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SWEET & MAXWELL

A Case Study in Arcane But Impactful Tax Administration: Ireland and Withholding Tax on Patent Royalties in 2010

Emer Hunt[*]

Abstract

This paper examines the genesis of a relief from withholding tax (WHT) on patent royalties introduced in Ireland in 2010. A legislative relief from WHT was introduced in February 2010 and a more expansive administrative relief (through an administrative statement of practice) was introduced in July 2010. Data obtained from the Irish Department of Finance (Finance) and the Revenue Commissioners (Revenue) under freedom of information (FOI) legislation provides some information on the reasons for introducing the two-pronged abolition of WHT on outward bound patent royalties and the importance of maintaining a competitive position for Ireland while, at the same time, protecting its reputation in the international tax landscape. The importance of patent royalties as a mechanism to shift profits internationally is examined within the context of Ireland being an important destination for foreign direct investment (FDI) and a focus of international tax planning. The administrative abolition of WHT is analysed as a possible example of executive rule-making and the Irish constitutional requirement for the separation of powers is considered. Finally, some conclusions are drawn about the malleability of statutory interpretation by the executive and how this might reflect on Irish legal culture.

Introduction and background

States can utilise their sovereignty in tax matters to construct a tax offering which will be attractive to peripatetic taxpayers.[1] As a statement of fact, this is unproblematic but is also under attack from international attempts to curb sovereignty in the area of tax, initiated by both the Organisation for Economic Co-operation and Development (OECD) and the European Commission.[2] The role of states as "procurer of profit shifting from other jurisdictions where companies' real economic activity takes place" has been viewed as more important than framing tax avoidance as something involving taxpayers.[3] Tax competition is not limited to setting low rates, but is an interdependent setting of tax rates and tax base, or strategic interaction with other states.[4] It involves states vying

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[1] Ronen Palan, "Tax Havens and the Commercialization of State Sovereignty" (2002) 56 *International Organization* 151; Tsilly Dagan, "The Marketization of Tax Sovereignty" in J. Cohen et al (eds), *Forms of Pluralism and Democratic Constitutionalism* (Cambridge: CUP, 2018).

[2] Sebastian Beer, Ruud de Mooij and Li Liu, "International Corporate Tax Avoidance: a Review of the Channels, Magnitudes, and Blind Spots" (2020) 34 *Journal of Economic Surveys* 660.

[3] Alex Cobham, "Procuring Profit Shifting: The State Role in Tax Avoidance" in P. Alston and N. Reisch (eds), *Tax, Inequality, and Human Rights* (Oxford: OUP, 2019), p.137.

[4] Michael P. Devereux and Simon Loretz, "What do we know about corporate tax competition?" (2013) 66 *National Tax Journal* 745.

for mobile assets and activities through de-regulation and de-taxation.[5] For their part, multinational enterprises (MNEs) operate in a competitive environment comprising a global market and state taxes or, put otherwise, "[m]arkets ignore political borders: taxes vary with them".[6] MNEs game the legal rules governing cross-border activity and there is evidence for the sensitivity of MNE behaviour to corporate tax considerations.[7]

Thus, while the current instability of the international tax system is well-known as a product of the symbiotic relationship between states and MNEs, the mechanics of how states compete to provide a benign tax environment are sometimes lacking in transparency.[8] Changes to state behaviour mandated by the European Union (EU) and OECD include the adoption of the automatic exchange of information on bank accounts and on tax rulings, the partial publication of MNEs' country-by-country reports, the adoption of anti-avoidance measures as part of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), and the proposals for income allocation and a global minimum tax on the profits of large MNEs. In this way, the focus of supranational organisations such as the OECD and the EU is on inculcating standards of transparency in the international tax system and curtailing the power of the state to compete in order to attract the tax revenues of MNEs. Yet competitive tax measures can sometimes be submerged in the interstices of the national legal system, reliant on a tacit knowledge of how the law operates and the levers to pull to resolve ambiguity or even to overcome an unhelpful, albeit long-standing, interpretation. The detail of jurisdictional rules can be hidden under broad regulatory standards generated by supranational organisations, and details of how states construct their tax offerings are deeply embedded in a specific legal culture.[9] Searching for tax culture is seeking to identify the "the body of beliefs and practices that are shared by tax practitioners and policy-makers in a given society and that provide the background or context in which tax decisions are made".[10] A note of early warning on this point: the incompleteness of the freedom of information (FOI) data may make a search for tax culture quite illusory.

Furthermore, the interaction of the jurisdictional tax systems with each other and with MNEs is often described from the viewpoint of economists or political scientists who, understandably,

[5] Philipp Genschel and Laura Seelkopf, "The Competition State: The Modern State in a Global Economy" in Stephan Leibfried et al (eds), *The Oxford Handbook of Transformations of the State* (Oxford: OUP, 2015).

[6] D.A. Shackelford and T. Shevlin, "Empirical tax research in accounting" (2001) 31 *Journal of Accounting and Economics* 360.

[7] Ruud A. De Mooij and Sebastian Ederveen, "Taxation and foreign direct investment: a synthesis of empirical research" (2003) 10 *International Tax and Public Finance* 673; Ruud A. de Mooij and Sebastian Ederveen, "Corporate tax elasticities: a reader's guide to empirical findings" (2008) 24 *Oxford Review of Economic Policy* 680.

[8] Thomas Rixen, "From double tax avoidance to tax competition: Explaining the institutional trajectory of international tax governance" (2011) 18 *Review of International Political Economy* 197; Philipp Genschel and Peter Schwarz, "Tax competition: A literature review" (2011) 9 *Socio-Economic Review* 339.

[9] Michael A. Livingston, "Law, Culture, and Anthropology: On the Hopes and Limits of Comparative Tax" (2005) 18 *Canadian Journal of Law & Jurisprudence* 119; Victor Thuronyi and Kim Brooks, *Comparative Tax Law* (Alphen aan de Rijn, the Netherlands: Kluwer Law International BV, 2016); M. Van Hoecke and M. Warrington, "Legal cultures, legal paradigms and legal doctrine: towards a new model for comparative law" (1998) 47 *International & Comparative Law Quarterly* 495.

[10] Livingston, "Law, Culture, and Anthropology: On the Hopes and Limits of Comparative Tax" (2005) 18 *Canadian Journal of Law & Jurisprudence* 119, 121.

do not focus on the legal mechanisms underpinning state tax competition.[11] This paper examines state competition by reference to a specific example within a legal context: the two-pronged relaxation by Ireland, in February and July 2010, of WHT obligations on outward bound payments of certain patent royalties by corporate taxpayers. This led to a situation where no WHT was levied on any outbound patent royalty, irrespective of the location of the recipient.

The remainder of this paper is organised as follows. First, the importance of patent royalties as a component in the recent history of international tax planning is explored against the backdrop of state competition for mobile tax revenues of MNEs. Secondly, details of the Irish change in WHT rules in 2010 are explained. This includes a review of parliamentary debates on the legislation of February 2010 and recourse to data obtained under FOI requests to Finance and Revenue to trace the introduction of the two-pronged relief from WHT in 2010. Thirdly, the Irish constitutional embargo on rule-making by the executive is explored as an element of separation of powers, together with an analysis of any residual discretion enjoyed by Revenue to amend or expand a tax relief. Finally, the paper concludes with a discussion on the lack of transparency of the administrative relief from WHT on patent royalties; the damage an administrative ruling of such magnitude does to the separation of powers in Ireland; and, within an international tax context, the state's motive in wishing to craft a tax offering to cut out a corporate intermediary in another member state.

