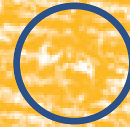
TAX SERVICES

Corporate Tax Services



New Tax Treatment of Headquarter and Holding Companies in Ireland

New Tax Treatment of Headquarter and Holding Companies in Ireland

A new type of holding company, the Irish holding company, has been announced. Multinational groups now have a new, attractive and flexible location in Ireland for their headquarter and holding companies. This is the latest addition to Ireland's range of favourable features for inward investment, these include the 12$^1/_2$% tax rate.

The new regime applies to all Irish companies.* A company can be entitled to this regime and be involved in manufacturing, shared services, financial services or any other activity in Ireland. Alternatively, the company can, simply, be a pure holding company.

The introduction of the new legislation for Irish headquarter and holding companies has removed or mitigated the main restrictions that previously hindered multinational companies from using Ireland as a holding company location. There is now a capital gains tax exemption for the sale of certain shareholdings and the tax treatment of dividends from outside Ireland has become significantly more generous.

The new regime takes effect from **2 February 2004**. Certain aspects of the rules are subject to Parliamentary approval in the Finance Act 2005; these changes will then be backdated to 2 February 2004.

"A new type of holding company, the Irish holding company, has been announced."

Capital gains tax exemption for Irish holding company on disposal of shares

The new regime provides for an exemption from tax on gains where an Irish holding company disposes of shares in another company (the 'investee' company) where, at the time of disposal, the following tests are met:

- **Residence test**
  The investee company is resident for tax purposes in Ireland, in another EU Member State or in a country with which Ireland has a tax treaty *(see Table 1)*;

- **Shareholding test**
  The holding company has held, directly or indirectly, for a period of at least 12 months ending in the previous 24 months, a minimum holding of 5% of the shares in the investee company. This test may be met by including shareholdings held by other members of the same, 51%, group; and

- **Trading test**
  The investee company is wholly or mainly a trading company or, taken together, the holding company and its, 5%, group and the investee company are wholly or mainly a trading group. For this test, the Irish meaning of 'trading' is complex. A company holding investments or assets passively would not be considered as trading. But, just because the activities are of a financial or investment nature does not mean that the company or group is not trading.

If a loss occurs, where a gain would have been exempt, the loss cannot be used to shelter other gains.

The tax exemption is extended to certain options and convertible securities that relate to shares. There is no exemption if the shares disposed derive the greater part of their value from Irish land, buildings, mineral or mining rights.

The exemption applies automatically. There is no claim, election or ruling required.

* The legislation applicable is in new sections 626B, 626C and new schedule 25A, and changes to schedule 24 of the Taxes Consolidation Act, 1997 as amended by the Finance Act, 2004.

Elimination of Irish tax on dividends received by Irish holding company

Dividends from one Irish tax-resident company to another are exempt from tax in the hands of the recipient.

Dividends received by an Irish company from a company resident in a country with which Ireland has a tax treaty or which is an EU country *(see Table 1)* may be sheltered by a tax credit for withholding or underlying taxes suffered; this is under either the terms of each particular treaty or the EU Parent/Subsidiary Directive.

Ireland has a system of unilateral credit relief for withholding and underlying tax suffered on dividends received from countries with which Ireland does not have a tax treaty. This relief also includes a credit for many state, local and municipal taxes suffered in countries with which Ireland has a tax treaty but which taxes are not covered by the treaty (for example, US state taxes).

The new holding company regime adds one major new feature to the Irish dividend credit system. Companies can now 'mix' credits for foreign tax on different dividend streams for the purpose of calculating the overall tax credit in Ireland (this is called 'onshore pooling'). Any excess credit unused can be carried forward indefinitely and offset in later years.

Since Irish tax is only payable on dividends actually received in Ireland, this allows companies great flexibility in allocating dividends from different periods and different countries to avoid any additional tax in Ireland.

This ability to onshore pool only requires a 5% shareholding (direct or indirect) in the dividend-paying company or that both companies are part of the same 5% group. The dividend-paying company can be tax-resident in *any* country.

