COMPETING IN A CHANGING WORLD

A Road Map for Ireland's Tax Competitiveness

OCTOBER 2014

An Roinn Airgeadais
Department of Finance

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Foreword by the Minister for Finance

Across the world the issue of how companies should be taxed has probably never before been as topical or as controversial.

The globalisation of trade and the emergence of a new digitalised economy are but two of the reasons why political leaders, commentators and the public more generally are asking themselves whether current international tax rules are on the one hand effective and on the other hand fair.

In a response to this, work is now ongoing in the European Union and at the Organisation for Economic Cooperation and Development (OECD) to redefine what is and what is not deemed to be fair tax competition, and to better align taxing rights with substantive activity.

Last year, at Budget time, I recognised the importance of these issues by publishing for the first time an International Tax Strategy for Ireland, a statement of the principles and objectives that guide our approach to international corporate tax issues.

This document now provides an update on the objectives set out in that Strategy, and sets out a Road Map for Ireland's Tax Competitiveness now and into the future.

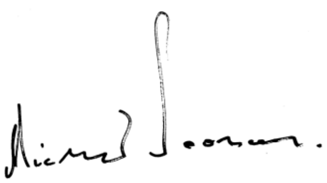
I believe that there are both risks and opportunities for Ireland in terms of the international tax policy discussions which are now underway.

It would be impossible to eliminate all the risks. But it is the Government's aim to manage the risks as best we can and maximise the opportunities for Ireland that will arise from the debate.

For this reason, I am now publishing this Road Map to outline the set of measures being undertaken to reposition Ireland so as to be best able to reap the benefits, in terms of sustainable foreign direct investment, of a changed international tax landscape.

This Road Map builds on the results of the OECD BEPS consultation process run by my Department earlier this year, and was also informed by the comprehensive analysis underpinning the Economic Impact Assessment of Ireland's Corporation Tax Policy, which I am also publishing today.

I hope you find this Road Map for Ireland's Tax Competitiveness both informative and useful.



Michael Noonan TD
Minister for Finance

14 October 2014

1. Introduction

For more than 50 years Ireland has been successful in attracting mobile foreign direct investment (FDI) which has brought both employment and substantial investment to this country.

Ireland's corporate tax strategy has three key elements: rate, regime and reputation.

The tax rate is settled policy. Ireland remains 100% committed to the 12.5% corporation tax rate. This will not change.

Countries are increasingly competing for mobile foreign direct investment. As the Minister for Finance said in his 2013 Budget Day speech, he wants Ireland to play fair – as we have always done – and play to win. In that regard, the competitiveness of Ireland's overall corporate tax regime is evaluated on an on-going basis.

Increasingly, tax reputation is also a key factor in winning mobile foreign direct investment. Over the last 24 months or so, the international rules for taxing multinational companies have been a focus for much discussion across the globe. The G20 has acknowledged that global challenges require global action. This is now happening through the OECD Base Erosion and Profit Shifting (BEPS) project, in which Ireland is playing an active part.

As part of the process of maintaining and enhancing Ireland's tax reputation, last year the Minister for Finance published a new international tax strategy statement which sets out Ireland's objectives and commitments in relation to international tax issues.

With the strong signals from the OECD BEPS Project that international tax rules must change, Ireland now needs to place itself in the best position possible to become the country of choice for mobile foreign direct investment in a post-BEPS environment.

This Road Map for Ireland's Tax Competitiveness aims to position Ireland towards maintaining the most competitive taxation offering that conforms with good practice. In conjunction with the non-tax measures set out in the Government's recent "Policy Statement on Foreign Direct Investment in Ireland"[1], this Road Map will provide the foundations for Ireland to continue to support the growth of our domestic companies and to maintain and expand our position as a thriving hub for FDI.

The next section (Section 3) sets out the international tax policy context within which Ireland now finds itself competing for foreign direct investment.

Section 4 contains an update on progress towards meeting the objectives set out in Ireland's International Tax Strategy published last year.

Section 5 sets out the Road Map for Ireland's Tax Competiveness which contains a suite of measures to be implemented over the coming months aimed at repositioning Ireland towards having a best-in-class internationally competitive and sustainable tax regime.