The importance of patent royalties in international tax planning involving Ireland

Corporate patents are important assets of MNEs and royalties are returns on licences to use or exploit patents.[12] Patents, like other intellectual property (IP), have a remarkable versatility, useful in tax planning for two reasons: first, due to their commercial value and secondly, because of their mobility.[13] The location and exploitation of IP has long been a well-trodden path to shift profits from one taxing jurisdiction to another.[14] There is evidence that IP is strongly implicated in tax avoidance structures adopted by MNEs.[15] The quantification of profits attributed to Ireland illustrates the importance of the issue. Tørsløv et al trace the profits of MNEs shifted through states: in 2015 US$100 billion profits were shifted through Ireland.[16] Coffey analyses a shift in destination of outbound royalties from Ireland after 2013: until then "relatively modest" amounts were paid to offshore financial centres but thereafter it increased rapidly because, posits Coffey,

[11] Peter Dietsch, *Catching Capital: The Ethics of Tax Competition* (Oxford: OUP, 2015); M. Keen and K.A. Konrad, "The theory of international tax competition and coordination" in A.J. Auerbach et al (eds), *Handbook of Public Economics* (Amsterdam, the Netherlands: Elsevier, 2013).

[12] Tom Karkinsky and Nadine Riedel, "Corporate taxation and the choice of patent location within multinational firms" (2012) 88 *Journal of International Economics* 176.

[13] Rachel Griffith, Helen Miller and Martin O'Connell, "Ownership of intellectual property and corporate taxation" (2014) 112 *Journal of Public Economics* 12; Beer et al, "International corporate tax avoidance: a review of the channels, magnitudes, and blind spots" (2018) *Journal of Economic Surveys* 660.

[14] For a description of the flow of royalties from Ireland to Bermuda, see Nadine Riedel, "Quantifying international tax avoidance: a review of the academic literature" (2018) 69(2) *Review of Economics* 169.

[15] Thomas Tørsløv, Ludvig Wier and Gabriel Zucman, "The missing profits of nations" (2023) 90(3) *The Review of Economic Studies* 1499.

[16] Tørsløv, Wier and Zucman, "The missing profits of nations" (2023) 90(3) *The Review of Economic Studies* 1499, 1517.

of a change in Ireland WHT rules on payments to non-treaty jurisdictions.[17] Moreover, the available data shows that almost all royalties paid from Ireland to the euro area went to the Netherlands.[18]

Ireland has been enormously successful in gaining a disproportionate level of FDI.[19] It is also home to a large number of MNEs, particularly from the United States (US).[20] Public discourse in the US and elsewhere concentrated on the so-called "Double Irish Dutch Sandwich", which recognised revenue in Ireland through the use of two Irish-incorporated companies and an intermediary company in the Netherlands to avoid WHT on outbound patent royalties.[21] The mechanism for attributing profits to Ireland, a low-tax jurisdiction, is the subject of continuing legal scrutiny at EU level of the application of state aid rules to tax rulings from Revenue to Apple.[22] Domestic tax rules governing attribution of income and deductibility of expenses, combined with any tax fetters on outward bound payments, are important components of a jurisdiction's tax offering.[23] Restricting source state taxation is of acute interest to MNEs engaged in cross-border income shifting and thereby becomes an important component of a state's tax offering.[24] When two themes—tax competition by states and tax avoidance by MNEs—are examined together, they collide in the realm of WHT on outbound patent royalties. Ireland exemplifies these interactions in its 2010 changes to WHT.

The rights of the source state to levy WHT on outbound payments, such as interest and royalties, has been a feature of double tax agreements since their inception in the early 20th century. Initially seen as a means of providing the source state with a taxing entitlement, WHT on interest, royalties and dividends came under pressure as a fetter on international investment.[25] Brauner notes that the clear trend, led by the OECD, has been to eliminate withholding taxes.[26] The EU viewed WHT on intra-group interest and royalties as an obstacle to the internal market.[27] Imposing

[17] Seamus Coffey, "The Changing Nature of Outbound Royalties from Ireland and their Impact on the Taxation of the Profits of US Multinationals" Working Paper 2021.
[18] Coffey, "The Changing Nature of Outbound Royalties from Ireland and their Impact on the Taxation of the Profits of US Multinationals" Working Paper 2021.
[19] Frank Barry, "FDI and the host economy: a case study of Ireland" in Giorgio Barba Navaretti and Anthony J. Venables (eds), *Multinational Firms in the World Economy* (New Jersey: Princeton University Press, 2020); Sheila Killian, "Where's the harm in tax competition?" (2006) 17 *Critical Perspectives on Accounting* 1067.
[20] Barry, "FDI and the host economy: a case study of Ireland" in Navaretti and Venables (eds), *Multinational Firms in the World Economy* (2020).
[21] Fiscal Affairs Department, *Fiscal Monitor, Taxing Times* (International Monetary Fund, 2013); Gabriel Zucman, "Taxing across Borders: Tracking Personal Wealth and Corporate Profits" (2014) 28 *The Journal of Economic Perspectives* 121; Emer Hunt, "(Un)fairness as an irritant to the legal system: the case of two legislatures and more multinational enterprises" in Peter Harris and Dominic de Cogan (eds), *Tax Policy* (Oxford: Hart Publishing, 2020).
[22] Ruth Mason, "The Advocate General's Opinion in Apple: Two Steps Forward, One Step Back" (2023) 112 *Tax Notes International* 1315.
[23] Beer et al, "International Corporate Tax Avoidance: a Review of the Channels, Magnitudes, and Blind Spots" (2020) 34 *Journal of Economic Surveys* 660.
[24] Scott Dyreng and Michelle Hanlon, "Tax avoidance and multinational firm behavior" in C. Fritz Foley, James R. Hines Jr and David Wessel (eds), *Global Goliaths: Multinational Corporations in the 21st Century Economy* (Washington DC: Brookings Institution, 2021).
[25] John Avery Jones, "The David R. Tillinghast Lecture—Are Tax Treaties Necessary" (1999) 53 *Tax Law Review* 1.
[26] Yariv Brauner, "What the BEPS" (2014) 16 *Florida Tax Review* 55.
[27] Directive 2003/49 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States [2003] OJ L157/49. For a critique of the abolition of WHT, see

WHT added, at best, administrative inconvenience to cross-border trade and, possibly, a cost to the MNE group if double tax was unrelieved. Nonetheless, non-taxation was also possible where profits flowed cross-border without WHT. Abolition of WHT on royalties has been identified as a "significant risk of profit base erosion" because a unilateral reduction in royalty WHT rates would encourage tax avoidance by directing gross royalties to tax havens.[28]

The shifting of profits to tax havens, unhindered by WHT, is traced by Tørsløv et al: while 77% of profits shifted out of the EU are shifted to other EU Member States (primarily Ireland, Luxembourg and the Netherlands), the ultimate destination of 46% of profits shifted out of the EU is non-EU tax havens.[29] As an explanation for this intermediate step, Tørsløv et al point to EU rules on taxation of interest and royalties.[30] The significance of royalty payments is also explained by Coffey, who describes routing royalty payments from Ireland through the Netherlands as a "a fairly straightforward workaround", which was rendered unnecessary by the changes in Ireland's WHT rules.[31]

This, then, explains the importance of WHT on royalty payments as a strategy of acute importance to smoothing the path of MNEs to shift profits to low-tax or no-tax jurisdictions. While this architecture is well-known, discussion of it can often appear unschooled by the need for tangible examples of how the legal framework came into being, and it is usually addressed in the context of macro-economic dissections of FDI or economists' estimates of how much tax transfer pricing strategies or treaty shopping costs certain jurisdictions.[32]

Ireland has not been particularly secretive about being in competition for FDI with other states.[33] In 2012, the Department of Finance published a (redacted) note of a high-level tax strategy group, in which it noted:

> "There are two major forces at play in shaping the future development of Ireland's corporate tax regime. The first is intensifying competition from other jurisdictions intent on winning greater shares of global FDI. *xxx* Such developments mean that we must constantly review the competitiveness of elements of our CT regime apart from the rate. The second is the increased focus of international organisations such as the OECD and the EU on what they see as 'aggressive tax competition'. This requires that we ensure that whatever

Steffen Juranek, Dirk Schindler and Andrea Schneider, "Royalty taxation under tax competition and profit shifting" (2023) 56 *Canadian Journal of Economics/Revue Canadienne d'économique* 1377.

[28] Kim Brooks and Richard Krever, "The troubling role of tax treaties" in G.M.M. Michielse and Victor Thuronyi (eds), *Tax Design Issues Worldwide*, Vol.51 (Alphen aan de Rijn, the Netherlands: Series on International Taxation, Kluwer Law International, 2015), p.173.

