# Exit Tax Provisions

## Part 20-02-01

This document should be read in conjunction with sections 627 to 629C of the Taxes Consolidation Act 1997

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# Executive Summary [section 627 – 629C]

This manual provides an overview of the Exit tax rules that were introduced by Finance Act 2018 and came into effect from 10 October 2018. It sets out information in relation to:

1. The events which give rise to a charge to exit tax

2. Exclusions from the charge to exit tax

3. The rate of exit tax and the anti-avoidance provision

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## Introduction

Section 32 Finance Act 2018 replaces existing targeted anti-avoidance exit tax provisions in Chapter 2 of Part 20 of the Taxes Consolidation Act (TCA) 1997 with a new broad-based exit tax charge, as provided for in Article 5 of the Anti-Tax Avoidance Directive (ATAD). The new exit tax charge applies from 10 October 2018.

In concise terms, the new exit tax provisions tax unrealised capital gains where companies migrate or transfer assets offshore, without an actual disposal, such that they leave the scope of Irish tax, by deeming a disposal to have occurred.

The charge will not apply to assets that remain within the charge to Irish CGT. Such assets include land, minerals or mineral rights, or shares that derive their value or the greater part of their value from such assets. Additionally, the charge will not apply to assets which continue to be used in Ireland by a permanent establishment of the company after the company migrated or to asset transfers which relate to the financing of securities, assets given as collateral or where the asset transfer takes place to meet prudential capital requirements or for liquidity management and such assets are to revert to the Member State of the transferor company within 12 months.

The rate of exit tax is 12.5%. An anti-avoidance provision is included to ensure that a rate of 33% rather than 12.5% applies if the exit forms part of a transaction to actually dispose of the asset and the purpose of the exit is to ensure that the gain is charged at the lower rate.

# 1 Charge to exit tax [section 627(2) – 627(3)]

## 1.1 Events which give rise to a charge to exit tax

**Section 627** imposes an exit tax charge with effect from 10 October 2018.

The exit tax charge applies where:

- an EU-resident company transfers assets from its permanent establishment in Ireland to its head office or to a permanent establishment in another country,
- an EU-resident company transfers the business carried on by its permanent establishment in Ireland to another country, or
- an Irish-resident company transfers its residence to another country.

**Section 627(3)** provides an exclusion from the exit tax charge where Ireland retains taxing rights on a subsequent disposal of the assets. Such assets include land, minerals or mineral rights or shares (other than shares quoted on a stock exchange) that derive their value or the greater part of their value directly or indirectly from such assets or assets of an overseas life assurance company which were held in connection with the life business carried on by the company which, at or before the time the chargeable gains accrued, were used or held by or for the purposes of that company's branch or agency in this country.

It is worth noting that Article 5 of the ATAD also covers a situation where an EU-resident company transfers assets from its head office in Ireland to a permanent establishment in another country. However, as the exit tax charge only applies in situations where Ireland loses its right to tax the assets, this aspect of Article 5 was not required to be implemented in Irish legislation as it can have no application.

## 1.2 Exit tax charge

A disposal and reacquisition of the relevant assets is deemed to have occurred on the happening of any the events referred to above. This results in a charge to tax in respect of any chargeable gains which may have accrued in respect of the assets. Normal CGT rules apply in calculating the amount of the exit tax charge which is based on the market value of the assets at the time of the deemed disposal.

In the context of exit tax, the term "market value" means the amount for which an asset can be exchanged or mutual obligations can be settled between unconnected willing buyers and sellers in a direct transaction.

For the purposes of imposing an exit tax charge in respect of deemed disposals by non-resident companies, **section 29(3)(c) TCA 1997** (assets associated with a trade carried on in Ireland by a non-resident person through a branch or agency) applies as if the reference in that paragraph to a trade were to a business and as if the references to a branch or agency were to a permanent establishment.

