Impact of BEPS Pillar II on investment funds industry; VAT and negotiation services; TAC rulings; leasing; options

In this month's Roundtable the panel looks at the potential impact of BEPS Pillar Two rule on the investment funds industry in light of the extension of rules to standalone entities under Ireland's domestic top up tax. New guidelines issued by Revenue on the VAT treatment of negotiation services in respect of financial services, with the panel outlining the conditions to be satisfied to fall within a VAT exemption. Building on the commentary on tax treatment changes for Aircraft Leasing activity in Ireland in last month's Irish Tax Monitor, this month the panel outlines industry adaptations to the new rules. Noteworthy determinations by the Tax Appeals Commission in the opening quarter feature royalty withholding taxes, 'expenses of management' and 'wide reaching' information requests. A guidance Update to the recently introduced ERR also features while the changes in taxation of share options when exercised, and what companies need to do to meet the new rules is explained.

BEPS and investment funds

What is the potential impact of the Pillar Two rules on the investment funds industry?

Aine Gibney, Senior Manager, Financial Services, Deloitte Ireland LLP: The investment funds industry is not immune from having to consider

Aine Gibney

the impact of Pillar Two. Generally, an entity which is consolidated on a line-by-line basis into the group's consolidated financial statements (or which itself is the ultimate parent entity) will be in scope of Pillar Two where the group's revenue exceeds €750m in two of the four previous fiscal years. For the purposes of the domestic top-up tax (QDMTT), the Pillar Two rules in Ireland are extended to include standalone entities that themselves meet the revenue threshold. The December

The April Roundtable Panel consisted of:
Aine Gibney, Senior Manager, Financial Services, Deloitte Ireland LLP; Philip Nolan – VAT Partner, BDO; Isha Mongia, Assistant Manager – Indirect Tax, Deloitte Ireland LLP; Cian O'Sullivan, Tax Director, BDO; Fiona McLafferty, Managing Director – Tax Controversy, Deloitte Ireland LLP; Ailish O'Connor, Manager, Financial Services, Deloitte Ireland LLP; Sarah Conry, Director, Global Employer Services, Deloitte Ireland LLP; Elaine Flynn, Associate Director, Tax Employer Solutions, Grant Thornton; Orla McConnell, Assistant Manager, Global Employer Services, Deloitte Ireland LLP; Michelle Dunne, Director – Tax Employer Solutions, Grant Thornton.

2023 administrative guidance considered the meaning of 'revenues' for Pillar Two purposes. The extension of the rules to standalone entities could be of particular relevance to the investment funds industry.

As well as reviewing the impact from a tax liability perspective, consideration should be given to the accounting disclosure, if any, that is required to be included in the audited financial statements of the entity under the relevant accounting standards.

While some funds may be in scope, there are exclusions to be considered. Irish tax legislation provides that an 'investment entity' should not be chargeable to the domestic top up tax in Ireland. The definition of an 'investment entity', at a high level, refers to an 'investment fund' which is further defined. The definition of both 'investment entity' and 'investment fund' is broadly aligned with OECD Model Rules and the EU Directive. Further, certain entities, referred to as excluded entities (such as an investment fund that is the ultimate parent entity), are outside the scope of the rules.

"The extension of the rules to standalone entities could be of particular relevance to the investment funds industry."

Investment managers and other service providers in the industry need to calculate if they will have a top-up tax payable in Ireland in respect of the current year and the cash tax impact on the relevant fund, management company or other entity type. While there are helpful exemption or exclusions provided in the law, each structure should be considered on a case-by-case basis.

VAT Treatment of Negotiation Services

The Revenue Commissioners has introduced new guidelines on the VAT treatment of negotiation services in respect of financial services. Can you outline the changes and implications for affected taxpayers?

Philip Nolan – VAT Partner, BDO: The Irish Revenue Commissioners (Revenue) published a Tax and Duty Manual entitled "VAT treatment of negotiation services in respect of financial services" (TDM) in March 2024. We understand that this manual was published to clarify the VAT treatment as a result of a number of queries being received by Revenue.