In practice, many of Ireland's EU or treaty partners have tax rates higher than 25% and additional Irish tax on dividends is often not a real problem. An example of onshore pooling is given in *Table 2*.

Additional features of tax system making Ireland a key location

Ireland is a major centre for international trade, manufacturing and financial services. These activities are attracted by the many advantageous features of the Irish economy, its intra-EU location and its favourable taxation and flexible regulatory regimes. The Irish authorities constantly seek to enhance and add to these attractive features, which include:

- a 12½% tax rate for trading activities;
- Ireland's extensive tax treaty network with 42 countries *(see Table 1)*;
- favourable withholding tax treatments for dividends and interest paid from Ireland *(see Table 1)*;
- no 'controlled foreign company' (CFC) rules;
- no 'thin capitalisation' rules;
- tax deduction for funds borrowed in most cases (including situations where the new holding regime is availed of);
- a tax incentive regime for research and development (R&D) activities carried on in Ireland and the EU (plus Norway, Iceland and Lichtenstein);
- favourable income tax treatment for expatriates working in Ireland; and
- flexible VAT, capital duty and stamp duty (transfer tax) regimes.

The 12½% tax rate for trading activities is expected to remain the tax rate in Ireland for the foreseeable future. This tax rate has been approved by the EU Commission.

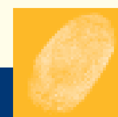
Table 1: Countries with which Ireland has a tax treaty

Generally, there is no interest or dividend withholding tax on interest or dividends paid by Irish companies to the following locations:

1	Australia	22	Lithuania
2	Austria	23	Luxembourg
3	Belgium	24	Malaysia
4	Bulgaria	25	Mexico
5	Canada	26	Netherlands
6	China	27	New Zealand
7	Croatia	28	Norway
8	Cyprus	29	Pakistan
9	Czech Republic	30	Poland
10	Denmark	31	Portugal
11	Estonia	32	Romania
12	Finland	33	Russia
13	France	34	Slovak Republic
14	Germany	35	Slovenia
15	Hungary	36	South Africa
16	India	37	Spain
17	Israel	38	Sweden
18	Italy	39	Switzerland
19	Japan	40	United Kingdom
20	Korea (Republic of)	41	United States of America
21	Latvia	42	Zambia

NOTE: Treaties have been signed but *not yet ratified* with Greece (Greece and Malta are the only members of the EU with which Ireland does not have a tax treaty) and Iceland.

Treaties are *under negotiation* with Argentina, Chile, Egypt, Malta, Morocco, Singapore, Tunisia, Turkey and Ukraine.



"An extensive tax treaty network."

Table 2: Example of Onshore Pooling

Dividend to Ireland from:	**USA**	**Bermuda***
Dividend	200	100
Underlying tax rate		
(including state taxes)	40%	0%
Dividend grossed up under Irish rules	267	100
Irish tax @ 25%	67	25
Underlying foreign tax actually suffered	133	0
Irish tax payable	0	25
"Gross" excess credit	66	0
"Net" excess credit	50**	
Sheltered by onshore pooling	0	25
Net Irish tax payable	**0**	**0**
Carry forward of excess	25	0

* The capital gains exemption is not available as Bermuda does not have a treaty with Ireland but a dividend credit (if required) and onshore pooling is available.

**Only 75% of the excess credit is available for pooling as the other 25% has already been utilised as a deduction.

New regime in practice – possible scenarios

Ireland as a headquarter location

- **US multinational company has a shared services centre (SSC) in Ireland.**
  The SSC can now be the European location for SSC activities, low-taxed financing activities, tax-enhanced R&D activities and be the holding company. The dividend policy can be set from Ireland to ensure no additional tax in Ireland and an optimised credit position in the USA.

- **US multinational company has a shared services centre (SSC) in the UK.**
  The UK company's profits are taxed at 30%. The US group holds its European operations under this UK company. The low tax rate in some of its eastern European locations is causing UK CFC problems.