## 1.3 Exit tax and losses

As exit tax operates within the framework of the Capital Gains Tax Acts:

- capital losses arising on a deemed disposal of assets can be offset against gains arising on a deemed disposal of assets on an exit tax event,
- net losses arising on an exit tax event remain available for offset against chargeable gains on an exit tax event in the period concerned or any subsequent period,
- a capital loss arising on a non-exit event in a previous period can be used to offset exit tax gains. Such a loss can be offset against gains chargeable at the 33% rate and, in so far as they cannot be deducted from gains chargeable at that rate, from gains chargeable at the exit tax rate of 12.5%,
- certain trading losses can be offset on a value basis under **section 396B** against chargeable gains arising on the exit tax event,
- certain losses can be offset by means of group relief on a value basis under **section 420B** against chargeable gains arising on the exit tax event,
- current period trading losses **cannot** be offset under **section 396 or 396A** against chargeable gains arising on an exit tax event. Group relief for certain losses **cannot** be offset under **section 420 or 420A** against chargeable gains arising on an exit tax event.

The position outlined above regarding losses is subject to the rule in **section 555** that the amount of the CGT loss is restricted by the amount of capital allowances granted.

## 1.4 Exit tax and section 626B

It should be noted that the substantial shareholding exemption in **section 626B does not apply** to a deemed disposal arising under **section 627** by virtue of **subsection (3)(e)** of **section 626B**.

## 1.5 Examples of the charge to exit tax

Examples of how the exit tax will apply in practice are set out below.

**Example 1**

An EU resident software services company with an Irish branch decided to shut down the branch in Ireland and transfer its business operations to its EU head office. The long leasehold Irish property held by the branch will be sold by the company once the space is vacated and the business relocation is complete.

Various assets held by the Irish company will be transferred/allocated to head office including intangible assets consisting of a brand name and software used in the course of the trade carried on by its Irish permanent establishment.

The software transferred to head office consists of two sets of software rights. One asset (asset 1) was purchased by the branch from an international group member for its market value of €1m. The value of this asset has decreased over time such that its market value at the date of transfer is €300,000. Capital allowances under section 291A TCA 1997 have been granted in respect of this asset.

Another software asset (asset 2) was also purchased from an international group member for its market value of €100,000 has been subject to considerable development effort by the branch. The R&D costs expended by the branch on developing the asset are considered to be of a revenue nature and have not formed part of the base cost of the asset for CGT purposes. The market value of this software asset at the date of the transfer is €2m.

The brand name was purchased by the permanent establishment in 2008 for €500,000. There was no entitlement to capital allowances in respect of expenditure on the asset as the expenditure was incurred prior to the introduction of section 291A. The market value of the brand at the date of reallocation has reduced to €100,000.

The exit tax charge is calculated as follows:

Irish leasehold property – no deemed disposal as the asset remains within the charge to Irish tax and will be chargeable to tax when the leasehold interest is ultimately sold by the company.

| | | |
|---|---|---|
| Software (asset 1) | € | € |
| Market value | 300,000 | |
| Base cost | (1,000,000) | |
| Loss on deemed disposal | *(700,000) | |
| *No loss available for offset due to capital allowances | | |
| Software (asset 2) | | |
| Market value | 2,000,000 | |
| Base cost | (100,000) | |
| Gain on deemed disposal | | 1,900,000 |
| Brand name | | |
| Market value | 100,000 | |
| Base cost | (500,000) | |
| Loss on deemed disposal | | (400,000) |
| Net gain | | 1,500,000 |
| Exit tax at 12.5% | | 187,500 |

**Example 2**

An Irish resident pharmaceutical company migrates residence to a non-EU state. The company continues manufacturing activities through a permanent establishment in Ireland. Certain of the patent rights with a market value at the date of transfer of €1.5m (originally acquired from a group member for €1.3m) will be allocated to the new head office located outside Ireland and will be exploited there. Capital allowances have been granted on the cost of the patent rights in accordance with section 291A TCA 1997.

The company moved premises in the past and incurred a capital loss of €150,000 on the disposal of the land and building to a third party which has been carried forward.

