-operates during the course of the audit.

The relevant categories of default are deliberate behaviour and careless behaviour (with significant consequences or without significant consequences).

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 that are consistent with intent.
- A breach that cannot be explained solely by carelessness.

For deliberate behaviour penalties to apply, the auditor must therefore be satisfied that either:

- The facts of the case are consistent with intent to default.
- 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.

Careless behaviour penalties

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

"Carelessly" is defined as the "failure to take reasonable care" *(TCA)*. 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.

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

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.

"Significant consequences" is not defined in the TCA, but is used to describe the statutory penalty applicable where the tax underpaid exceeds 15% of the tax correctly payable. The 15% test must be applied separately to each type of tax and period in respect of which a return or statement of liability must 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% 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.

TRANSFER PRICING DEVELOPMENT AND REFORM

17. ARE THERE ANY CURRENT TRENDS, DEVELOPMENTS OR REFORM PROPOSALS THAT HAVE OR WILL AFFECT THE AREA OF TRANSFER PRICING IN YOUR JURISDICTION?

In anticipation of an increased number of international transfer pricing disputes and in light of the introduction of the formal advance pricing agreement programme (*see Question 10*), the Irish Revenue has recently devoted significant additional resources to its international transfer pricing and competent authority teams.

Ireland is also engaged in the development of the multilateral instrument under Action 15 of the OECD Base Erosion and Profit Shifting (BEPS) project, and is expected to sign the multilateral instrument during the course of 2017. As part of this process, Ireland has committed to introducing mandatory binding arbitration as a means of resolving treaty disputes.

The updated OECD guidelines contained in the final BEPS report on Actions 8 to 10 have not been implemented into Irish domestic law to date. Therefore, the updated guidelines are technically not applicable to wholly domestic disputes or arrangements involving non-treaty partner countries. However, the updated guidelines will apply to pricing disputes that arise under any of Ireland's double tax treaties in accordance with general OECD principles. It is expected that the updated OECD guidelines will be incorporated into Irish law in the near future.

TAX AVOIDANCE: GENERAL OVERVIEW

18. WHAT HAVE BEEN THE MAIN NATIONAL AND INTERNATIONAL TRENDS AFFECTING TAX ENFORCEMENT AND ANTI-AVOIDANCE PRACTICE IN YOUR JURISDICTION IN THE PAST 12 MONTHS?

The current Irish policy is to very firmly target and narrow the scope of aggressive tax planning and abusive tax avoidance through:

- The Irish Revenue's wide powers of investigation.
- A general anti-avoidance rule (GAAR) (*see Questions 20 and 22*).
- A broad based mandatory disclosure regime.
- A judiciary that is prepared to look at substance over form.

The Tax Appeals Commission (TAC) was recently introduced in Ireland. The TAC is an independent statutory body that is responsible for hearing, determining and disposing of appeals against assessments and decisions of the Irish Revenue concerning taxes and duties in accordance with relevant legislation. This includes appeals against determinations made regarding the applicability of the GAAR to a particular transaction or series of transactions.

19. HOW DOES YOUR JURISDICTION MAKE THE DISTINCTION BETWEEN ABUSIVE TAX AVOIDANCE AND LEGITIMATE TAX PLANNING?

The scope of acceptable tax planning in Ireland has narrowed over the last years, in particular since the Irish Supreme Court held that the Irish GAAR should be broadly interpreted (*O'Flynn Construction Limited v Revenue Commissioners (14 December 2011)*).

20. DO THE REVENUE AUTHORITIES IN YOUR JURISDICTION OFFER ANY GUIDANCE ON THE DISTINCTION BETWEEN LEGITIMATE TAX PLANNING MECHANISMS AND ABUSIVE OR AGGRESSIVE TAX AVOIDANCE?

There is no comprehensive list of transactions that Irish Revenue considers to be abusive. However in recent years, a mandatory disclosure regime was introduced for certain transactions. The Irish Revenue emphasises in published guidance notes that a transaction falling within the mandatory disclosure regime does not necessarily falls foul of the GAAR. However, the types of transaction that are subject to mandatory disclosure are indicative of the transactions that Irish Revenue regards as undesirable, and may fall foul 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 falls within one of the following descriptions:

- There is a desire to keep the scheme confidential from other promoters or from the Irish Revenue.
- 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.
- The scheme is a standardised tax product that does not require tailoring to the client's specific circumstances to any material extent.
- 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.
- A transaction structured so as to create a loss buying scheme for corporates.
- 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 (for example, retirement benefit schemes).
- 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 (for example, share ownership trusts).
- Schemes that convert income (taxable at a higher rate) into a gift (taxable at a lower rate).

The Irish Revenue does 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.