[29] Tørsløv et al, "The missing profits of nations" (2023) 90(3) *The Review of Economic Studies* 1499, 1526, 1527.

[30] Tørsløv et al, "The missing profits of nations" (2023) 90(3) *The Review of Economic Studies* 1499, 1527.

[31] Coffey, "The Changing Nature of Outbound Royalties from Ireland and their Impact on the Taxation of the Profits of US Multinationals" Working Paper 2021, p.4.

[32] Tørsløv et al, "The missing profits of nations" (2023) 90(3) *The Review of Economic Studies* 1499; Coffey, "The Changing Nature of Outbound Royalties from Ireland and their Impact on the Taxation of the Profits of US Multinationals" Working Paper 2021.

[33] Dietsch, *Catching Capital: The Ethics of Tax Competition* (2015); Frank Barry, "Ireland and the changing global foreign direct investment landscape" (2019) 67 *Administration* 93.

> ‘enhancements’ we introduce to our broader regime do not damage our international tax reputation. *xxx*.”[34]

There are some interesting points to make about this Department of Finance document. First, the parameters of tax policy are transparent: the note is published, albeit it in redacted form. Secondly, it provides a synopsis of the competitive pressures identified by Ireland and, thirdly, the curbs on that competition through international pressure which militate in favour of low-profile or non-transparent “enhancements”.

The focus of this paper is on one particular “enhancement”, namely the abolition of WHT obligations on outbound patent royalties by Ireland in 2010. It explores this “enhancement” within the context of the legal system: examining the publication of an administrative practice very soon after the legislature had legislated on the same point.

Changes to Irish WHT on patent royalties in 2010

There are two relevant events which are very simply stated:

1. in February 2010 the Irish Parliament enacted a law removing an obligation on companies to withhold tax on patent royalties paid to foreign companies resident in the EU and other jurisdictions with which Ireland has a double tax treaty; and[35]
2. in July 2010 the Irish Government issued an administrative ruling, Statement of Practice CT/01/10 (SP CT01/10), extending the exemption from WHT beyond the statutory relief, with the effect that Irish-resident companies were not obliged to withhold tax on patent royalties paid to any foreign companies, including those situated in tax havens.[36]

The legislative change introduced on 4 February 2010 by s.55 of the Finance Act 2010 (henceforth s.55 or Section 55) enabled the payment of patent royalties free of WHT to a company resident in the EU or a state with which Ireland had a double tax treaty.[37] Section 55 was subject to a number of conditions: the recipient must be resident in a state which generally imposed taxation on foreign source royalties; the royalties must be paid; first, in the course of a trade or business carried out by the payer; secondly, for commercial purposes; and thirdly, not for the avoidance of tax.[38]

The lacuna in the legislative relief was that it did not apply to patent royalty payments made to recipients in states outside the EU or to recipients resident in states with which Ireland did not have a double tax treaty. This was the situation between 4 February 2010 and 26 July 2010.

[34] Note of the Tax Strategy Group, Department of Finance, TSG 12/16 on Corporation Tax, *https://www.gov.ie/pdf/?file=https://assets.gov.ie/25827/dfb5a1f874274f87b2ac9dfc2bec2629.pdf#page=null*, redactions in emphasis [Accessed 14 February 2024].

[35] Finance 2010 s. 55, *https://www.irishstatutebook.ie/eli/2010/act/5/section/55/enacted/en/html* [Accessed 14 February 2024].

[36] Statement of Practice CT/01/10, *https://www.taxfind.ie/binaryDocument//pdfs/http___www_revenue_ie_en_practitioner_law_statements_of_practice_sp_ct_01_2010_pdf.pdf* [Accessed 14 February 2024].

[37] Finance 2010 s.55.

[38] This legislative relief was in addition to the exemption from withholding tax provided for within the EU under Directive 2003/49 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States [2003] OJ L157/49.

The administrative change introduced by SP CT/01/10 went substantially further than s.55. With effect from 26 July 2010, Revenue exempted an Irish tax-resident company paying certain patent royalties from WHT, irrespective of the tax-residence of the recipient company. This was subject to a number of conditions: first, the paying company must be trading in Ireland and the royalty paid in the course of the trade; secondly, the recipient company must be the non-resident beneficial owner of the royalties; thirdly, the royalties must be payable under a foreign law licence agreement; and, fourthly, the royalties must not be part of a conduit arrangement relating to the licensing of the foreign patent.

There are some aspects of how SP CT/01/10 is drafted that jar slightly. First, SP CT/01/10 is really much wider in ambit than s.55: the legislation required that the state of residence of the recipient must impose a tax that applies generally to royalties receivable from sources outside that jurisdiction. This requirement is absent from SP CT/01/10. This has the effect of ensuring that a nil WHT applied to royalties paid to tax haven jurisdictions. Secondly, the proximity in timing between the legislative exemption from WHT and the administrative relief from WHT is not immediately obvious in the main body of SP CT01/10 and is only evident from the reference to Finance Act 2010 in a footnote.[39] Thirdly, SP CT01/10 states that the Revenue accepts that there is no charge to income tax on a non-resident company receiving a royalty payment in respect of a non-Irish registered patent where the licence agreement is executed outside Ireland and not subject to Irish jurisdiction. This could be an understandable justification for not imposing a WHT (on the basis that there is no Irish source), yet it sits uneasily with the condition in s.55 that relief from WHT was available only where the recipient jurisdiction imposed a tax on royalties generally. The change in approach—from a concern that royalties must be taxable somewhere to a disclaimer of any Irish liability to tax on the same royalties, even if payable to a tax haven—begs the question as to how the position changed between February and July 2010.

The tax changes to Irish WHT made by these events are summarised in Table 1. The payer is a company tax-resident in Ireland making royalty payments to the Netherlands, the US and Bermuda as exemplars of EU and cross-border destinations.[40]

Table 1: Changes to WHT on patent royalties, using Netherlands, the USA and Bermuda as examples

Date	**Payer: company tax-resident in Ireland**	**Recipient: company tax-resident in the Netherlands**	**Recipient: company tax-resident in the US**	**Recipient: company tax-resident in Bermuda**	**Amount received by Irish Revenue**
Prior to 4 February 2010	100	100[41]	80	80	40

[39] The legislative change of February 2010 is noted in a footnote to SP CT/01/10, which states that Taxes Consolidated Act 1997 s.242A was inserted by Finance Act 2010 s.55.

[40] Tørsløv et al, "The missing profits of nations" (2023) 90(3) *The Review of Economic Studies* 1499; Coffey, "The Changing Nature of Outbound Royalties from Ireland and Their Impact on the Taxation of the Profits of US Multinationals" Working Paper 2021.

[41] This assumes that the provisions of the EU Interest and Royalties Directive (Directive 2003/49 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States [2003] OJ L157/49 as amended), implemented by the Taxes Consolidation Act 1997 (TCA 1997) Pt 8 Ch.6, apply. This provides for nil WHT in the case of certain royalty payments to associated companies resident in other member states.

Date	Payer: company tax-resident in Ireland	Recipient: company tax-resident in the Netherlands	Recipient: company tax-resident in the US	Recipient: company tax-resident in Bermuda	Amount received by Irish Revenue
4 February 2010 to 26 July 2010	100	100	100[42]	80	20
After 26 July 2010	100	100	100	100[43]	0

Table 1 illustrates that, potentially, Ireland relinquished taxing rights as a result of both the statutory change in February 2010 and the administrative change in July 2010. To summarise, the effect of the SP CT 01/10 change was to ensure that outward bound patent royalties could be paid gross, irrespective of the location of the recipient company.

Three further points need to be emphasised. First, prior to 4 February 2010 intra-group royalty payments to the Netherlands and other EU Member States could generally be made free of WHT under the EU Interest and Royalty Directive. This ensured that, in the use of the "Double Irish Dutch sandwich", royalty payments were not made from Ireland to the tax haven jurisdiction (e.g. Bermuda) in which the IP was held, but were instead routed through the Netherlands, and from there were paid free of WHT to the tax haven jurisdiction.[44] The change after 26 July 2010, therefore, facilitated a direct royalty payment to tax havens free of Irish WHT, achieved without the intermediate step of routing through the Netherlands.