The TDM outlines Revenue's current view as to what a "negotiation or agency" service is and the conditions which need to be satisfied to fall within the VAT exemption. In summary, please note the following:

Philip Nolan

- Merely describing a party as an "agent" or "intermediary" or a service as "agency" or "negotiation" is not sufficient;
- The nature of the service being provided and the relationship between the parties is key;
- A negotiation or agency service must consist of bringing together parties with a view to either "concluding a contract" or "negotiating a change to contract terms".
- The agent or intermediary must:
  - Not be a party to the agreed or amended contract;
  - Do all that is necessary for the parties to enter into or amend a contract; and,
  - Provide more than the mere outsource of clerical or admin tasks.
- Negotiation is a distinct act of mediation which may consist of:
  - Pointing out to your client, as one of the parties to a contract, suitable opportunities for the conclusion of such a contract;
  - Making contact with another party; or,
  - Negotiating, in the name and on behalf of your client, the detail of the payments to be made by either side.

  Examples:
- Stock, shares, debentures & other securities
  - Post a decision to effect a transaction, an adviser becomes actively involved in making the arrangements and has clear and specific responsibility to carry out the negotiations essential towards bringing the deal to its conclusion.
- Payments
  - Services consisting of the marketing, distribution, and sale of payment products, where the distributor is responsible for carrying out all tasks necessary to facilitate, negotiate and arrange the sale of the product to customers and arrange the incoming payment flows.
- Debts
  - Services consisting of bringing together the credit provider and the debtor with a view to either concluding a contract or negotiating a change to the payment terms.
- Credit
  - Services consisting of negotiation in relation to the granting of credit, regardless of whether any such transaction is finally concluded.

"The TDM does provide however a very welcome insight into Revenue's current view on the VAT treatment of negotiation and agency services in the context of financial services, particularly in respect of stocks, shares, debentures, securities, payments, debts, and credit. "

As you can see from the above summary, this is a very complex area of VAT law and as with all VAT exemptions they are to be interpreted narrowly. The TDM does provide however a very welcome insight into Revenue's current view on the VAT treatment of negotiation and agency services in the context of financial services, particularly in respect of stocks, shares, debentures, securities, payments, debts, and credit. As this issue is extremely topical and as VAT is a transactional based tax where errors can lead to substantial VAT liabilities, we would strongly recommend that affected businesses review their current activities to confirm whether the VAT treatment applied is in line with Revenue's current view.

Isha Mongia, Assistant Manager – Indirect Tax, Deloitte Ireland LLP: In March 2024, the Irish Revenue Commissioners (Revenue) published guidance on VAT treatment of negotiation services in respect of financial services. The guidance outlines Revenue's current

Isha Mongia

view as to what a "negotiation or agency" service is and the conditions which need to be satisfied for such a service to fall within the exemption provisions of Paragraphs 6 (1) and 7 of Schedule 1 to the VAT Consolidation Act 2010.

This guidance will be of interest to Ireland-based providers of such services as well as Ireland-based recipients of such services on a cross-border basis.

A negotiation or agency service is the act of bringing together a party seeking to make a financial service with another party seeking to receive a financial service with a view to either concluding a contract or negotiating a change to contractual terms. That financial service must be one falling within Paragraph 6 of Schedule 1.

Negotiation is a distinct act of mediation (as per the CJEU in CSC Financial Services (C-235/00)) which, among other services, may consist of -

- pointing out to one of the prospective parties to a contract suitable opportunities for the conclusion of such a contract,
- contacting another party, or
- negotiating, in the name and on behalf of a client, the detail of the payments to be made by either side.

The agent must –

- Carry out all the necessary for the parties to be able to enter into a contract.
- Not be a party to the agreed or amended contract.
- Carry out more than the mere clerical or administrative tasks.

Merely describing a party as an "agent" or "intermediary" or services as "agency" or "negotiation" or framing an agreement as an "Agency Agreement" is not sufficient for VAT exemption to apply. Whether a party is an "agent," or the services being provided are "agency services" is based on the nature of the services and relationship between the parties. The application of the VAT exemption will be decided on the particular circumstances of each case.