The Road Map relies heavily on research and analysis carried out throughout 2014, the results of which are contained a separate publication entitled 'Economic Impact Assessment of Ireland's Corporation Tax Policy'. This work highlights how important a competitive corporation tax policy is for the overall Irish economy.

[1] Policy Statement on Foreign Direct Investment in Ireland – published by the Department of Jobs, Enterprise and Innovation, July 2014

2. International Tax Policy Context

International context

Internationally, corporate tax planning by multinational companies has moved to the top of the political agenda as a result of the global financial crisis.

Tax planning by multinationals has evolved to take advantage of the differences between jurisdictions' tax codes, which can unintentionally provide opportunities for some multinational corporations to significantly reduce taxation in a manner which is inconsistent with the policy objectives of such rules. Rules put in place at a particular time for a particular purpose can give rise to unintended results over time. This is recognised as a complex global problem.

Some of the international rules are also perceived as being outdated, as not having kept pace with evolution from traditional business structures to new models involving integrated global supply chains and the digital economy - where national borders become less relevant and the location of profit generation becomes more difficult to identify.

Traditionally, a jurisdiction designed its tax laws to only take account of factors within its own borders. The tax laws of other jurisdictions, even its closest neighbours, were of little relevance. However as international markets became more integrated, especially with the arrival of the EU's internal market, borders have become more open and taxing rights less clear-cut. The issue of which jurisdiction has the right to tax has become even more clouded by the emergence of the digital economy.

The task facing tax policy makers and legislators from all around the world is to put the appropriate rules in place to ensure as much consistency as possible between jurisdictions, which in turn will provide both taxpayers and tax authorities with a greater degree of certainty as to where and how income should be taxed.

Against this backdrop, policy makers face an increasingly difficult balancing act – designing tax rules which stimulate economic growth, whilst also managing to increase tax revenues.

Tax policy is at the core of national sovereignty, and each country is free to devise its tax system in the way it considers most appropriate in accordance with internationally-accepted standards. OECD studies have indicated that international competitiveness concerns and pressures are felt in all countries. They have also shown that corporate taxes are the most harmful to economic growth prospects.

There are international rules around fair tax competition which recognise that a competitive tax system is a legitimate tool for promoting business and economic growth, but also acknowledge that there are limits as to what a country can do with its tax system before it constitutes "harmful" tax competition. It is in this context that Ireland seeks to strike the appropriate balance of playing fair, but playing to win.

Corporate context

It is not just governments who are striving to be competitive as regards taxation. It is also a competitiveness issue that affects companies. It is often highlighted that the "fiduciary duty" obligations imposed on company directors by company law oblige them to make decisions in the best interests of their shareholders, particularly with reference to the value of company shares. It has been argued that that it is in the interests of shareholders, and therefore a responsibility of company directors, to strive to use all legitimate means possible to reduce their effective tax rates.

Balanced against this however is the intense international public interest in the tax affairs of multinational companies, and the debate around the morality of aggressive tax practices driving down corporation tax rates or revenues in particular jurisdictions.

The resulting uncertainty created by these opposing considerations is to the detriment of all parties, and contributes to the complexity of the current international policy environment.

Recent events and the proposed BEPS solution

There is a growing perception that governments lose substantial corporate tax revenue because of tax planning.

The "BEPS" project was born at OECD level, backed by political stimulus. The G20 Leaders' meeting in Mexico in June 2012 explicitly referred to "the need to prevent base erosion and profit shifting".

The project has continued to be politically endorsed at the highest level internationally since then, and an OECD report in February 2013 and subsequent action plan in July 2013 were both endorsed by the G20.

The principle underpinning the current OECD work is that domestic rules for international taxation and internationally agreed standards are still grounded in an economic environment characterised by a lower degree of economic integration across borders. Today's environment of global business, characterised by the increasing importance of intellectual property as a value-driver and by constant developments of information and communication technologies, no longer fits comfortably within these rules.

The aim of the BEPS Action Plan is to *"provide countries with domestic and international instruments that will better align rights to tax with economic activity"*.

In summary, international tax policy is, and always was, complex and challenging, and evolution in business models has heightened this complexity. There is a consensus that the global system needs some fixing, which the OECD will examine and make recommendations on, and it will then be up to countries to consider the implementation of the recommendations in their own domestic systems.