Secondly, SP CT01/10 finishes with a mantra familiar to readers of administrative rulings:

> "[t]he practice set out in this Statement should be relied upon only to the extent that the royalty payments concerned are made in good faith and for purposes that do not include tax avoidance."

It is not particularly clear what type of tax avoidance is included or what could be meant by good faith as the Revenue was aware of the possibility of payment to a tax haven. In fact, the distinction between s.55 and SP CT01/10 is the absence in the latter of any requirement for the recipient of the patent to be resident in a jurisdiction which generally imposed a tax on royalty payments.

Thirdly, the changes enabled the stripping of the Irish tax base through payment of outward-bound patent royalties without WHT. Yet this was unlikely to result in a loss of tax to Ireland as, prior to 26 July 2010, patent royalties with an ultimate destination of Bermuda, were routed through the Netherlands in a "straightforward workaround".[45] Patent royalties continued to be deductible for corporation tax purposes as before: SP CT01/10 explicitly states that the payment of patent royalties free of WHT would not preclude the deductibility of royalties.[46] The

[42] Change effected by s.55 which sets out certain conditions to benefit from an exemption from WHT.
[43] Change effected by Revenue publishing an administrative ruling, SP CT 01/10, which sets out certain conditions to benefit from nil WHT.
[44] Zucman, "Taxing across Borders: Tracking Personal Wealth and Corporate Profits" (2014) 28 *The Journal of Economic Perspectives* 121; Coffey, "The Changing Nature of Outbound Royalties from Ireland and their Impact on the Taxation of the Profits of US Multinationals" Working Paper 2021.
[45] Coffey, "The Changing Nature of Outbound Royalties from Ireland and their Impact on the Taxation of the Profits of US Multinationals" Working Paper 2021.
[46] SP CT01/10 para.3.2.

changes in 2010 were, therefore, nugatory in an immediate fiscal sense, which begs the question as to why they were introduced.

Parliamentary debates on the February 2010 relief from WHT on patent royalties

During parliamentary debates about the legislation, the Minister for Finance, noting that the debate was "very well informed", stated that:

> "the complete abolition of withholding tax is not possible, as it would have adverse implications for our relationship with tax treaty partners and foreign tax authorities generally. The EU code of conduct group is examining the issue of withholding taxes. For us to make a unilateral change in advance of this discussion would be seen, therefore, as very tax aggressive by our EU partners."[47]

In reply to a suggestion that a wider withholding tax relief be introduced to improve Ireland's competitive position, the Minister for Finance replied that the wider exemption:

> "could apply to royalties paid to a tax haven. This could facilitate the use of Irish companies to undermine the tax base of Ireland or other countries. That would not be appropriate. I do not think we can go down that road."[48]

Two points can be made about these parliamentary debates: first, the legislative amendment was discussed in terms of maintaining Ireland's tax competitiveness and secondly, there was a clear government policy, ultimately reflected in s.55, that Ireland would not abolish WHT on patent royalties but would merely expand to relief where recipients were resident in the EU or treaty jurisdictions where there was a charge to tax on royalties. In short, the legislative amendment in February 2010 was a distinct policy choice put to parliament by the Irish Government and enacted into law.

Data obtained under FOI requests to the Department of Finance and Revenue

That the policy choice in February 2010 was carefully considered is also evident from the data released under FOI requests.[49] This FOI data can be divided temporally into two sections. The first is the period leading up to the enactment of s.55, the legislative amendment that went some way to relaxing WHT rules on outbound patent royalties but, crucially, required that the recipient company was subject to tax in the foreign jurisdiction and resident in the EU or a jurisdiction with which Ireland had a double taxation agreement. The second part of the FOI data relates to the period from February to July 2010.

At least some of the impetus for change to the WHT rules came from industry and professional advisers. In November 2009, a meeting was set up between the Minister for Trade, Enterprise and Employment and a group described as "Silicon Valley". The briefing paper for this meeting

[47] Dail Debates, 24 February 2010, *https://www.oireachtas.ie/en/debates/debate/select_committee_on_finance_and_the_public_service/2010-02-24/2/* [Accessed 14 February 2024].
[48] Dail Debates, 24 February 2010.
[49] See further details in the Appendix to this paper.

(from the redacted company or professional adviser) suggested the removal of WHT on patent royalties, stating:

> "Ireland is in direct competition for investment and jobs with countries such as the Netherlands, Switzerland, Hungary and Luxembourg. None of these countries levy withholding tax on outbound royalty payments. A change in the Irish withholding provisions would put Ireland on a level footing with numerous other high-profile European jurisdictions."

The briefing paper goes on to say: "The list of supporters of this measure is long and includes some of the leading employers all across the country". A diagram attached to the briefing paper showed the "Double Irish Dutch Sandwich", showing the "straightforward workaround" through the Dutch BV to avoid WHT.[50]

It was clear to everyone involved in discussions about WHT on patent royalties that it was easily avoided by routing the patent royalties through an intermediary company resident in the Netherlands. In an internal Revenue email dated 16 October 2009, it was remarked: "There is somewhat of an incongruity in our trying to attract companies to establish in Ireland rather than Holland while at the same time advising them to make patent royalty payments through a Dutch BV."

On 30 November 2009, the Department of Enterprise, Trade and Employment emailed a case study, prepared by a public relations company, to Finance and Revenue. This case study stated the "significant and unnecessary administrative burden for the taxpayer in interposing intermediary companies" and attached a diagram showing the Double Irish tax structure with the Netherlands company interposed between an Irish incorporated company, resident in Bermuda. A draft paper on WHT, prepared by Revenue and dated 18 January 2010, notes:

> "Irish withholding tax on royalties can be avoided by routing royalty flows out of Ireland through companies in countries with which we have a tax treaty that abolishes withholding tax or through EU Member States. Netherlands is often used by Irish resident companies to route payments to companies in countries with which Ireland does not have a tax treaty."

Attention was paid to the tax offerings of other Member States. The paper continued: "It is without doubt that as long as our European counterparts continue to grant such generous concessions to innovators, so too must we".

There is a good audit trail in the FOI material which shows the detailed consideration by Revenue and Finance of introducing any legislative relief. There was a repeated concern that abolition of WHT on outbound royalties might facilitate the erosion of the tax base of other jurisdictions which would be damaging to Ireland's international reputation. On 15 January 2010, Revenue emailed Finance stating that abolition of all WHT on royalty payments "would allow royalties to flow to non-treaty countries (possibly tax havens) free of tax". The discussion veered between maintaining the status quo (i.e. WHT on all outbound patent royalties) to a recommendation of the so-called "Option 3", which was the abolition of WHT on royalty payments by companies to EU Member States and tax treaty countries. It was clear that Revenue

[50] Coffey, "The Changing Nature of Outbound Royalties from Ireland and Their Impact on the Taxation of the Profits of US Multinationals" Working Paper 2021.

favoured no change or, as ultimately happened under s.55, a limited legislative change. This is characterised by an internal Revenue email, dated 15 January 2010, stating:

> "I think that doing the EU and treaty country option will not give much particularly in the context of IRNRs and might just cause more lobbying on the basis that we appear to have missed the point. Consequently, I think we should go for the status quo."[51]

Section 55 did make changes, yet they were minimal and certainly not what MNEs and professional advisers had in mind. Criticism came quickly after the enactment of s.55 in February 2010. One MNE wrote to the Minister for Finance on 17 February 2010, commenting on the limited changes to WHT in the draft Finance Bill, and saying: "Anecdotally we understand that competitor States are referencing such a negative component of the Irish regime to their advantage." This was quickly followed by a professional adviser emailing Finance on 18 February 2010, asking: "Would you have any time this afternoon or tomorrow to talk briefly about [section 55] Finance Bill? It is causing some angst amongst the FDI community." Another MNE wrote on 10 February 2010 to the Prime Minister and refers to "up to 200 companies" that may be impacted by WHT on patent royalties, before continuing: "We were hopeful that the Finance Bill … would have addressed the issue by introducing certain exemptions for qualifying companies. However [Section 55] fell short of what is needed …".