The exit tax charge is calculated as follows:

Patents and other business assets used by the permanent establishment for the purposes of its trade – no exit tax charge by virtue of section 627(6) TCA 1997.

| Patent rights transferred overseas | € | € |
|---|---|---|
| Market value | 1,500,000 | |
| Base cost | (1,300,000) | |
| Gain on deemed disposal | | 200,000 |
| Capital loss carried forward | | (150,000) |
| Net gain | | 50,000 |
| Exit tax at 12.5% | | 6,250 |

# 2 Exclusions from the charge to exit tax [section 627(3), (5), (6) and (7)]

## 2.1 Ireland retains taxing rights

As noted above, **section 627(3)** provides an exclusion from the exit tax charge where Ireland retains taxing rights on a subsequent disposal of the assets. Such assets include land, minerals or mineral rights or shares (other than shares quoted on a stock exchange) that derive their value or the greater part of their value directly or indirectly from such assets or assets of an overseas life assurance company which were held in connection with the life business carried on by the company which, at or before the time the chargeable gains accrued, were used or held by or for the purposes of that company's branch or agency in this country.

**Section 627(3)(d)** re-affirms that in circumstances where an actual gain would remain within the scope of Irish capital gains tax because the assets in question are relevant assets as defined in section 29 TCA 1997, the exit tax will not apply.

## 2.2 Roll-over relief

Roll-over relief under **section 597** is not available in respect of assets disposed of before the migration of a company and replaced afterwards. This will be of relevance to certain taxpayers who made claims under the previous roll-over relief regime.

An exception from the exit tax charge applies where the assets of the company that migrated continue to be used in Ireland by a permanent establishment of the company after it migrated. Roll-over relief continues to apply to such situations.

## 2.3 Assets which continue to be used in the State

**Section 627(6)** provides that the charge to exit tax will not apply to assets which continue to be used in Ireland for the trade of a permanent establishment of the company after the company migrated.

## 2.4 Temporary transfers of assets for specific purposes

An exclusion from exit tax is provided for in **section 627(7)** in the situations referred to in Article 5(7) of the Directive, for example, assets related to the financing of securities or where the transfer of assets takes place in order to meet prudential capital requirements and such assets are to revert to the Member State of the transferor company within 12 months.

# 3 Rate of exit tax and anti-avoidance [section 627(4)]

## 3.1 Rate of exit tax on a deemed disposal

Exit tax is charged at the rate of 12.5%.

## 3.2 Anti-avoidance rule

However, the legislation includes an anti-avoidance provision to ensure that a rate of 33% rather than 12.5% will apply if the event that gives rise to the exit tax charge forms part of a transaction to dispose of the asset and the purpose of the transaction is to ensure that the gain is charged at the lower rate.

In this regard, the term “transaction” has the same meaning as it has in **section 811C**, i.e. any transaction, action, course of action, course of conduct, scheme, plan or proposal, any agreement, arrangement, understanding, promise or undertaking, whether express or implied and whether or not enforceable or intended to be enforceable by legal proceedings, and any series of or combination of these.

The scenario envisaged where a 12.5% rate will apply is a transfer of a company’s or permanent establishment’s, assets or operations to another jurisdiction to carry on activities in that other jurisdiction, which is not intended at the time of the exit event to result in a subsequent actual disposal of the assets.

The risk identified to which the anti-avoidance provision applies is the scenario whereby a company migrates residence or a permanent establishment in Ireland transfers assets or its business for the purpose of actually disposing of an asset, in a zero or low CGT jurisdiction, to attract the 12.5% rate which applies on exit, rather than the 33% which applies on actual disposals. In other words, to distinguish between an exit event which occurs for commercial reasons and a tax avoidance strategy to avoid the 33% rate on an actual disposal outside this country. The intention/motive of the taxpayer at the time of exit is the relevant factor. If the purpose of the exit is to avoid a 33% rate on an actual disposal, then that rate will apply.

## 3.3 Illustrative examples related to commercial restructurings

The commercial context for business restructuring events occurring within corporate groups involves balancing a complex range of factors including consideration of where best to hold and exploit assets. Restructuring to achieve improved commercial outcomes can trigger exit tax events and could be motivated by either external or internal factors.

It is suggested that, based on the fact patterns as described in the examples below, the anti-avoidance provisions should not apply so as to treat the exit event as a transaction whose purpose was to ensure the application of the 12.5% exit tax rate instead of the standard rate of capital gains tax to the asset disposal.

**Example 3**

A medical devices group identifies an opportunity to adapt a delivery mechanism already developed for one of its products for use in other new products. The rights to the mechanism are held by an Irish resident company. Its Irish subsidiary exploits the product in the course of its Irish trading activities of manufacturing and distributing the product.

