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Bridging opportunities

Ireland after US Tax Reform
What does it mean for business?

Ireland has an open, pro-business economy that offers significant opportunities to multinational companies, including as a gateway into the European market for US multinationals across all business sectors.

Ireland remains an attractive jurisdiction for multinationals

Ireland has a low headline corporate tax rate of 12.5% and offers an attractive holding company regime that provides an exemption from Irish tax on the sale of certain subsidiaries and advantageous tax treatment of foreign dividend income. Companies that develop intellectual property in Ireland may also be able to claim additional benefits, including tax relief on the acquisition of intangible rights, a significant R&D tax credit and a BEPS compliant patent box regime, under which eligible income may be taxed at a rate of 6.25%. Ireland also continues to provide a market leading platform which provides significant tax efficiencies for regulated investment funds, structured financings, securitisations and aircraft leasing.

In addition to its competitive tax system, Ireland offers access to the EU single market through a competitive regulatory and commercial framework within which to do business. These factors have made Ireland an attractive jurisdiction which many US multinationals have chosen to make an integral part of the structure of their European, and in some cases, global, operations.

Key elements of US Tax Reform

On December 22, 2017, the Tax Cuts and Jobs Act (the TCJA) was signed into law. The TCJA is the most substantial overhaul of the US Internal Revenue Code since 1986. The TCJA is far-reaching and significantly changes how the US taxes domestic businesses and multinational businesses.

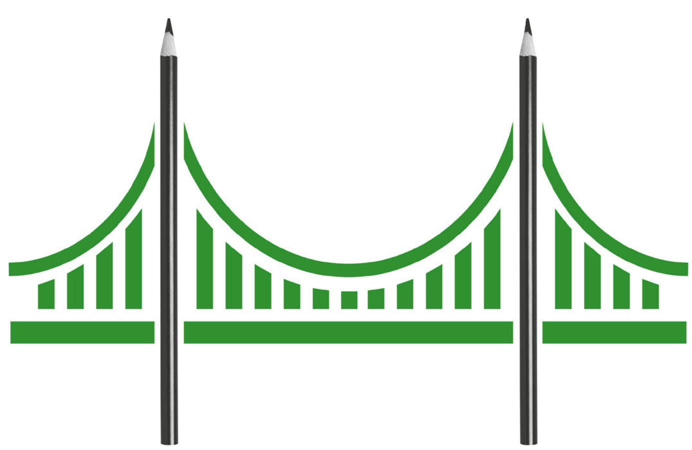
While the centrepiece of the TCJA is the reduction of the US corporate tax rate from 35% to 21%, the TCJA also adopted a number of significant changes to the way the US taxes multinational businesses that are relevant to US multinationals with operations or investments in Ireland.

The US is transitioning to a quasi-territorial system of taxation and so the repatriation of future non-US earnings should be exempt from US tax for 10% owned non-US corporations. In tandem, a mandatory one-time transition tax/deemed repatriation tax was introduced on previously untaxed accumulated earnings of certain non-US corporations at rates of 15.5% to the extent of cash/liquid assets and 8% on the remainder of such earnings.

Importantly, the US has adopted a new tax on global intangible low-taxed income (GILTI). GILTI is broadly defined and, notwithstanding its name, generally includes the net earnings of a US shareholder's controlled non-US subsidiaries in excess of a notional 10% return on the tax basis in the depreciable assets of non-US subsidiaries. In effect, this provision introduces an immediate US income tax liability for controlled foreign companies of US corporations and acts as a worldwide minimum tax on such earnings. Such US shareholders receive a deduction equal to 50% of their GILTI and, subject to applicable limitations, are able to claim foreign tax credits (FTCs) for 80% of the taxes paid by non-US subsidiaries in respect of such earnings. For a corporate US shareholder that can fully utilise its FTCs, if the GILTI is subject to local tax at a blended rate of less than 13.125%, it will be subject to residual US tax, while if the GILTI is subject to local tax at a blended rate of at least 13.125%, it generally will not be subject to residual US tax. Beginning in 2026, the amount of the deduction decreases from 50% to 37.5%, with the impact that the rate of tax at which a corporate US shareholder, that can fully utilise FTCs, will not be subject to residual US tax on GILTI, increases from 13.125% to 16.4%.