All this could be dismissed as the objections of disappointed taxpayers, were it not for somewhat oblique references to a further step. On 19 January 2010 (i.e. before the Finance Act 2010 was enacted), a civil servant referred to a forthcoming meeting between the Minister and some MNEs and noted, without further explanation: "I think that there is a way out that is not legislative." On 17 February 2010, a professional adviser emailed Finance and Revenue, saying "I understand the policy implications of an abolition of WHT in this area via a legislative change and the sensitivities around the optics of this". A further internal Revenue email of 22 April 2010 refers to considering "the merits of an administrative response". Even as what became s.55 made its way through Parliament, it is clear from the FOI documentation that a further administrative solution was under consideration.

Some sort of administrative response was the subject of a meeting between MNEs, professional advisers "representing some companies in the coalition" and Revenue which was held on 30 April 2010. No record of that meeting was released under FOI. However, there is a reference to the 30 April meeting in an email dated 13 May 2010 from Revenue to an unnamed MNE:

> "To be clear I would emphasize that, while the issues are being actively considered, there is not a Revenue proposal at this stage. I mentioned at our meeting that it would be important to ensure that there was full consideration at the appropriate level of any exercise of administrative discretion by Revenue in relation to these issues."

Again, there is no clarity as to how Revenue approached the question of its administrative discretion, although it is likely that this was at least one of the subjects discussed with counsel

[51] IRNR generally refers to an Irish registered non-resident company, i.e. one which is incorporated in Ireland but is not Irish-resident for tax purposes. It was used as part of the "double Irish" tax structure. See, e.g. Frank Barry, "Aggressive tax planning practices and inward-FDI implications for Ireland of the new US corporate tax regime" (2019) 50 *The Economic and Social Review* 325.

and the subject of an opinion dated 26 April 2010, the release of which was refused under the FOI application. The issue of discretion was not a new concern. Revenue had been aware of this as a potential problem, as illustrated by an email from Revenue to Finance on 17 February 2010: "A decision was made for FB 2010 *not* to abolish the WHT on royalties. If it were to be effectively abolished by interpretation a question would then arise as to whether that was a satisfactory outcome from a policy perspective."

The continued importance of interaction between Revenue, MNEs and professional advisers is evident from the span of FOI data released and not released. Two snippets, in particular, show the influence of professional advisers. The first is in an email dated 18 January 2010, where draft legislation was circulated within Revenue, asking for comments on a draft of what became s.55. One addressee of the email is redacted, and the body of the email requests that all Revenue comments be copied to a redacted name. This is intriguing as under the FOI process, names of Revenue personnel were not redacted but the names of employees of MNEs or professional advisers were redacted. This is some, possibly weak, evidence for the continued involvement of professional advisers in the crucial activity of drafting legislative change. The second snippet dates from 18 July 2010 and relates to the drafting of SP CT01/10 when an internal Revenue email asks "There's also the question whether we can get an advance business view without inviting dilution of the text?". The material released under FOI does not indicate whether this was done. These are indicators of a close collaborative process between Revenue and taxpayers in agreeing a construction of a problem, co-operating in solving it and changing a long-standing application of the law.

A further line of lobbying, after the enactment of s.55, took the form of explaining to Revenue and Finance that the Revenue's "settled view for some years" on WHT was incorrect. This argument relied upon a view that royalties on foreign patents were not Irish-source income and that there was, therefore, no charge to Irish tax. Where there was no charge to Irish tax in respect of foreign patents, an argument made at length by a professional services firm to Revenue and Finance, there could be no obligation to WHT. This was based on a fundamental view of WHT being a tax collection mechanism, rather than a tax charging mechanism. A professional advisory firm helpfully wrote to Finance on 17 February 2010 that "[T]he law has not been correctly applied for many many years now by Irish Revenue", and WHT on outbound royalties was a "core issue affecting nearly all of the Irish subsidiaries of US tech companies". The letter continued: "Hence there has been some lobbying on this issue to the Department".

The technical argument about source of foreign patents and the nature of WHT was not, in fact, a new argument, and there is FOI data showing that it had been made to Revenue by another professional adviser in September 2009. In any event, when provided with the argument by the professional advisers, Revenue emailed Finance on 17 February 2010:

> "My view regarding [professional adviser's] analysis is that, as it would effectively amount to the abolition of the WHT on royalties, we would need to be very sure that he is right before agreeing. But agree we will—if his analysis is, in fact, correct."

Perhaps this analysis was found to be correct, not in time to render the legislative amendment in February 2010 redundant, but to sustain a view that SP CT01/10 merely restated existing law when it noted that a patent royalty paid to a non-resident company does not give rise to a charge to Irish income tax in certain circumstances.[52]

This is contrary to Revenue's own explanatory note when drafting the legislative relief. This note, dated 18 January 2018 and prepared by Revenue, states "Where the conditions [of the future Section 55] are met, the payment will be exempt from withholding tax and from any underlying charge to tax that would otherwise arise on the payment as Irish-sourced income". The nuance, urged upon Revenue by MNEs and various professional advisers, that certain patents would not have an Irish source is simply unexplored. Section 55 proceeded along a different path and is drafted on an assumption that WHT can apply to any royalty.

One internal document which might have made many of these matters clear, and which presumably discussed the question of constitutionality of Revenue rule-making, its vires and discretion, is the instructions to legal counsel and the note of legal counsel's advice. Yet these were withheld from the FOI data on the basis of legal professional privilege.

The postscript to the publication of SP CT01/10 is interesting. FOI data show that notes from professional advisory firms to clients were circulated within Revenue on 5 August 2010, with a note that: "there seems to be no end of professional firms trying to jump on this." This is combined with quite a nervous look towards the international media, particularly a series of Bloomberg stories which were appearing about Irish tax practices, and a suggestion was made by Revenue to a PR company in an email dated 23 July 2010 that: "There's been some unexpected informal publicizing of the development already explicitly linking it to the double Irish arrangements. This may not be best advised, in the light of recent negative coverage in Bloomberg for example."

The stated rationale for making an administrative change is to be found in a Revenue paper dated 15 July 2010, just before the draft SP went to the Board of the Revenue Commissioners for approval. The paper states:

> "It is proposed that an administrative practice be implemented whereby, in specific circumstances, Revenue will permit companies to pay patent royalties to non-residents without deduction of tax. An administrative, as opposed to a legislative, solution is being proposed here as legislation would be difficult to devise and would require deployment of resources out of proportion to the inherent importance of this matter."

This is a misdirection, as legislation had already been extensively considered and decided against, including during parliamentary debates. The "inherent importance of this matter", while possibly not clear to Revenue, was certainly clear to the "companies in the coalition" and their professional advisers, who pursued their disappointment and angst at the limited nature of the legislative change in February 2010, met Revenue in April 2010 and trumpeted their victory in notes to clients in July 2010.

Rule-making by the Revenue: July 2010

The sequence of events in 2010 prompts the question as to how a statutory relief (explicitly limited to payment flows to EU and treaty jurisdictions) can be followed seven months later by an executive decision by the government to extend the same relief from WHT to all jurisdictions.

[52] SP CT01/10 para.2.2.

This question can first be addressed in a legal context, through a technical examination of Revenue's power to issue this type of administrative ruling and the extent to which taxpayers can rely on it.

There are two strands to this analysis. The first is to examine the July 2010 administrative ruling within the confines of Irish constitutional law, specifically the separation of legislative from executive power. The second, and related, part of the analysis is to examine the statutory framework within which Revenue operates and test whether it has a residual administrative discretion to publish a statement of practice clarifying its view on the circumstances in which WHT is due on the outbound payment of patent royalties. In both these strands, an important consideration is how to classify Revenue practice: that SP CT01/10 changed the law governing Irish WHT or that the Revenue came to a realisation that its long-standing interpretation was, in law, incorrect.