TAX ANTI-AVOIDANCE PROVISIONS

21. CAN YOU IDENTIFY ANY DIRECT OR INDIRECT IMPACT IN YOUR JURISDICTION OF THE OECD OR OTHER RECENT INTERNATIONAL INITIATIVES TO COMBAT ABUSIVE TAX AVOIDANCE?

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

Directive 2016/1164/EU laying down rules against tax avoidance practices that directly affect the functioning of the internal market (Anti-Tax Avoidance Directive) includes a GAAR that targets "non-genuine" arrangements to the extent that they are not entered for valid commercial reasons that reflect economic reality. Although Irish tax law already contains a GAAR, it is unclear whether the existing Irish GAAR will be regarded as adequate implementation of the Anti-Tax Avoidance Directive, or if a new GAAR will be required. A consultation will be held in 2017 to make a determination on this point.

22. DOES YOUR JURISDICTION HAVE GAAR DESIGNED TO PREVENT OR REDUCE ABUSIVE TAX AVOIDANCE?

Sections 811 and 811C of the Taxes Consolidation Act 1997 (TCA) contains Ireland's general anti-avoidance rule (GAAR) (section 811 applies to transactions made on or before 23 October 2014 and section 811C applies to transactions after that date). The GAAR is intended to defeat the effect of transactions that 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.

The GAAR applies where the Irish Revenue forms the opinion that a transaction is a "tax avoidance transaction". A tax avoidance transaction is a transaction that both:

- Gives rise to a tax advantage.
- 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, the Irish Revenue must 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 provide that a transaction is not a tax avoidance transaction where it was undertaken with a view to either:

- The realisation of profits in the course of the business, and not primarily to give rise to a tax advantage.
- Obtain the benefit of a relief, allowance or abatement, 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, the Irish Revenue can have regard to the substance of a transaction, and of related transactions, so as to go beyond the mere form of the transaction.

The Supreme Court observed in the O'Flynn case that the test to determine whether a transaction is a tax avoidance transaction 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".

23. WHAT ARE THE LEGISLATIVE PROVISIONS THAT ARE DESIGNED TO REINFORCE GAAR AND ANY OTHER ABUSIVE TAX AVOIDANCE PROVISIONS?

See *Question 20* for details regarding Ireland's mandatory disclosure regime.

24. IDENTIFY AND DISCUSS ANY CASE LAW OF INTEREST CONCERNING GAAR AND ANY OTHER CASES DEALING WITH ABUSIVE TAX AVOIDANCE IN YOUR JURISDICTION.

Current case law relevant to abusive tax avoidance

The most recent Irish case that considered the substance of Ireland's general anti-avoidance rule (GAAR) was the *O'Flynn* case in 2011 (*see Question 23*). However, a recent Supreme Court decision has addressed the procedural elements of this provision.

The case of *Revenue Commissioners v Droog [2016] IESC 55* was decided in October 2016. The taxpayer in the case, Mr Droog, had filed his income tax return for the tax year 1996/1997 on 30 January 1998. He was a member of a partnership, which was involved in the acquisition, distribution and licensing of films. In his return, Mr Droog claimed loss relief in the amount of GB£50,046 in respect of partnership losses. The ability to claim loss relief was curtailed under the Finance Act 1998 through amendments to tax legislation, limiting the relief to active partners. In 2007, the Irish Revenue issued a notice of opinion under section 811 of the Taxes Consolidation Act 1997 (TCA), asserting that the transaction was undertaken for the purposes of tax avoidance. Droog appealed the notice.

The Supreme Court held that the issuance of the notice of opinion was out of time. It observed that the Irish tax authorities had a four-year time limit in which to issue this notice of opinion, and there was nothing in section 811 of the TCA that would override this time limit. In particular, the Supreme Court stated that where a taxpayer had made a "full and true" disclosure of all relevant facts, the legislature must have considered that it would be unfair to allow the Irish Revenue to reopen the amount of tax due after the four-year period.

Historic case law relevant to abusive tax avoidance

The *O'Flynn* case focused on whether a claim for a particular tax relief should be denied under 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 of 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 (that is, the principle that a taxpayer is entitled to arrange its affairs so as to minimise tax) (see *Inland Revenue Commissioners v Duke of Westminster 1936 A.C. 1*). The Supreme Court offered two (somewhat informal) tests of whether section 811 should deny a claim for a tax relief:

- Was the claim a "proper and intended use" of the relevant tax relief?
- 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 (that is, the Irish Parliament) intended").