The guidance provides examples of services that may qualify as negotiation services and for the application of the VAT exemption (both domestically and on a reverse charge basis) in case of stocks, shares, debentures, and other securities, payments, debts, credits.

"The VAT exemption does not apply to the services of personal insolvency practitioners or services that are comprised of the design, management and operation of a budget which are taxable services."

- Stocks, shares, debentures, and other securities - Once a decision is taken to effect a share, stock, debenture or other security transaction and an adviser becomes actively involved in making the arrangements and has a clear and specific mandate to carry out the negotiations essential towards bringing the deal to its conclusion. Up to the point where the advisor's mandate becomes clear, it is possible that such services could be taxable.
- Payments - Services consisting of the marketing, distribution, and sale of payment products, where the distributor is responsible for carrying out all tasks necessary to facilitate, negotiate and arrange the sale of the product to customers and arrange the incoming payment flows.
  The exemption may also apply in case of sourcing of customer and distribution of payment products.
- Debts - Services consisting of bringing together the credit provider and the debtor with a view to either concluding a contract or negotiating a change to the payment terms.

However, the VAT exemption does not apply to the services of personal insolvency practitioners or services that are comprised of the design, management and operation of a budget which are taxable services.

- Abortive transactions can still qualify for the VAT exemption where the underlying services consist of negotiation in relation to the granting of credit.

In light of the Revenue's position highlighted in the recent guidance, affected businesses should review their current business activities to understand whether the VAT treatment followed by them, from the perspective of an Irish business receiving such services on a cross-border basis and a domestic supplier raising fees for such services, is in line with the Revenue's view.

Tax Appeals Commission

Can you comment on noteworthy determinations from the Tax Appeals Commission from the first quarter of 2024?

Cian O'Sullivan, Tax Director, BDO: A particular determination of interest was 47TACD2024, which dealt with

Cian O'Sullivan

the deductibility of royalty withholding taxes (RWHT). This was the latest of a number of determinations relating to the deductibility of foreign taxes.

The appellant licenced its technology solutions to a large number of distributors internationally. A number of licensees deducted RWHT at source and the appellant claimed a corporation tax deduction for the RWHT under section 81 of the Taxes Consolidation Act 1997 ("TCA 1997") on the basis that they were incurred wholly and exclusively for the purpose of its trade. Revenue argued that RWHT are not a deductible expense, one of the reasons being that foreign RWHT are, by their nature, taxes on income.

The Appeal Commissioner found in favour of the appellant by determining that it had shown on the balance of probabilities that it met the test for deductibility as outlined in the UK case Strong & Co of Romsey Limited v Woodifield (Surveyor of Taxes) 5 TC 215.

"The determinations do not provide any real clarity on the order of claiming credits under schedule 24 TCA 1997 versus a deduction under section 81 TCA 1997 where both options are available to a company."

The facts of this case were similar to a 2023 determination (128TACD2023), in which the Appeal Commissioner also found in favour of the appellant. It is worth noting that the accounting periods in question for both cases predated the introduction of section 81(2)(p) TCA 1997, which specifically disallows a deduction in respect of any taxes on income. The Appeal Commissioners in both cases accepted that the RWHT were taxes on income but noted a Digital Services Tax is also a tax on income and may be allowable as a deduction, as acknowledged by Revenue. Therefore, there may be some doubt over whether the introduction of section 81(2)(p) TCA 1997 would necessarily deny a deduction for foreign RWHT.

It is also worth noting that credits in respect of the RWHT were not available to the appellants in both cases. The determinations do not provide any real clarity on the order of claiming credits under schedule 24 TCA 1997 versus a deduction under section 81 TCA 1997 where both options are available to a company.

Both the 2023 and 2024 determinations are being appealed to the High Court by Revenue, the outcomes of which may provide further clarity on this topic.

Fiona McLafferty, Managing Director – Tax Controversy, Deloitte Ireland LLP: The publication of determinations of the Tax Appeals Commission provides a source of information which may assist in managing interactions with the Revenue Commissioners on similar issues.