Separation of powers: a constitutional embargo on rule-making by Revenue

The starting point is the strict separation of powers provided for in the Irish Constitution which specifies, in art.15.2.1, that the sole legislative authority rests with Parliament.[53] The doctrine of separation of powers is a "high constitutional value",[54] much discussed and disputed in its application and consequences.[55] It is the theoretical justification for the antipathy towards discretionary power being vested in the executive branch of government and the careful attention that is given to delegated rule-making authority invested in government bodies and regulators.[56] Guarding rule-making authority within the legislature is based on normative conceptions of the legitimacy and accountability of government rule, where the administrative bodies (in this case Revenue) are intended to be "directed drones rather than autonomous actors in the policy-making or policy-implementing processes of government".[57] In this sense, legitimacy means the reservation of democratic legitimacy (and accountability through the electoral cycle) to parliament, effected through the separation of powers.[58]

The limits of Revenue's discretion to extend the law has been recognised by the courts in a tax context.[59] The Supreme Court declined to follow a UK line of anti-avoidance case law construing tax liability according to economic substance rather than legal form, stating that this would "constitute the invasion by the judiciary of the powers and functions of the legislature,

[53] D.G. Morgan et al, *Hogan and Morgan's Administrative Law* (Dublin: Thomson Reuters (Round Hall), 2020).

[54] David Kenny, "The Separation of Powers and Remedies: The Legislative Power and Remedies for Unconstitutional Legislation in Comparative Perspective" in Eoin Carolan (ed.), *The Irish Constitution: Perspectives and Prospects* (London: Bloomsbury Professional, 2012), p.89.

[55] Eoin Carolan, *The New Separation of Powers: A Theory for the Modern State* (Oxford: OUP, 2009); Kenny, "The Separation of Powers and Remedies: The Legislative Power and Remedies for Unconstitutional Legislation in Comparative Perspective" in Carolan (ed.), *The Irish Constitution: Perspectives and Prospects* (2012).

[56] Carolan, *The New Separation of Powers: A Theory for the Modern State* (2009); Conor Casey, "The Supreme Court and the Reformation of the Non-Delegation Doctrine: Náisiunta Leictreacht v Labour Court, Minister for Business Enterprise, and Ireland [2021] IESC 36" (2022) 4 *Irish Supreme Court Review*.

[57] Carolan, *The New Separation of Powers: A Theory for the Modern State* (2009), p.50.

[58] Jeremy Waldron, "Separation of Powers in Thought and Practice" (2013) 54 B.C.L. Rev. 433; Yvette Lind, "Blurring the separation of powers—a legal and political study of the phenomenon of tax administrations moving from the executive branch towards the legislative branch" (2023) 21 *eJournal of Tax Research* 383.

[59] *McGrath v McDermott* [1988] I.R. 258, *Wylie v Revenue Commissioners* [1993] I.L.R.M. 482, *Zappone and Gilligan v Revenue Commissioners* [2006] IEHC 404.

in plain breach of the constitutional separation of powers".[60] While this application of separation of powers related to the power of the judiciary to formulate tax policy, and did not concern the executive, it nonetheless is an indicator of the strength of the constitutional embargo on law-making by any body other than the legislature.

Nonetheless, in spite of the bald adherence to the doctrine of strict separation of powers in art.15.2.1 of the Constitution, there is sometimes a lack of reality to this embargo on delegated rule-making authority. Casey notes that the power to invalidate rules on the grounds of incompatibility with art.15.2.1 has been sparsely exercised by the courts.[61] The constitutionally permissible delegation of power by Parliament has been given a wider ambit in recent case law, including upholding the Labour Court's competence to set sectoral employment conditions.[62] Recasting delegated authority in a more permissive way focuses on whether Parliament has set down boundaries or rules of conduct for the administrative body, and whether there are review procedures before the administrative act gains the force of law.[63]

SP CT01/10 was reviewed by the Board of the Revenue Commissioners in July 2010 before publication and was approved. Counsel's opinion, together with a note on the draft SP CT01/10, were provided to the Board of the Revenue Commissioners and a Revenue email dated 16 July 2010 to an individual Commissioner states that: "There is considerable pressure for a change and it would be best to publish, if the Board agrees the proposal, before the Summer holidays delay the process further". It is not altogether clear that this type of self-approval by Revenue is quite what the Supreme Court had in mind when formulating a more permissive approach to executive rule-making.

The constitutional question may well come down to the robustness of (and evidence for) the argument that Revenue, sometime between January and July 2010, became convinced of the incorrectness of its previous interpretation of the obligation to WHT on outbound royalties. As this is also relevant to the residual level of discretion enjoyed by Revenue, it is further addressed later in this article.[64] In summary, and at this stage of the analysis, there is a question mark over the constitutional status of SP CT01/10.

Revenue discretion: how far does it extend?

Leaving aside the constitutional issues relating to separation of powers, it is clear that Revenue operates within a statutory framework which allows for a certain element of discretion. This is something short of rule-making but is nonetheless on the spectrum of changing the effect of statute through a new or revised interpretation. Tax law is complex: a certain amount of freedom as to how the law is interpreted is necessary to operate the tax system. This approach is heavily dependent upon an understanding of the indeterminacy of language and reflects an understanding of tax law as being, to a sometimes disputed extent, socially and dynamically constructed.[65]

[60] *McGrath v McDermott* [1988] I.R. 258 at 264.
[61] Casey, "The Supreme Court and the Reformation of the Non-Delegation Doctrine: Náisiunta Leictreacht v Labour Court, Minister for Business Enterprise, and Ireland [2021] IESC 36" (2022) 4 *Irish Supreme Court Review*.
[62] *NECI v Labour Court and Ireland* [2020] IEHC 178.
[63] *NECI v Labour Court and Ireland* [2020] IEHC 178.
[64] See section "The legal argument as to WHT on outbound patent royalties" below.
[65] Dominic de Cogan, "A Changing Role for the Administrative Law of Taxation" (2015) 24 *Social & Legal Studies* 251.

As a matter of formal law, Revenue is charged with care and management of the tax system and empowered to "do all such acts as may be deemed necessary and expedient for raising, collecting, receiving and accounting for tax".[66] The limitation on executive discretion has a deep impact on how the power of the tax authority is approached, and is often seen in the ambit of any legitimate expectation enjoyed by the taxpayer.[67] As a problem of risk analysis, a taxpayer who considers relying on a published or private ruling from Revenue, needs to assess Revenue's competency or vires to produce such a ruling, since vires must be established to ground a legitimate expectation that the ruling can be relied upon.[68]

Clearly, there is an element of discretion inherent in the administrative activities of any tax authority, both substantive and procedural.[69] The latter is quite easily understood, as efficient administration of tax law does not require Revenue to, for example, pursue all available avenues of litigation against an evasive or wrong-headed taxpayer.[70] The substantive discretion, to re-interpret legislation or change a long-standing interpretation, is a balancing act which will relate to the strength (and possibly the motivations) of the Revenue's change in approach.[71] In saying this, the balancing act will call into play the same constitutional preoccupations with executive rule-making, namely the concern about democratic accountability and the legitimacy of the legislative process and is subject to review by the courts as the arbiters of statutory meaning.[72]

Testing the legitimacy of Revenue's activities steps past the constitutional protection for separation of powers to assess, more widely, whether there has been a justifiable exercise of discretion by a government institution.[73] Borrowing from political science, legitimacy can be divided into input legitimacy, output legitimacy and throughput legitimacy.[74] These aspects of legitimacy have been variously articulated in a tax context as equal participatory rights by citizens or taxpayers in the decision-making process (input legitimacy), the substantive quality of the result (output legitimacy) and the governance process between input and output (throughput legitimacy).[75] The publication of SP CT01/10 can be analysed according to who was involved