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

- Where the Irish Parliament has not contemplated at all the scheme subsequently constructed.
- Where there was a gap that the Irish Parliament had neglected.
- Where an intended scheme was not foreseen.
- Where the tax relief is "so technical and detailed so that no broad or general purpose can be detected".
- 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". The Supreme Court observed that certainty could be achieved 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 the tax relief in question, 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:

- The form and substance of the transaction.
- Whether the transaction was undertaken for the realisation of profit in the course of business activities carried out by any person.
- 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, the Irish Revenue should have regard to all these matters to which attention is directed under section 811 of the TCA.

However, in the *O'Flynn* case the Supreme Court also reviewed some technical aspects of the tax relief in question, namely its:

- Interaction with company law.
- Requirement for profits (as opposed to revenues).
- Requirement for the company's capacity to declare a dividend.
- Silence on the ability to sell or transfer these tax-free reserves.

Following the successful outcome for the Irish Revenue in the *O'Flynn* case, the Irish Revenue has been actively issuing notices to taxpayers where it forms 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 although it took 25 years for the first GAAR case to be heard in the Irish Supreme Court, it is unlikely that it will take that long for the next case to be heard by the Court.

The High Court case of *Ronan McNamee v Revenue Commissioners [2012] IEHC 500* involved a judicial review of the process the Irish Revenue deployed in challenging transactions under the GAAR. The judge found in favour of the Irish Revenue and found that the applicant was not entitled to any of the reliefs sought. The applicant had sought an order quashing the Irish Revenue's notice of opinion stating that a number of transactions entered into by the applicant and his wife together constituted a tax avoidance transaction under the GAAR. The issuing of the notice of opinion led to the withdrawal of a tax advantage of over EUR6 million.

The judge found that the notice of opinion issued by the nominated officer of the 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 that there was no breach of natural or constitutional justice.

TAX AVOIDANCE PENALTIES

CIVIL AND ADMINISTRATIVE PENALTIES FOR ABUSIVE TAX AVOIDANCE

25. WHAT CIVIL AND ADMINISTRATIVE PENALTIES CAN BE IMPOSED IN ABUSIVE TAX AVOIDANCE CASES IN YOUR JURISDICTION?

The penalties provided for under general tax legislation and the Code of Practice for Revenue Audit apply equally to tax avoidance transactions (*see Question 16*). However, an additional 20% surcharge can apply to tax avoidance transactions. Additionally, the most serious tax offences can be punished by a fine or imprisonment, or both (in addition to paying tax, interest and penalties).

Where the opinion of the Irish Revenue that a transaction is a tax avoidance transaction (within the meaning of the general anti-avoidance rule) becomes final, interest and a 20% surcharge will be payable on the tax that the taxpayer unsuccessfully attempted to avoid paying (*sections 811A and 811D, Taxes Consolidation Act 1997 (TCA)*).

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

CRIMINAL PENALTIES FOR ABUSIVE TAX AVOIDANCE

26. WHAT CRIMINAL PENALTIES CAN BE IMPOSED IN ABUSIVE TAX AVOIDANCE CASES IN YOUR JURISDICTION?

Criminal proceedings can be initiated where serious tax evasion is suspected. The types of offences that are most likely to be prosecuted include:

- Deliberate omissions from tax returns.
- False claims for repayment.
- Use of forged or falsified documents.
- Facilitating fraudulent evasion of tax.
- Systematic scheme to evade tax.
- Use of offshore bank accounts to evade tax.
- Insidious schemes of tax evasion.
- Failure (as distinct from minor delays) in remitting fiduciary taxes.

TAX AVOIDANCE DEVELOPMENTS AND REFORM

27. ARE THERE ANY CURRENT TRENDS, DEVELOPMENTS OR REFORM PROPOSALS THAT HAVE OR WILL AFFECT THE AREA OF TAX AVOIDANCE IN YOUR JURISDICTION?

There has been a significant increase in disputes regarding perceived tax avoidance before the Tax Appeals Commission and the courts. This trend is likely to continue.

THE REGULATORY AUTHORITY

IRISH REVENUE COMMISSIONERS (IRISH REVENUE)

T + 353 1 865 5000
F + 353 1 865 5000
E NationalCompaniesUnit@revenue.ie
W www.revenue.ie

Outline structure. The Irish Revenue is structured into various divisions based on the type of tax levied.

Responsibilities. The Irish Revenue is responsible for the collection and enforcement of taxes in Ireland.

Procedure for obtaining documents. Documents are available on the Irish Revenue online service at: *www.ros.ie*.

ONLINE RESOURCES

IRISH REVENUE COMMISSIONERS (IRISH REVENUE)

W www.revenue.ie

Description. Website of the Irish Revenue, containing details on tax collection and enforcement in Ireland.

COURTS SERVICE

W www.courts.ie

Description. Website of the Courts Service of Ireland, containing details and judgments of cases in the Irish courts system.