The new product will be developed for use by a Swiss group member. The group decides that the Irish company owning the rights to the delivery mechanism will become resident in Switzerland. An exit tax event arises under section 627(2)(c) and exit tax is payable at 12.5% on a gain arising on the deemed disposal of the intangible asset rights by the Irish company when it ceases to be Irish resident and becomes Swiss resident.

The intangible asset rights to use and exploit the delivery mechanism for the current product range will continue to be licenced by the now Swiss resident company to the Irish manufacturing company.

The now Swiss resident company continues to develop the rights for use in new products and to facilitate the protection of rights to the adapted delivery mechanism for use by other group members who will manufacture and distribute the new product. This development work includes the conduct of Phase I clinical trials using the device under development. The trials produce very positive results and following the publication of the results a number of months later, a third party makes an offer to purchase outright the rights to the delivery mechanism under development.

The group evaluates the purchase offer and decides to sell the rights. The (former Irish resident) Swiss resident company sells to the third party all of its rights to the development stage of the new delivery product.

It is not considered that this future disposal by the former Irish resident company forms part of a transaction to dispose of the asset such that the purpose of the exit transaction is to ensure that the chargeable gain on a deemed disposal is charged at 12.5% rather than at the 33% standard rate of capital gains tax. At the time the company migrated residence, the sale of the rights to the third party company was not contemplated.

**Example 4**

A US parented multinational is engaged in the delivery of software as a service and software products on a global scale. The Irish subsidiary of the group holds the rights to an operating platform that supports the group's services outside the US.

As part of centralising the development of the platform for existing services to European customers (which requires continuing upgrade and development in order that the services supported by the platform continue to be competitive), the Irish company transfers residence to an EU Member State where it continues to develop the platform for European customers. An exit tax event arises under section 627(2)(c) and exit tax is payable on a gain arising on the deemed disposal of the intangible asset rights by the Irish company when it ceases to be Irish resident.

The now EU resident company uses the platform to deliver services to its customers.

The US parent identifies an opportunity to broaden the scope of its software as a service offering by entering into a joint venture with a US based third party which can offer data warehouse facilities for customers in the US and Europe. This will require building a new delivery platform interlinked with the platform of the data warehouse provider which is located in the US.

The group selects a range of software products which will be moved to this new digital delivery environment. The EU resident company sells its rights to the selected products and software platform to the US group member which will lead the joint venture development with the US based data warehouse provider.

It is not considered that this future disposal by the former Irish resident company forms part of a transaction to dispose of the asset such that the purpose of the exit transaction is to ensure that the chargeable gain on a deemed disposal is charged at 12.5% rather than at the 33% standard rate of capital gains tax. At the time the migration took place to centralise the development of the European platform, the opportunity for the joint venture for these assets had not been identified.

## 3.4 Mitigation of double taxation

**Section 620A** provides that an exit charge applies in relation to an asset which ceases to be chargeable to CGT because it becomes situated outside Ireland and in respect of which relief was granted under **section 615, 617** or **620**. Where an exit tax charge arises under both **section 620A** and **section 627**, the charge under **section 620A** will take precedence.

## 3.5 Value of certain assets to be accepted for the purposes of the Capital Gains Tax Acts

**Section 628** gives effect to Article 5(5) of the Directive. It provides that, where exit tax is charged in another Member State in respect of an asset by virtue of Article 5(1) of the Directive, the value of the asset established under the law of that Member State for the purposes of the exit tax charge will be accepted as the acquisition cost of that asset in Ireland unless that value does not reflect the market value of the assets.

Where an exit tax event arises in another Member State under an exit tax regime that complies with the Directive, the tax charged on such an exit tax event will be considered to have been charged by virtue of Article 5(1) of the Directive.

# 4 Deferral of exit tax [section 629 and 629A]

## 4.1 Availability of option to defer and the instalment dates

**Section 629** provides that a taxpayer can defer the payment of exit tax by paying it in instalments over 5 years. The first instalment will be due and payable on the specified date and the remaining instalments will be due and payable on each of the next anniversaries of the specified date. The specified date means -

- as regards corporation tax, the last day of the period of 9 months starting on the day immediately following the date of the event that gave rise to the exit tax charge, but in any event not later than day 23 of the month in which that period of 9 months ends, or
- as regards capital gains tax payable in respect of a year in which the exit charge arises, 31 October in the following year.