[66] TCA 1997 s.849.
[67] Stephen Daly, *Tax Authority Advice and the Public* (Oxford: Hart, 2020), Ch.6.
[68] *Wylie v Revenue Commissioners* [1993] I.L.R.M. 482; *Cork Opera House v Revenue Commissioners* [2007] IEHC 388. Other factors will also be relevant to establish legitimate expectation, see *Perrigo v Revenue Commissioners* [2020] IEHC 552.
[69] Dominic De Cogan, "Tax, discretion and the rule of law" in Chris Evans, Rick Krever and Judith Freedman (eds), *The Delicate Balance: Tax, Discretion and the Rule of Law* (Amsterdam: IBFD, 2011).
[70] Judith Freedman and John Vella, "HMRC's Management of the U.K. Tax System: The Boundaries of Legitimate Discretion" in C. Evans et al (eds), *The Delicate Balance: Tax, Discretion and the Rule of Law* (Amsterdam: IBFD, 2011).
[71] SP CT01/10 could conceivably be challenged as unlawful, and motivation could be relevant in arguing that Revenue was unreasonable, irrational, and took into account factors irrelevant to its statutory mandate for "care and management" of the tax system under TCA 1997 s.849. See *O'Keeffe v An Bord Pleanala* [1992] I.L.R.M. 237.
[72] Daly, *Tax Authority Advice and the Public* (2020).
[73] Hans Gribnau, "Improving the Legitimacy of Soft law in EU Tax law" (2007) 35 *Intertax* 30.
[74] Fritz Scharpf, *Governing in Europe: Effective and democratic?* (Oxford: OUP, 1999); Vivien A. Schmidt, "Democracy and Legitimacy in the European Union Revisited: Input, Output and 'Throughput'" (2013) 61 *Political Studies* 2.
[75] Stephen Daly, "The OMC, intelligent accountability and the monitoring of national tax authorities" (2022) 85 *Modern Law Review* 1109; Stefanie Geringer, "A change in the law or a guideline from the EU VAT Committee? Evaluating soft law instruments for clarifying EU VAT Law through the lens of legitimacy" (2024) 52 *Intertax* 3;

and consulted (only a "coalition" and their professional advisers) and how the process was conducted (after a legislative solution had been rejected). Splitting legitimacy in this way facilitates this question: was the process by which SP CT01/10 drafted and published consistent with values underpinning legitimacy; trust, accountability, transparency and inclusiveness?[76] The question of output legitimacy is vast: how could the substantive quality of an instrument, which notionally eroded the Irish tax base, be assessed, and in whose interests could SP CT01/10 be viewed as efficient and effective?[77] (Ireland, Revenue, MNEs, professional advisers are possibilities that come to mind.)

These are dense concepts and, for the purposes of this article, are not dissected into their interrelated elements. Instead, we take as a general viewpoint that Revenue possesses some legal discretion (disputed as to its ambit) to issue statements of practice on how it interprets or applies tax legislation. The legitimacy of how this discretion is exercised must be thoroughly probed as, in the context of SP CT01/10, it was used as an instrument of de-taxation.[78] The wider context is the influential position of Ireland in the international tax landscape (as economically quantified by Tørsløv et al and Coffey);[79] its depiction as a tax haven prior to 2010;[80] and the political consequences of SP CT01/10 (noted in the FOI process as being detrimental to the state's international relations). This brings us to an examination of the underlying legal issue: was Irish WHT due on outbound foreign patent royalties?

The legal argument as to WHT on outbound patent royalties

This is not the forum for a detailed rehashing of an old argument as to the source of income and property.[81] Certain views are, however, reasonably uncontroversial. The source of a cross-border payment can be difficult to determine, particularly when looking at IP, which is a legal construct.[82] There are also possible arguments, under Irish law, that a statutory obligation to WHT must have a territorial limitation and that WHT is a collection mechanism, rather than a charging

Cees Peters, "The Legitimacy of the OECD's Work on Pillar Two: an Analysis of the Overconfidence in a 'Devilish Logic'" (2023) 51 *Intertax* 8.

[76] Schmidt, "Democracy and Legitimacy in the European Union Revisited: Input, Output and 'Throughput'" (2013) 61 *Political Studies* 2.

[77] Schmidt, "Democracy and Legitimacy in the European Union Revisited: Input, Output and 'Throughput'" (2013) 61 *Political Studies* 2; Sol Picciotto, "Constructing compliance: Game playing, tax law, and the regulatory state" (2007) 29 *Law & Policy* 11.

[78] Genschel and Seelkopf, "The Competition State: The Modern State in a Global Economy" in Leibfried et al (eds), *The Oxford Handbook of Transformations of the State* (2015).

[79] Thomas Tørsløv et al, "The missing profits of nations" (2023) 90(3) *The Review of Economic Studies* 1499; Coffey, "The Changing Nature of Outbound Royalties from Ireland and Their Impact on the Taxation of the Profits of US Multinationals" Working Paper 2021.

[80] J.R. Hines and E.M. Rice, "Fiscal paradise: Foreign tax havens and American business" (1994) 109 *The Quarterly Journal of Economics* 149; Mihir A. Desai, C. Fritz Foley and James R. Hines, "The demand for tax haven operations" (2006) 90 *Journal of Public Economics* 513.

[81] Stephen E. Shay, J. Clifton Fleming Jr and Robert J. Peroni, "The David R. Tillinghast Lecture—What's Source Got to Do with It—Source Rules and US International Taxation" (2002) 56 *Tax Law Review* 81.

[82] Brooks and Krever, "The troubling role of tax treaties" in Michielse and Thuronyi (eds), *Tax Design Issues Worldwide*, Vol.51 (2015). For instance, in the Finance Act 2016, the UK introduced a specific rule determining that a royalty comes from a source in the UK if paid in connection with the trade of a permanent establishment in the UK.

mechanism.[83] Furthermore, it can be unclear what is meant by the statutory requirement to withhold tax on payment of "any royalty or other sum paid in respect of the user of a patent".[84] Is the source of the royalty payment the underlying patent or the licence agreement under which the royalty is agreed?

The existence of these arguments might allow Revenue to assert that SP CT01/10 was merely drawing out some implications of an arguable legal interpretation. It would thereby enable an argument that issuing a better interpretation was within the ambit of normal Revenue discretion. Therefore, the benign interpretation of Revenue events between February and July 2010 is that re-consideration of the law, possibly based on the unseen counsel's advice, meant that no WHT was due.

As against this, there is the FOI data indicating that Revenue's view of WHT was a longstanding position, being noted both by Revenue and professional advisers as being of long duration, and its amendment was extensively considered prior to the enactment of s.55. Legislative change would have been unnecessary in February 2010 if the Revenue had come to a view that no tax was to be withheld on foreign patent royalties where there was no underlying liability to Irish tax. It was aware of these arguments since, at least, September 2009. In all of this discussion, Revenue pointed to reputational problems arising from a statutory abolition of WHT and the possibility of tax base erosion. The FOI data shows Revenue briefing Finance on these points prior to the enactment of s.55 in February 2010. The legislative policy choice was clear but was quickly reversed by an executive action.

The motivation for introducing SP CT01/10 is, at least optically (to quote the professional adviser writing to Revenue on 17 February 2010), also not helpful. Revenue's power was exercised in clear knowledge that payments to tax havens would go tax free and in seeming fulfilment of the Revenue's desire that payments within the Double Irish Dutch Sandwich would cut out the Dutch layer. Thus, the discretion appears to have been exercised for reasons of state competition and not truly as a reflection of the interpretative difficulties attendant upon notions of source, location of IP or the function of WHT. On this view, interpretative difficulties were a fig leaf for keeping MNEs and professional advisers from "angst".

In summary, both at a constitutional level and in regard to the residual statutory discretion enjoyed by Revenue, the timing and content of the administrative action pushed Revenue or executive discretion to its absolute limit, if not beyond. Yet SP CT01/10 remained in force, unchallenged by taxpayers, as an accepted part of the architecture of the state which was never placed on a statutory footing.[85]

[83] See, on these points, *Colquhoun v Brooks* (1889) 14 App. Cass 493; 2 T.C. 490 and *Colclough v Colclough* (1964) 2 I.T.R. 332, both of which have been used in this argument to limit territorial application of WHT and to view WHT as a collection mechanism only.

[84] TCA 1997 s.238(2).