In Determination 48TACD2024, it was stated that had the taxpayer provided documentary evidence which separately quantified the expenditure on compliance and the expenditure on defending an

Fiona McLafferty

approach relating to the ownership of the company, the expenditure on compliance would have been part of the duties of managing investments and qualify as 'expenses of management' under section 83 of the Taxes Consolidation Act, 1997.

In Determination 47TACD2024, it was determined that foreign royalty withholding tax was an expense incurred by the taxpayer in earning its profits, and consequently deductible under section 81 of the Taxes Consolidation Act, 1997 as an expense wholly and exclusively incurred for the purposes of the trade. This conclusion was grounded in the evidence that the withholding tax was applied on gross royalties payable and was incurred irrespective of whether the taxpayer earned any profits. The taxpayer received royalties in respect of licensed technology solutions and selling the product could not be made without incurring the concurrent obligation to discharge the withholding tax on the sale.

In Determination 44TACD2024, it was determined that the taxpayer had submitted valid claims for repayment of tax within the meaning of section 865 of the Taxes Consolidation Act, 1997 and that information requested by the Revenue Commissioners was not information which was reasonably required to enable them to determine if and to what extent a repayment of tax was due. This conclusion was rooted in the finding that the information requested by the Revenue Commissioners was aimed at ascertaining whether or not Ireland had taxing rights and was not reasonably required to determine the claim for repayment. It was remarked that the information requested by the Revenue Commissioners was a 'wide reaching request'.

Aircraft Leasing

Given the changes to the corporation tax treatment of leases (see March 2024 Irish Tax Monitor), how are Irish-based aircraft leasing companies adapting to the changes?

Ailish O'Connor, Manager, Financial Services, Deloitte Ireland LLP: As discussed in the March 2024 Irish Tax Monitor, Finance (No.2) Act 2023 contains

Ailish O'Connor

a number of changes to the corporation tax treatment of leases, which are having an impact on Irish-based aircraft leasing companies. As Revenue have now confirmed that companies can no longer rely on historic leasing practises from the end of 2023, we are seeing clients actively reviewing their structures in order to assess the impact, if any, and adapt where needed to the changes by exploring restructuring options. In particular, clients are considering the trading status of single aircraft owning entities (SAOEs) and finance companies for the purposes of qualifying for the Case I 12.5% corporate tax rate. In this regard it is important that these type of structures are considered carefully as the trading status of entities are now being viewed on an entity by entity basis as opposed to having regard to the operations of the group as a whole. Other relevant considerations in terms of trading status include whether SAOEs originated the acquisition of its aircraft and lease and how and from where the SAOE is managed. It is important that Irish-based leasing companies who have not yet considered the changes undertake a review of the trading status of SAOEs and finance companies (where they have not been structured as s.110 companies) in order to determine if any steps should be taken.

Further, the evolution in Revenue practice as set out above as well as the expansion of S.403 TCA 1997 which impacts the leasing ring fence (discussed in detail in the March 2024 Irish Tax Monitor) is giving rise to a re-design of cash pooling and financing structures within leasing groups, as well as additional considerations from a loss efficiency perspective.

In addition to the above, the changes which have been introduced with respect to the taxation of finance leases are being carefully considered by impacted lessors. Notably, there are a number of key new requirements with respect to documentation and disclosures which must be met in order for certain tax treatments to apply.

"It is important that Irish-based leasing companies who have not yet considered the changes undertake a review of the trading status of SAOEs and finance companies."

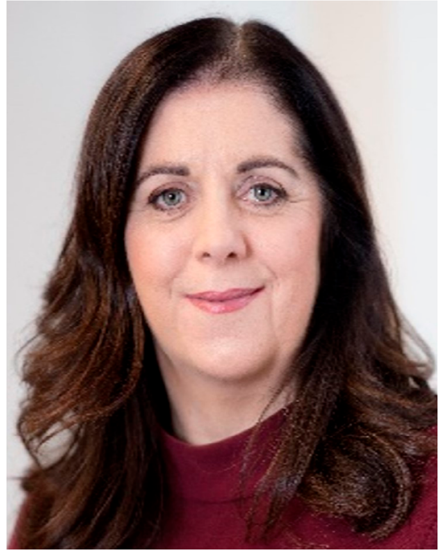
It is crucial that Irish-based aircraft leasing companies continue to reach out their advisors in order to consider the impact of these changes and consider restructuring options and alternative structures where necessary in order to mitigate any potentially negative impacts.

