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REPORT

From:	General Secretariat of the Council
To:	Delegations
Subject:	Code of Conduct Group (Business Taxation) - Report to the Council

STANDSTILL – IRELAND (IE018) - Participation exemption for foreign dividends

I. Background

Ireland has notified the introduction of a participation exemption for certain foreign distributions in the framework of the annual standstill exercise for 2024.

II. Description of the measure

1. Relevant legal framework

The participation exemption for certain foreign distributions (hereafter "the participation exemption") was introduced by section 50 of the Finance Act 2024. The measure is contained section 831B of the Taxes Consolidation Act 1997 (TCA). The participation exemption applies in respect of relevant distributions made on or after 1 January 2025.

2. Purpose of the measure

The policy objective of introducing a participation exemption is to simplify the redistribution of profits and other reserves from overseas subsidiaries to their parent companies by providing double taxation relief in the form of an exemption.

Ireland was the only EU Member State and one of a very small number of OECD countries that did not operate some form of participation exemption for foreign dividends. Ireland traditionally operated a worldwide tax system, whereby an Irish resident company is liable to corporation tax on all its profits wherever arising. Where income is chargeable to tax in more than one country, as is the case where a parent company receives distributions from a foreign subsidiary, the parent company receives a credit for the tax paid in respect of that income in the subsidiary's jurisdiction.

The participation exemption simplifies these rules by providing a corporation tax exemption for qualifying foreign distributions received by parent companies. Consequently, the participation exemption arrives at the same outcome, but through a less onerous system.

The tax treatment applicable to capital gains is not dealt with under the notified participation exemption of section 831B.

3. Design of the measure

The participation exemption is available to corporate taxpayers receiving a relevant distribution from a relevant subsidiary, subject to certain conditions.

A relevant distribution is a payment from a subsidiary to a parent company made out of profits or, in certain circumstances, out of assets of the subsidiary. The distribution must be made to the recipients in their capacity as shareholder.

To qualify for the exemption, the distribution must be classified as Case III income, which generally relates to investment income. A distribution which constitutes trading income for the recipient is not in scope of the exemption.

In order to avail of the exemption, the parent company must make a claim in its corporation tax return. If a claim is made to avail of the participation exemption in respect of an accounting period, all relevant distributions are exempted. A claim cannot be made on a dividend by dividend, or subsidiary by subsidiary, basis.

3.1. Beneficiaries

The parent company must be tax resident in Ireland or a non-resident company from the EEA which has a permanent establishment in Ireland. The parent company must have a holding of at least 5% of ordinary shares in the relevant subsidiary, for a continuous period of at least 12 months. In addition, the parent company must have a beneficial entitlement to at least 5% of both the (i) profits and (ii) assets on a winding up of the relevant subsidiary, that are available for distribution to equity holders of the relevant subsidiary. These holding requirements ensure there is substance and prevent contrived holdings. The relevant subsidiary must, on both the date that the distribution is made and throughout the five-year period prior to this date, have also been resident in the EEA or a country with which Ireland has a Double Tax Agreement.

3.2. Activity based exclusions

The participation exemption does not apply to certain entities based on the activity which they undertake. These activities are subject to specific rules for the computation of corporation tax. These entities are excluded from the participation exemption:

- Collective investment vehicles and securitisation companies.
- Life assurance companies generally.
- Offshore funds.

3.3. Prevention of double non-taxation or double benefit

The prevention of double non-taxation is achieved through several provisions.

- To avail of the participation exemption, the relevant subsidiary must not be generally exempt from a foreign tax which corresponds to Irish corporation tax, both at the date the distribution is made and throughout the five-year period prior to this date. A foreign tax is a tax that generally applies to income, profits and gains of a resident company, imposed at a nominal rate greater than zero per cent.
- The relevant distribution must constitute income in the hands of the recipient (parent) company for Irish tax purposes. This mirrors the requirement for double tax relief in the form of a credit whereby the dividend must be an income receipt, rather than a capital receipt.
- A distribution which is deductible for tax purposes in any jurisdiction is not eligible for exemption.
- Payments of any interest or other income from debt claims providing rights to participate in a company’s profits, or payments of interest equivalents, cannot qualify for exemption.
- Only distributions from subsidiaries resident in EU/EEA Member States and tax treaty partner jurisdictions qualify. Distributions from subsidiaries resident in jurisdictions included on the EU Code of Conduct list of non-cooperative jurisdictions for tax purposes do not qualify for the participation exemption.