Ireland's interaction with the international tax architecture

Ireland fits into this global tax architecture on two levels.

Firstly by participating in international fora such as the EU and the OECD, and secondly by reflecting internationally agreed principles in our own domestic system where appropriate.

- Since 2010 Irish transfer pricing rules have been codified in legislation.
- Ireland has full exchange of tax information with our treaty partners through our network of 71 double tax agreements and more than 20 tax information exchange agreements, which are based on OECD model agreements.
- A General Anti-Avoidance Rule (GAAR) has been in place in Irish legislation since 1989 – the EU Commission are now calling for all Member States to introduce such domestic legislation.
- The recent OECD Global Forum Peer Review Report on Ireland's legal and regulatory framework for transparency and exchange of information found that Ireland has an effective

system for the exchange of information in tax matters and is fully compliant with OECD standards.

- Recently, Ireland also pushed forward the international tax reform agenda during our EU Presidency 2013, and achieved progress in countering tax fraud and aggressive tax planning.

- Ireland was also one of the early movers in relation to new international initiatives on Exchange of Tax Information – being the fourth country in the world to sign a FATCA agreement with the US in December 2012.

Ireland's commitment to OECD BEPS Project

It has consistently been stated that the BEPS project cannot succeed without coordinated multilateral action and in this regard Ireland intends to move forward with the other countries involved in the process. Ireland will advance on the actions proposed in step with other countries, to take a measured and considered approach to the adoption of any necessary changes. It is critically important that agreement is reached among all parties because if some jurisdictions decide not to implement the proposals they could completely undermine the whole BEPS project.

The BEPS project is hugely important to the future of worldwide co-operation on taxation but the number one priority must be to get it right.

The alternative to co-ordinated BEPS engagement is unilateral action by individual countries, taking their own defensive measures on a piecemeal basis. This could be ineffective or, worse still, it could impact on certain countries, particularly smaller countries, most severely.

Indeed, while the BEPS project will involve challenges, Ireland believes that it could also offer a number of opportunities for small countries.

The Irish taxation system is built upon substance and as such the alignment of profits with substance, allied to a competitive rate of tax, accords well with the concepts that have been the cornerstone of Ireland's corporation tax policy since the 1950s.

3. Update on Ireland's International Tax Strategy

Last year, the Government published Ireland's International Tax Strategy, which set out the principles and objectives underlying Ireland's international tax policy.

Progress in terms of meeting those various commitments over the last twelve months is set out below.

<table>
<tr><th>Commitments</th><th>Developments since October 2013</th></tr>
<tr><td>Ireland is committed to full exchange of tax information with our tax treaty partners

We achieve this by:
• Responding to requests for information in an efficient manner
• Providing information in as comprehensive a manner as possible taking account of the nature of the request
• Complying fully with our responsibilities and obligations set out in tax treaties and other bilateral and multilateral agreements</td><td>• Two new DTAs signed
• Three Protocols to existing DTAs agreed, including two which provide for new exchange of information provisions
• In November 2013 the Global Forum on Transparency and Exchange of Tax Information gave Ireland a top rating following an extensive peer-review process – only 18 countries world-wide received this top rating</td></tr>
<tr><td>Ireland is committed to global automatic exchange of tax information, in line with existing and emerging EU and OECD rules

We promote this by:
• Timely transposition of relevant EU legislation into Irish law
• Full participation in OECD developments, making appropriate provision in Irish law as necessary
• Promoting the use of automatic exchange of information with tax treaty partners</td><td>• Ireland was one of the first countries to join the "Early Adopters" – a group of over forty jurisdictions who are committed to implementing the OECD's new Common Reporting Standard
• Ireland has participated in EU discussions on the revision to the Directive on Administrative Cooperation to bring it into line with the new Common Reporting Standard, and it is expected that this will be adopted by the end of 2014</td></tr>
</table>