Share options changes

The Finance Act changes the way tax is collected from the exercise of share options, which is also the subject of a recent update from the Revenue Commissioners. Can you explain the changes and steps that should be taken to meet the new requirements?

Sarah Conry, Director, Global Employer Services, Deloitte Ireland LLP: A gain, taxable in Ireland, on the exercise of a share option by an employee or director on or after 1 January 2024 is required to be reported via payroll by the employer. Historically an employee or director exercising a share option was required to pay the taxes directly to Revenue within 30 days of exercise. The employee was required to complete and file an RTSO1 within 30 days and subsequently file a Form 11 for the tax year in which the option was exercised.

Employees need to file a Form 11 for



Sarah Conry

2023 if they exercised share options in 2023. From 1 January 2024 taxes should be withheld via payroll and an employee will not automatically be required to file a Form 11.

Employers should establish a process to ensure that payroll taxes are withheld on the exercise of share options. This may be via a sell to cover mechanism whereby shares are sold to cover the taxes or via a direct transfer of funds to the employer before shares are released. Employee Share Purchase Plans (ESPPs) are all employee plans typically operated by US multinationals. In our experience these plans are often taxed as options and employees have been responsible for the payment of taxes. Where the ESPP has been treated as an option withholding will apply to the discount on the acquisition of shares under the ESPP on or after 1 January 2024.

"Employers should establish a process to ensure that payroll taxes are withheld on the exercise of share options. This may be via a sell to cover mechanism whereby shares are sold to cover the taxes or via a direct transfer of funds to the employer before shares are released. "

There is a requirement to withhold in respect of past employees if they exercise after leaving the employment. Additional challenges arise in relation to mobile employees where part of the share option gain may be reportable. It is important for employers to establish a process to ensure compliance with the withholding requirements. Share based remuneration must be reported separately to Revenue via payroll so it is important the relevant payroll component is correctly set up. In addition, share option gains will be exempt from employer's PRSI where the shares acquired are in the employer company or a company controlling the employer.

Clear employee communications are vital to ensure employees are aware of the change, their continued obligation for 2023 and their personal obligations in respect of dividends or capital gains tax. Lack of quality employee communication erodes the value of the options from a talent retention and reward perspective.

Elaine Flynn, Associate Director, Tax Employer Solutions, Grant Thornton: Finance Act (No. 2) 2023 introduced an amendment to the

Elaine Flynn

collection and reporting requirements of share option related taxes. The taxation of a gain realised on the exercise, assignment or release of share options has moved from an individual self-assessment system to a PAYE real-time payroll withholding system. This treatment will apply to gains realised on or after 1 January 2024. From this date, employers will be responsible for collecting income tax, USC and PRSI from employees on share option gains and remitting those taxes to Revenue as part of the payroll process.

Any gains realised before 31 December 2023 will remain taxable under self-assessment and the employee will be required to submit a Form RTSO1 along with payment of the relevant taxes within 30 days of exercise.

While the extension of PAYE real-time reporting to share options may be a welcome measure from an employee perspective as it removes the onus from employees to settle their own taxes, it is a significant change for employers who, previously, may not have needed to record and collate data for tracking share option gains in order to remit taxes to the Revenue Commissioners.

"While the extension of PAYE real-time reporting to share options may be a welcome measure from an employee perspective as it removes the onus from employees to settle their own taxes, it is a significant change for employers."

Employers should be making the necessary preparations now and may wish to consider the following:

- Ensuring that the necessary processes and controls are in place so that the correct taxable gains are captured in real-time via the PAYE system and that the information is reported correctly to Revenue as share-based remuneration;
- Identifying stakeholders to ensure information is provided in a timely manner for tracking share option events for current and former employees, as well as globally mobile employees;
- Revising communications with employees on how and when to report share option related taxes to capture these new rules;
- Where employers intend to provide a 'sell to cover' option i.e. the sale of sufficient shares to cover taxes arising, consideration will need to be given on how this will be communicated to share option holders and how such a process will operate in practice.