- Anti-avoidance measures exist to prevent the exemption of a distribution sourced from a company resident in a non-qualifying country, if this is contrived through means of a group reconstruction or merger arrangement.

3.4. Anti-abuse rules

In addition to the safeguards outlined above, the participation exemption legislation also contains a targeted anti-avoidance rule. This provides that distributions which arise in respect of an arrangement put in place to obtain a tax advantage, or in respect of an arrangement which is not genuine, do not qualify for the participation exemption.

Furthermore, the exemption will not apply where another provision takes precedence, for example, the ATAD-compliant general anti-avoidance rule (GAAR) contained in section 811C of the TCA.

Ireland transposed CFC rules, as foreseen in the ATAD Directive, via Finance Act 2018. Ireland would also highlight that subsection (1)(e) of section 50 of the Finance Act 2024 provides that a CFC's undistributed income (on which the CFC charge arises) will not be reduced where a distribution has been made to an Irish resident person and a claim for the participation exemption has been made with respect to that distribution.

4. Impact of the measure

The policy objective of the participation exemption is to simplify the current practice of providing double tax relief for tax already paid on the same profits. The tax credit system achieved this outcome but was administratively onerous.

This measure simplifies the current rules for double taxation relief, it is not expected to result in additional relief or the application of a lower level of taxation than the level which generally applies and therefore there is no anticipated budgetary impact.

III. Preliminary remarks

The Irish participation exemption provides relief from double taxation in the form of exemption. The measure does not include capital gains[1].

In the 1999 report[2], the Group decided that participation exemptions should be combined with an appropriate controlled foreign company legislation, in order to avoid that income from tax havens and other harmful regimes is received tax free in a Member State. These principles have then been laid down in the 2010 Guidance on inbound profit transfers[3], which mandates Member States that grant a corporate tax exemption on foreign source dividends to apply either effective anti-abuse provisions (e.g. CFC rules) or a switch-over provision.

The Guidance was superseded by the ATAD Directive (2016/1164), according to which EU Member States have to implement a CFC rule. As a result, by the implementation of the ATAD Directive, the 2010 guidance on inbound profit transfers was implemented as well[4].

Ireland applies CFC legislation since 2018, as foreseen in the ATAD Directive.

Furthermore, Ireland ensures an effective taxation of the distributed profits through several other provisions:

Firstly, through the requirements of the participation exemption, especially the following:

The distributing company should not be exempt from taxation and the distribution is not allowed to be deductible for tax purposes in any jurisdiction.

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1 The Irish capital gains exemption and the Irish holding company regime have been examined by the Group in 2005, and more recently in 2019. In 2019, under the monitoring of the compliance with the relevant Guidance, the holding company regime was considered compliant with the 2000 Guidance on Holding companies regime.

2 Report of 23.11.1999, SN 4901/99, para. 48. See also SI004 (9427/05 FISC 55); CYP017, (16766/10 FISC 139)

3 Document 16766/10 FISC 139. The Guidance reads: *"Member States may opt to tax inbound profit transfers or to operate a participation exemption. Member States which operate a participation exemption should either ensure that the profits which give rise to foreign source dividends are subject to effective anti-abuse or countermeasures, or apply switch-over provisions targeted at ensuring effective taxation. The first could be achieved through a Member State having CFC-legislation or other anti-abuse provisions which ensure that profits artificially diverted from that Member State which may give rise to foreign source dividends are appropriately taxed."*

4 Room document of 6.4.2018, WK3998/2018.

Only distributions from subsidiaries in the EU/EEA and countries which have a Double Taxation Treaty with Ireland qualify for the exemption. Distributions from subsidiaries resident in jurisdictions included in the EU list of non-cooperative jurisdictions for tax purposes do not qualify for the participation exemption.

Secondly, through anti-abuse rules:

There is a targeted anti-abuse rule (TAAR), which avoids that non-genuine arrangements qualify for the participation exemption.

Furthermore, Ireland has a general anti-abuse rule, which may be applied instead of, or in addition to, the TAAR depending on the circumstances.

IV. Conclusion

Considering that Ireland applies CFC rules and that additional, adequate anti-abuse provisions are in place, the measure does not need to be assessed.

V. Follow-up

In view of the above, the Group agreed that this measure does not need to be assessed.