  The SSC and the holding company activities are moved to Ireland. The 12 1/2% tax rate for the shared services activities is obtained and the new holding company regime is available. Ireland has no CFC rules.

Ireland as a holding company location

- **US multinational company has a Dutch holding company for its European operations.**
  Dividends paid to the USA by the Dutch holding company suffer a 5% withholding tax.

  The European operations are moved under a holding company in Ireland. There is no withholding tax on dividends from Ireland to the USA. The dividend policy can be set from Ireland to ensure no additional tax in Ireland and an optimised credit position in the USA.

- **Multinational company, ultimately held out of the Barbados.**
  It is having difficulty repatriating income and dividends to its parent company without suffering withholding taxes.

  The holding company of the group is migrated to Ireland.

"The new holding company regime can be coupled with the 12 1/2% tax rate."

1 November 2004

Disclaimer

The material in this guide is provided for general information purposes only and does not constitute professional advice. It is necessarily in a condensed form. It should not be regarded as a basis for ascertaining the liability to tax in specific circumstances. Readers are advised to seek professional advice with regard to their particular factual situation concerning specific tax or other matters before taking any decision or course of action.

Any review, retransmission, dissemination or other use of, or taking of any action in reliance upon this information by persons or entities other than the intended recipient is prohibited.

DUBLIN
Ernst & Young, Harcourt Centre,
Harcourt Street, Dublin 2, Ireland.

Telephone: +353 (0) 1 475 0555
Fax: +353 (0) 1 475 0599

Corporate Tax Services
David Smyth, Partner
Email: david.smyth@ie.ey.com

Dermot Clarke, Partner
Email: dermot.clarke@ie.ey.com

Joe Bollard, Partner
Email: joe.bollard@ie.ey.com

PJ Henehan, Partner
Email: pj.henehan@ie.ey.com

Eamonn O'Doherty, Partner
Email: eamonn.odoherty@ie.ey.com

Declan O'Neill, Partner
Email: declan.oneill@ie.ey.com

Donal O'Sullivan, Partner
Email: donal.osullivan@ie.ey.com

Kevin McLoughlin, Director
Email: kevin.mcloughlin@ie.ey.com

Aidan Walsh, Director
Email: aidan.walsh@ie.ey.com

NEW YORK
Ernst & Young, 5 Times Square,
New York, NY 10036

Telephone: +1 212 773 8744
Fax: +1 212 773 5583

Declan Gavin, Principal
Email: declan.gavin@ey.com

CORK
Ernst & Young, Stapleton House,
89 South Mall, Cork, Ireland.

Telephone: +353 (0) 21 427 7116
Fax: +353 (0) 21 427 2465

Frank O'Neill, Partner
Email: frank.oneill@ie.ey.com

Damian Riordan
Email: damian.riordan@ie.ey.com

GALWAY
Ernst & Young, Dock Gate,
Dock Road, Galway, Ireland.

Telephone: +353 (0) 91 530 600
Fax: +353 (0) 91 565 242

Jerry O'Leary
Email: jerry.oleary@ie.ey.com

LIMERICK
Ernst & Young, Barrington House,
Barrington Street, Limerick, Ireland.

Telephone: +353 (0) 61 319 988
Fax: +353 (0) 61 319 865

John Heffernan, Partner
Email: john.heffernan@ie.ey.com

WATERFORD
Ernst & Young, Annaville House,
Newtown, Waterford, Ireland.

Telephone: +353 (0) 51 872 094
Fax: +353 (0) 51 872 392

Paul Fleming
Email: paul.fleming@ie.ey.com

Ernst & Young is a professional services firm providing a range of services including accounting, auditing and taxation services. Ernst & Young is authorised by the Institute of Chartered Accountants in Ireland to carry out investment business in the Republic of Ireland.

www.ey.com/ireland/tax

© 2004 Ernst & Young.
All Rights Reserved.
Ernst & Young is
a registered trademark.