Enhanced Reporting Requirements - ERR

The recently introduced Enhanced Reporting Requirements has been the subject of a recent guidance update. Can you outline the new guidance?

Orla McConnell, Assistant Manager, Global Employer Services, Deloitte Ireland LLP: The Enhanced Reporting Requirements (ERR) were introduced from 1 January 2024 and apply to all employers with an Irish payroll obligation. ERR is a real-time reporting

Orla McConnell

regime for certain non-taxable items provided to employees.

Employers are required to notify Revenue "on or before" any of the following items are provided to an employee:

- Non-taxable travel and subsistence – vouched and unvouched;
- An incentive availing of the small benefit exemption; or
- The remote working allowance.

"It is important to be aware that this is likely to be phase one of ERR. It is anticipated that future phases will expand on the types of reportable information."

It is important to be aware that this is likely to be phase one of ERR. It is anticipated that future phases will expand on the types of reportable information.

The "on or before" reporting requirement is a major challenge for employers. Employers should review their expense reimbursement and benefits policies and determine the frequency of the reporting, e.g. if expenses are reimbursed weekly, ERR submissions are required weekly even if payroll is a monthly process.

The method of reporting is also proving challenging for employers. Revenue have made three facilities available to file ERR submissions:

- Manual filings – there are only likely to be relevant to smaller employers;
- Direct reporting – note that some payroll software providers are not offering this option; and
- File upload to ROS – this is the most common at present. Revenue require the uploaded file to be in XML or JSON format but a workable template to generate this type of file is not provided. There are solutions available in the market to assist but at an additional cost to employers.

In terms of the new guidance, Revenue have shared FAQ documents on their website to address topical issues, including where advance payments are made to employees for travel and subsistence. While this is welcomed, there are complexities and manual intervention is required. This might not be a long-term option for most employers.

Revenue have confirmed that a relaxed approach will be taken until 30 June 2024 which will involve supporting employers who are attempting to comply with their reporting obligations. During this period, Revenue will not intervene and will not seek to apply any penalties for non-compliance. It is key that employers demonstrate effort to comply with ERR during this period and should not just wait until 1 July 2024 to make their first submission.

Michelle Dunne, Director – Tax Employer Solutions, Grant Thornton: Since 1 January 2024 employers are required to notify Revenue of certain payments made to employees known

Michelle Dunne

as 'reportable benefits' which include vouchers or benefits provided under the Small Benefit Exemption, remote working tax-free allowance and travel & subsistence payments.

Revenue updated their Enhanced Reporting Requirements (ERR) Tax & Duty Manual Part 38-03-33 in March 2024 to include a new optional administrative practice for advance travel and subsistence payments. This new practice will be particularly relevant for employers providing advance payments to employees where those employees are undertaking business travel. Ordinarily, advance payments, regardless of reason, are subject to income tax, USC and PRSI at the point of payment to the employee however, subject to certain conditions, advance travel and subsistence payments may now be made without the application of tax via payroll.

"This new practice will be particularly relevant for employers providing advance payments to employees where those employees are undertaking business travel."

Under this administrative practice, the advance travel and subsistence payment may be treated as a tax free payment and reported under ERR at the time of payment. When the expense is incurred and the claim submitted by the employee, the employer will be required to update their ERR submission to record the actual travel and subsistence expense incurred.

The conditions that must be satisfied for this administrative practice to apply are as follows;

- The employer must have appropriate controls in place to track and reconcile all travel and subsistence advance payments.
- The advance travel or subsistence payment must be reported under ERR when the payment is made using a new subcategory of Travel and Subsistence.
- The travel or subsistence advance payment must be a reasonable estimate of the expected claim amount and must qualify for travel or subsistence relief.
- A claim for the actual travel or subsistence cost must be received by the employer without any undue delay, with the ERR submission subsequently updated in respect of this claim.
- Any excess in payment should be recouped by the employer without undue delay or subject to tax if not so settled.

Revenue are currently updating their software functionality to facilitate this practice, which is expected in May 2024.