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AMERICAN CHAMBER of COMMERCE IRELAND

Public Consultation on the Second Feedback Statement on Participation Exemption in Irish Corporate Tax System for Foreign Dividends

Submission from American Chamber of Commerce Ireland (AmCham) to the Department of Finance

September 2024

The American Chamber of Commerce Ireland
The Voice of US-Ireland Business

The American Chamber of Commerce Ireland (AmCham) is the collective voice of US companies in Ireland and the leading international business organisation supporting the Transatlantic business relationship. Our members are the Irish operations of all the major US companies in every sector present here, Irish companies with operations in the United States and organisations with close linkages to US-Ireland trade and investment.

AmCham welcomes the opportunity to comment on the Second Feedback Statement on the introduction of a Participation Exemption into Irish legislation.

As Ireland is a small open economy, international tax developments have a significant impact on the overall success of the domestic Irish economy. Considering the recent introduction of the minimum tax rate of 15 percent under Pillar Two, it is essential that Ireland adapts and enhances its tax offering to ensure it remains a destination of choice for US FDI and the introduction of a broad and simple participation exemption regime is key to this. As currently drafted, the legislation has not met the policy objective as being competitive or administratively efficient.

Our comments are as follows:

Requirement to source dividends from "profits"

The proposed requirement for dividend payments to be made from profits which have been included in the payor's profit and loss account, similar to the definition in section 21B TCA 1997, will cause significant complexity, and would decrease the competitiveness of the regime being introduced.

AmCham would suggest the deletion of the reference to "out of profits" in the definition of 'relevant distribution'. In this regard, consideration should be given to the fact that other protections exist within the proposed participation exemption legislation and through Pillar Two (i.e., ensuring a minimum tax rate is in force for in scope groups), and significant safeguards and protections are already in place.

The current proposed wording has the potential to restrict the ability of Irish resident companies to repatriate funds either by means of a dividend or a return of capital from their overseas subsidiaries. Proceeds from distributions are an important way of funding shareholder dividends and ongoing investment. As drafted the repatriation of the funds originally invested from certain subsidiaries and also from companies which may have certain negative attributes (e.g. impairment losses) may not be able to avail of either the capital gains tax exemption or the dividend participation exemption. We have set out below some examples of the common place scenarios in which the exemption would not apply as drafted.

1. Non-Irish holding company receives a dividend from its subsidiary which results in an impairment of the investment. The net effect of this to the P&L would be zero, as the dividend income and impairment would offset. Any subsequent payments to the Irish holding company would not be paid out of profits included in the P&L.

2. Non-Irish holding company with existing negative reserves or losses receives a dividend from its subsidiary. In such an instance, the company may be able to pay a dividend to Ireland from other reserves, but the dividend would not be paid from profits included in the P&L.
3. Dividends paid from a capital contribution account. The dividend would not be paid from profits included in the P&L, but the receipt would not be regarded as a capital receipt. The payment would then unlikely satisfy either regime. A dividend from a capital contribution account paid by an Irish resident company to its Irish parent would be regarded as franked investment income.
4. In common law jurisdictions, it is common practice to convert a non-distributable reserve (e.g. share capital, revaluation reserve) to a distributable reserve through a corporate mechanism, e.g. a share capital reduction. Any dividend payments made from this newly created distributable reserve would not be paid from profits which have been included within the P&L. From an Irish standpoint, this conversion is a very common mechanism to create distributable reserves and can be achieved via a summary approval procedure or a High Court application. Any dividends paid by an Irish resident company to its Irish parent from such a reserve would be regarded as franked investment income for Irish tax purposes.
5. The implications regarding the payment of a distribution from a share premium account has been noted on a number of occasions. However, it is worth reiterating that such a distribution is unlikely to satisfy either the CGT or dividend participation exemption regimes.
6. A number of jurisdictions allow mergers or amalgamations. The assets and liabilities of the merged entity will transfer to the surviving entity, but the historic P&L reserves may not transfer to the surviving entity. In its place, a merger reserve would be created. Any dividends paid from the surviving entity may not be regarded as being paid from the P&L profits of the company.
7. A number of jurisdictions allow for companies to make dividend payments without requiring any distributable reserves, providing that the paying company satisfies a solvency test. This would be the case in respect of Irish unlimited companies.
8. In the case of a cost-plus subsidiary, a company may have a policy not to recharge share-based payments. However, for the purpose of local statutory accounts a notional Stock Based Compensation (SBC) expense may be required to be debited to the P&L and credited to an SBC reserve account in the balance sheet. This reduces the profits in the P&L and hence reduces the amount of the dividend

to be paid out of retained earnings which have hit the P&L. In many jurisdictions a dividend can be paid out of the SBC reserve account.

Further to the above, by including the requirement for the dividend to be paid out of profits, it will be necessary to trace the historic profits of the company. This will lead to significant administrative complexities and will also be difficult to trace in respect of certain locations and also for acquired groups.

Relevant Distribution

'Relevant distribution' is currently defined as "*a dividend paid, or other distribution made, out of profits in respect of a relevant subsidiary's share capital other than redeemable share capital*". From an Irish corporate law perspective, shares have the capability of being redeemed subject to the constitution of the company. Similar flexibility arises in many other countries. As participation exemption is not available for a dividend that falls within interest equivalent, the redeemable share capital should not be required. This provision should be revisited to avoid unintended consequences.

Additionally, with respect to the redeemable capital, it is important to note that a similar construct exists in the definition of relevant participation, which also requires revision. Both instances should be addressed to ensure the rules are clear and prevent potential complications.

Definition of "Parent company" and "relevant subsidiary"

The proposed definitions of 'parent company' and 'relevant subsidiary' include the phrase *"without the possibility of being exempt or an option of being exempt, …"* This language gives rise to ambiguity and should be amended. We view that the very broad wording can lead to unnecessary ambiguity. Depending on the individual jurisdiction, there may be options to elect for the entity to be exempt, such as the US check-the-box regime. Based on the wording, the exemption may not apply to a number of US companies, irrespective of the fact that the individual company may be fully subject to tax. With the introduction of Pillar Two, the vast majority of companies will be subject to tax at the rate of 15 percent. As such, we do not believe that this wording has any practical benefits. Failing the complete removal of the wording, we strongly recommend that in order to be excluded from the participation exemption regime, the company should be exempt or has opted to be exempt from tax.

Geographic Scope

The Feedback Statement provides that the geographic scope of the participation exemption currently remains at EU/EEA and tax treaty partner source jurisdictions. We are of the view that the scope should be expanded to include dividends paid by a

company that is a constituent entity of the same Pillar Two group as the Irish recipient regardless of the location of the payee company.

Anti-Avoidance

The second Feedback Statement includes an anti-avoidance provision with language not previously used in Irish tax legislation. The use of terms such as “economic reality” and “valid commercial reasons” are not defined and will cause uncertainty for taxpayers.

Irish tax legislation already contains comprehensive anti-avoidance and anti-base erosion provisions, and the introduction of more anti-avoidance provisions is too complex and unnecessary.