Commitments	Developments since October 2013
Ireland is committed to actively contribute to the OECD and EU efforts to tackle harmful tax competition We achieve this by: • Active participation in the EU's Code of Conduct and the OECD's Forum on Harmful Tax Practices • Rejecting introduction of measures in national legislation which could constitute harmful tax competition • Eliminating any measure in national legislation in the event that it were found to be harmful • Active participation in the OECD Base Erosion and Profit Shifting project	• Legislation was introduced in Finance (No.2) Act 2013 to ensure that a mismatch in company residence rules between Ireland and a treaty-partner country could not allow an Irish company to be "Stateless" for tax purposes • Public consultation on BEPS project conducted
Ireland is committed to engage constructively and respectfully with developing countries in relation to tax matters including by offering assistance wherever possible We achieve this by: • Supporting international efforts to build developing country capacity to benefit from enhanced global tax transparency • Promoting the extension of Country-by-Country Reporting to areas beyond the "extractive" sector and greater international reporting to competent authorities • Offering financial support to regional initiatives to strengthen tax administrations in Africa • Strengthening the Public Financial Management systems of developing countries	• Spillover Analysis currently being undertaken to research what spillover effects the Irish tax regime may have on the economies of developing countries • DTA with Botswana signed • Two DTAs with other African partners agreed and ready for signature • Guidelines on country-by-country reporting produced in the context of Capital Requirements Directive IV

4. Road Map for Ireland’s Tax Competitiveness

Now is the right time for Ireland to take stock of recent international tax developments and plot out its strategic direction for the future that will ensure a sustainable and competitive tax regime that plays by the rules but also plays to win for foreign direct investment.

This road map builds on the results of the public consultation on BEPS held earlier in the year, and was also informed by the comprehensive analysis underpinning the Economic Impact Assessment of Ireland’s Corporation Tax Policy which complements this publication.

There are 10 key elements to Ireland’s Roadmap for Tax Competitiveness, covering not only corporation tax, but also income tax. A summary of the commitments is outlined below, with further detail on the following pages.

Road Map – Summary

Item	Road Map – Summary of Actions
1.	Maintain the **12.5%** Corporation Tax Rate, supported by independent research
2.	Introduce default **corporate tax residence** rule
3.	Improve **intellectual property** regime Consult to develop “Knowledge Development Box” and enhance existing IP regime
4.	Enhance **R&D regime** – remove base year restriction
5.	Enhance Special Assignee Relief Programme **(SARP)** to attract mobile talent
6.	Enhance Employment & Investment Incentive **(EII)** to support indigenous businesses
7.	Enhance the Foreign Earnings Deduction **(FED)** tax regime, to support Irish businesses in accessing foreign export markets
8.	Increase **Revenue competent authority** resources to defend transfer pricing disputes
9.	Continued expansion of **Tax Treaty Network**
10.	Maintain commitment to ensuring an **open and transparent tax regime**

Road Map – Detailed Commitments and Actions

Item	Commitment and Action
1.	**Rate: maintaining the 12.5% corporation tax rate is settled policy, it will not change** • The Department of Finance has commissioned independent research, conducted by the ESRI, which shows that an increase in Ireland's corporation tax rate would have reduced FDI flows into the country. • For this reason the Government is more certain than ever that the 12.5% CT rate should not and will not change.
	ACTION 1: **Budget 2015 publication of independent ESRI Research in the Department's "Economic Impact Assessment of Ireland's Corporation Tax Policy"**
2.	**Reputation: Company Residence Rules** • Ireland's company tax residence rules have not kept pace with international tax developments. • They therefore will be updated in Finance Bill 2014 to provide a default rule that all companies incorporated in Ireland are tax resident in Ireland. • The change will come into effect on 1 January 2015 in respect of new companies. • In the interest of giving certainty to companies with existing operations in Ireland, a transition period to 2020 will be provided.
	ACTION 2: **Legislative change on Ireland's company residence rules introduced in Finance Bill 2014**

3.	**Regime: Intellectual Property**
	• EU and OECD rules on what will be acceptable competition in this area are not yet settled.
	• However, following international trends in competitor jurisdictions, it is clear that making Ireland an attractive location for the development of intangible assets should be a priority.
	• The Government intends to introduce a "Knowledge Development Box" income-based tax regime for intangible assets in 2015, and will open a public consultation on the development of the regime in late 2014.
	• In addition, Ireland's existing s.291A capital allowances regime for expenditure on intangible assets will be enhanced in Finance Bill 2014:
	    ○ The current 80% cap on the aggregate amount of allowances and related interest expense that may be claimed will be removed.
	    ○ The definition of specified intangible assets will be amended to explicitly include customer lists.

