itm IRISH TAX MONITOR

The Roundtable August 2022

Debt vs Equity Finance

Can you please outline the tax advantage of using debt finance over equity finance? How is the EU's DEBRA directive attempting to level the playing field in this regard?

Yvonne Diamond, Senior Manager, Financial Services Tax, BDO: The main advantage of debt financing over equity financing, is the availability of a tax deduction for interest arising on the debt (subject to meeting the various requirements, and avoiding the many anti-avoidance provisions, in Irish tax law). The return on equity meanwhile, that is, profit distributions by way of dividends, are not tax deductible.

Yvonne Diamond

Of course, it is not always the case that debt financing provides a tax advantage. This is particularly the case for inter-company, cross-border debt, as the interest deduction in Ireland (at 12.5% if against trading profits) will in many cases provide a lower tax benefit than the tax cost of the interest receipt (i.e. when received in a foreign jurisdiction with a higher tax rate).

The DEBRA Directive aims to reduce the bias in the tax system in favour of debt financing over equity, by introducing an equity allowance, as well as an (additional) limitation on the deductibility of debt financing costs. The equity allowance provides a deduction based on new equity, multiplied by a notional interest rate, capped at 30% of EBITDA, and available for 10 years, while interest deductions are limited to 85% of the net interest expense.

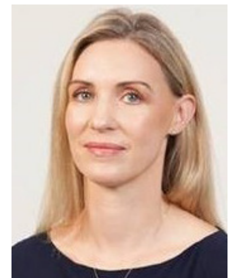
Ireland's Tax Treaty Policy

The Department of Finance recently outlined its Tax Treaty priorities and plans in a policy published on 27th June. Ireland's longstanding tax treaty policy has been to expand, maintain and enhance its tax treaty network, in order to remove barriers and facilitate trade and investment opportunities between Ireland and partner countries.
Can you please explain how Double Taxation Treaties can encourage trade and activity between countries and comment on Ireland's Tax Treaty Policy Statement?

Angela Fleming, Partner & Head of Financial Services Tax, BDO: The Tax Treaty Policy Statement published on 27th June was developed following a public consultation held in 2021.

As a small open economy, access to a comprehensive tax treaty network is pivotal to ensuring that Ireland can continue to maximise the benefits from the globalised economy. Double tax treaties can encourage trade and activity between countries by minimising withholding taxes, and supporting specific sectors of the economy and industry.

The policy statement acknowledges both the need to continue to enhance Ireland's tax treaty network, as well as focussing resources in order to maximise the potential benefit of prospective tax agreements. As a result, the following priorities were identified:


Angela Fleming

- Priority A – Have double tax agreements with all G20 members (currently Ireland has treaties with 16 G20 member counties). This would involve the expansion of Ireland's tax treaty network to include Argentina, Brazil and Indonesia.
- Priority B – Development of tax treaties with all current and accession OECD countries, and EU accession countries, including Argentina, Brazil, Colombia, Costa Rica and Peru.
- Priority C – Renegotiation and modernisation of some of Ireland's oldest tax treaties.
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The policy statement also sets out the core principles to be applied to Ireland's tax treaty policy with developing countries. Core to this policy is an undertaking not to approach any Least Developed Country (LDC). However, where Ireland it approached by an LDC, consideration will be given to negotiating a treaty with such country, following an analysis of the potential impacts and spillovers, and fully considering the preferences of the partner country regarding source taxation.

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