The deferral option will not be available in respect of assets which have been transferred to a third country unless that country is a party to the EEA Agreement and has concluded an agreement with this country or the EU equivalent to the mutual assistance provided for in Council Directive 2010/24/EU of 16 March 2010.

## 4.2 Requirement for an election and annual statements

An election to pay tax by instalments or on a disposal of assets must be made in the company's tax return. The return must be made electronically and specify:

- the date the company ceased to be resident in this country,
- the EU/EEA territory where the migrated assets were transferred,
- the amount of tax,
- the deferral option the company is electing to make, and
- any other information that Revenue may require for the purposes of the section.

Irrespective of the type of election made by a company, the company is obliged to make, without being notified to do so, an annual statement to Revenue specifying whether the company is treated as tax resident in a relevant territory (i.e. an EU Member State other than the State or a third country which is party to the EEA Agreement that has concluded an agreement with the State or the European Union equivalent to the mutual assistance provided for in Council Directive 2010/24/EU of 16 March 2010) throughout the period covered by the return.

In the case of companies electing to pay tax by instalments, annual statements are due within 21 days of the end of each of the 5 calendar years following the event giving rise to the charge to tax under **section 627(2)**.

Companies electing to pay tax on the disposal of assets are required to supply the following additional information in their annual statement:

- whether any tax became due and payable during the relevant period,
- the amount of tax, interest and whether the tax and interest has been paid, and
- the computation of such tax liability.

## 4.3 Triggers for immediate payment

Any tax which has not been paid at the time of the relevant event and any interest charged on that tax will become due and payable on the occurrence of the following events:

(a) the assets referred to in **section 627(2)** are sold or otherwise disposed of;
(b) the assets referred to in **section 627(2)** are transferred to a third country,
(c) the company ceases to be resident in a Member State and becomes resident in a third country or the business carried on by a permanent establishment of the company is transferred to a third country;
(d) the company becomes insolvent or a liquidator is appointed to the company; or
(e) the company fails to pay the instalments on the due date and this failure has not been rectified within 12 months of that date.

The references in paragraphs (b) and (c) to a third country do not include reference to a third country that is a party to the EEA Agreement if it has concluded an agreement with the State or the European Union equivalent to the mutual assistance provided for in Council Directive 2010/24/EU of 16 March 2010.

## 4.4 Interest

Simple interest is payable on outstanding tax and is due and payable at the same time as that tax is due and payable.

## 4.5 Tax on non-resident company recoverable from another member of group or from controlling director

Provision is made in **section 629** for a guarantee where there is a risk of non-recovery of tax. However, an exclusion from the provision of a guarantee applies where the tax debt can be recovered from another Irish resident company which is a member of the same group or from an Irish resident controlling director.

**Section 629A** provides that exit tax payable by a non-resident company can be recovered from another member of a group of companies or from a controlling director.
The collection procedure is initiated (generally within 3 years of the due date for the making of the return by the defaulting company) by the inspector:

- serving a notice on the Irish resident group company or controlling director,
- stating the amount of tax outstanding, and
- requiring payment within 30 days,

if the tax is not paid within 6 months of the return date.

It is sufficient for the relationship to the defaulting company to have existed at any time within the 12-month period preceding the gain.

Any amount which a person is required to pay by a notice under the section may be recovered from the person as if it were tax due by that person. That person can recover any such amount paid on foot of a notice under the section from the taxpayer company.

A payment made on foot of a notice under the section will not be allowed as a deduction in computing income, profit or losses for any tax purposes.

# 5 Transitional provision and miscellaneous [section 629B and 629C]

**Section 629B** contains transitional provisions to ensure that Revenue's power to serve notice under the former section 629 is not affected by the new provisions.

**Section 629C** restates the previous section 629A, which relates to companies ceasing to be resident in the State on formation of an SE (a European public liability company) or an SCE (a European Cooperative Society). Such companies will be deemed to continue to be resident in the State or, if the company has ceased to exist, as if the SE or SCE were the company for the purposes of liabilities accruing or matters arising before the date of cessation.