	ACTION 3: **Public consultation on "Knowledge Development Box" to open in 2014, and legislative enhancements to s.291A introduced in Finance Bill 2014**

Item	Commitment and Action
4.	**Regime: R&D tax credit** • In Budget 2014 the Minister for Finance announced his intention to phase out the base year restriction, subject to resources. • Finance Bill 2014 will implement this intention and provide for the full removal of the restriction. • The Revenue Commissioners also plan to publish new guidelines to enhance clarity on the administration of the R&D tax credit.
	ACTION 4: **Legislative changes to R&D regime introduced in Finance Bill 2014**
5.	**Regime: Special Assignee Relief Programme (SARP)** • International competition to attract high-quality mobile talent is intense. • SARP was introduced to enable Irish employers to compete with other countries, to attract the talent necessary to establish and develop global businesses in Ireland. • A comprehensive review of SARP was undertaken in advance of Budget 2015, to identify cost-effective options to improve the effectiveness of the regime. • Finance Bill 2014 will provide for the continuation and enhancement of the SARP regime.
	ACTION 5: **Legislative changes to SARP introduced in Finance Bill 2014**
6.	**Regime: Employment and Investment Incentive (EII)** • The EII scheme assists small and medium-sized enterprises to access development capital, in order to expand and increase employment. • The Department of Finance, in consultation with the Revenue Commissioners, undertook a comprehensive review of the EII in advance of Budget 2015. • As a result the EII is to be amended to raise company limits, increase the holding period by 1 year and include medium-sized companies in non-assisted areas and internationally traded financial services subject to certification by Enterprise Ireland. • The operating and managing of hotels, guest houses and self-catering accommodation will remain eligible under the EII for a further 3 years.
	ACTION 6: **Legislative changes to EII introduced in Finance Bill 2014**
7.	**Regime: Continue to Diversify and Improve Access to new Export Markets** • Support for Irish enterprises to expand and access new export markets is key to the diversification of the corporation tax base. • A review of the Foreign Earnings Deduction (FED) tax regime, which supports Irish businesses in accessing foreign export markets, was undertaken in 2014. • In Finance Bill 2014 the list of countries relevant for the FED will be expanded to include a number of countries in the Middle East and Asia.
	ACTION 7: **Legislative changes to FED regime introduced in Finance Bill 2014**

Item	Commitment and Action
8.	**Regime: Competent Authority for Transfer Pricing** • International Transfer Pricing disputes are likely to grow in number and Ireland must be ready to defend its tax base. • Accordingly Ireland will strengthen the capabilities of its transfer pricing competent authority by assigning new resources to the Revenue Commissioners to meet this priority need.
	ACTION 8: **Additional Competent Authority staff to be recruited**
9.	**Reputation: Expansion of Tax Treaty Network** • Ireland's extensive network of tax treaties and information exchange agreements is a key factor in attracting globalised business to locate substance in Ireland. • Continued expansion of Ireland's tax treaty network is critical to continued success.
	ACTION 9: **Work to expand Ireland's DTA Network is continuing, and will be accelerated where possible**
10.	**Reputation: Ireland is maintaining its commitment to ensuring an open and transparent tax regime** In line with the International Tax Strategy published last year, Ireland will be: • An early adopter of Automatic Exchange of Tax Information. • Supportive of OECD proposals for Country by Country reporting. • One of the first countries worldwide to carry out a Spillover Analysis of the impact of its tax system on developing economies.
	ACTION 10: **Publication of Spillover Analysis report and continued support of information exchange and reporting**

5. Conclusion

This is a time of both great challenge and great opportunity for Ireland. International tax rules are changing as an inevitable response to the increasing globalisation of trade and the ever-expanding digital economy.

Ireland is playing a full part in these discussions at international level.

As a small country with an established pedigree for attracting substantive foreign direct investment, Ireland is also well placed to capitalise on the outcome of these discussions, through the focussed implementation of strategic actions to adapt to the evolving international environment.

The Road Map contained in this document outlines ten actions, identified through an extensive process of research and public consultation, which will guide Ireland's tax competitiveness into the future.

The certainty provided by this Road Map will provide a firm foundation from which businesses located in Ireland, of both domestic and foreign origin, can continue to prosper in the global economy.