As a corollary to GILTI and incentive to retain activities domestically, the US adopted a deduction for US corporations equal to 37.5% of the corporations' foreign-derived intangible income (FDII).

FDII generally includes a portion of the income from sales of goods, services and intangibles to unrelated non-US parties based on the taxpayer's total US income in excess of a 10% return on the tax basis in the corporations' depreciable assets compared to its total income. The impact is that FDII is generally subject to an effective US rate of tax of 13.125%. Beginning in 2026, the amount the deduction decreases from 37.5% to 21.875%, with the impact that the effective US rate of tax on FDII increases to 16.4%. In theory, GILTI and FDII are intended to make US companies indifferent as to whether sales to non-US parties are made directly from the US or through a subsidiary in a lower taxed jurisdiction. The US also adopted several provisions intended to address perceived erosion of the US tax base. The US adopted a new limitation on the ability to deduct interest expense, generally limiting such deductions to 30% of adjusted taxable income. The US also adopted a new



base erosion and anti-abuse tax (BEAT). The BEAT is effectively a minimum tax for certain large taxpayers, which is computed disallowing the benefit of deductions for certain payments to related non-US parties, including for example, interest that is not otherwise disallowed under the new interest expense limitation and disallowing the benefit of FTCs, including with respect to GILTI. Thus, a taxpayer subject to the BEAT will owe residual US tax on GILTI regardless of the local taxes paid with respect to the earnings of its non-US subsidiaries.

Next steps?

The changes enacted by the TCJA are significant, therefore, multinationals should analyse the impact of these provisions on their existing structures. For US multinationals with operations or investments in Ireland, earnings from Irish operations could be subject to residual US tax as GILTI, particularly if the US parent corporation is limited in its ability to use FTCs or, if the earnings are subject to reduced rates under the patent box regime. That said, GILTI applies broadly and the combined rate of Irish tax and any residual US tax is still very competitive to other jurisdictions.

The deduction for FDII reduces the difference between the effective US rate of tax on qualifying income and the Irish rate of tax that would apply to the same income. However, companies may want to pause before moving operations to the US on this basis. The deduction for FDII is subject to challenge on trade law grounds, the effective rate of tax on FDII increases to 16.4% beginning in 2026 and any transfer of intangibles and/or operations may trigger significant local or US tax costs. In particular, the effective US tax rate available under FDII remains above Ireland's headline corporate tax rate of 12.5%. Companies may however want to look at restructuring their financing to take account of the impact the new restrictions on interest deductibility may have on existing debt/equity structures.

The base erosion measures described above could have an impact on investments into the US by Irish companies. However, as with GILTI, these provisions apply to all jurisdictions and, importantly, do not disadvantage Ireland relative to other jurisdictions.

In this respect Ireland can continue, and indeed enhance, its attractiveness as the jurisdiction of choice outside the US for locating outside US value. The core principles of many US/non-US operating models remains the same and there will be a continued requirement in many instances to have operations outside the US to service other markets. This is particularly the case in respect of intellectual property. Ireland has a favourable IP tax regime and continues to develop as one of the most attractive jurisdictions in which to hold non-US IP.

Concluding comment

In overview, the TCJA enacted significant changes that are relevant to US multinationals with operations or investments in Ireland. As noted, such multinational groups should work with their advisors to understand the impact of these provisions on them. However, in the final analysis, they are likely to discover that Ireland remains an extremely attractive jurisdiction for investment, being ideally placed as a gateway to do business both in Europe and beyond.

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