[85] See Revenue Tax and Duty Manual Pt 08-01-04, "Treatment of Certain Patent Royalties Paid to Companies Resident Outside the State" updated June 2023, *https://www.revenue.ie/en/tax-professionals/tdm/income-tax-capital-gains-tax-corporation-tax/part-08/08-01-04.pdf* [Accessed 14 February 2024]. SP01/10 is likely to be rendered obsolete by the Finance (No.2) Act 2023 s.36, which introduced certain "outbound payments defensive measures", including WHT on royalties paid to associated entities in zero tax and EU non-cooperative jurisdictions and a corresponding charge to Irish tax on such royalties. This comes into effect in 2024 or 2025.

Conclusion

The first, and most obvious conclusion, was that Revenue pursued a course of action, described by the Minister for Finance in Parliament as "very tax aggressive" in an untransparent way. The immediate fiscal impact of SP CT01/10 was not to raise additional revenue for Ireland. In fact, it stripped Ireland of its tax base by abolishing WHT on patent royalties paid anywhere. It is an example of the paradoxical nature of state tax competition: de-taxation and de-regulation are instruments used by competing states to attract mobile capital and FDI.[86] In 2010 the Irish state knowingly improved its tax offering, undercutting the Netherlands by offering MNEs (largely US) the administrative convenience and less risky (in terms of cost and audit risk) direct payment to Bermuda, free of WHT.

This tax competition benefitted Ireland, acted to the detriment of the Netherlands and reflected an acceptance by both states that outbound royalties ended up in tax havens. The administrative ruling in July 2010 was based on co-operation between the state and MNEs, or their professional advisers, to remove source state taxation, a nirvana of tax planning. Such is the sensitivity to reputational concerns that the excision of the Netherlands from Irish tax planning was seen as a reputational problem at the time and is still so seen. A significant amount of material is not released under FOI legislation on the basis that its release would continue to harm Ireland's international relations with other states.

The next conclusion is that Revenue discretion in issuing SP CT01/10 is, at best, under some constitutional strain. The process of responding to lobbying from MNEs and professional advisers was secret and the alacrity with which SP CT01/10 was published so soon after the legislative amendment is unedifying. It has implications for the legitimacy of tax administration, and the oversight of the executive by the legislature. Even if not under constitutional strain, on the basis that it was a robust, albeit modified, interpretation of existing law, the process by which Revenue reached its view was so heavily dependent upon external pressure from MNEs and professional advisers that it bodes ill for consistent, transparent and justifiable administration. The allyship of Revenue with those wishing to pay outward-bound royalties without WHT chips away at the input and throughput legitimacy of tax administration by Revenue.

What therefore can be gleaned of the culture of the Irish legal system, specifically tax law? Van Hoecke and Warrington write that "law cannot be understood unless it is placed in a broad historical, socio-economic, psychological and ideological context".[87] This is a very weighty prescription, which this paper has approached only in a limited empirical context, based on incomplete and redacted FIO data. However, it is clear from the FOI data that MNEs and their professional advisers pushed for a legislative change, expressed disappointment at its lack of ambition, and then switched tactics to pushing for a change in interpretation, or an administrative solution. This could be further explored as the access of privileged taxpayers to extensive engagement and discussion with Revenue, Finance and government ministers.[88]

[86] Genschel and Seelkopf, "The Competition State: The Modern State in a Global Economy" in Leibfried et al (eds), *The Oxford Handbook of Transformations of the State* (2015).
[87] Van Hoecke and Warrington, "Legal cultures, legal paradigms and legal doctrine: towards a new model for comparative law" (1998) 47 *International & Comparative Law Quarterly* 495, 496.
[88] There is a question as to whether this type of contact would now fall within the Regulation of Lobbying Act 2015, which was not in place in 2010.

It is also clear that this push for further change fell on receptive ears: Revenue issued an administrative solution after meeting with representatives of the "coalition" on 30 April 2010. Revenue itself writes (16 October 2009), about "advising [companies] to make patent royalty payments through a Dutch BV". This shows Revenue to be conflicted, as it assumes a role of adviser in addition to its clear role as tax collector or regulator. The events of 2010 throw a light on "the body of beliefs and practices that are shared by tax practitioners and policymakers in a given society" and show a collective will to craft a tax offering, excluding the Netherlands and hiding from legislative oversight.[89] Revenue appears motivated to provide advice to taxpayers, rather than applying the law. The entire process evidences a view that interpretation of Irish tax law is a malleable practice, dynamic and responsive to, at least, sustainable concern or, at worst, lobbying by taxpayers and their professional advisers.

Without seeing the counsel's opinion which, presumably, discussed capacity and discretion of executive power (and their limits), it is not possible to say whether Revenue ever took the view that legal interpretation was a matter for the courts. But in the FOI material that was released, there was no discussion of the courts being the proper forum to arbitrate on the correctness of a long-standing Revenue interpretation of a WHT obligation. Instead, at the exact time a limited legislative amendment was wending its way through parliament, an expansive administrative solution was being discussed.

Finally, at one level, the events of 2010 are, in international tax terms, ancient history. The Double Irish Dutch Sandwich is a thing of the past.[90] There are a number of reasons for the obsolescence of the tax structure. First, BEPS Actions 8–10 have an impact on transfer pricing rules, as they attempt to align pricing with value creation and the economic substance of functions relating to the development, enhancement, maintenance, protection and exploitation of IP, rather than any contractual arrangements.[91] BEPS Actions 8–10 were introduced into Irish law in Finance Act 2019.[92] Secondly, Irish law governing the residence of companies was changed in 2015, with existing arrangements being grandfathered until December 2020. When combined with the third factor, namely the US legislative changes in 2017 which abolished the concept of deferral of US tax due on passive income, including royalties, it can be seen that the international tax landscape is changed. Finally, this changed landscape is both achieved and reflected in Ireland's 2021 commitment to the European Council that it would tackle aggressive tax planning, including outbound payments to zero tax jurisdictions or those on the EU list of non-cooperative jurisdictions, as part of the process of obtaining funding under an EU-funded Recovery and Resilience Plan.[93] This commitment followed the European Commission's view that the high

[89] Livingston, "Law, Culture, and Anthropology: On the Hopes and Limits of Comparative Tax" (2005) 18 *Canadian Journal of Law & Jurisprudence* 119, 121.

[90] Reuben Avi-Yonah, "International Taxation, Globalization, and the Economic Digital Divide" (2023) 26 *Journal of International Economic Law* 101.

[91] Mirna Screpante, "Rethinking the Arm's Length Principle and Its Impact on the IP License Model after OECD/G20 BEPS Actions 8–10: Nothing Changed but the Change?" (2019) *World Tax Journal* 425.

[92] See OECD, *Ireland: Transfer Pricing Country Profile*, December 2021, *https://www.oecd.org/tax/transfer-pricing/transfer-pricing-country-profile-ireland.pdf* [Accessed 14 February 2024].

[93] Department of Public Expenditure and Reform, *Ireland's National Recovery and Resilience Plan, Europe's Contribution to Ireland's Recovery* (2021), *https://www.gov.ie/en/publication/d4939-national-recovery-and-resilience-plan-2021/* [Accessed 14 February 2024]; Department of Finance, *New Taxation Measures to apply to Outbound*

level of outbound royalties from Ireland as problematic.[94] Fulfilling its commitment to the EU, Ireland enacted "outbound defensive measures" which come into force in 2024 or 2025 and impose WHT on royalty payments to zero tax jurisdictions or those listed as non-cooperative by the EU and impose a charge to Irish tax in respect of such royalties.[95]

This saga of administrative largesse in granting WHT exemptions through SP01/10 is ending. Yet the essence of state competition is to adapt to changed circumstances imposed by other states. The great game is likely to continue.

Appendix

Process and product of FOI requests

On 30 November 2020, an FOI request was issued to both the Department of Finance and Revenue Commissioners in the following terms:

> "I am issuing a FOI request in relation to the introduction of relief from withholding tax on royalties. Certain measures were introduced as follows:
>
> Section 55 Finance Act 2010 provided that withholding tax was not to apply to royalties paid by a company in the course of a trade or business to a company resident in a treaty country.
>
> Later in 2010 a statement of practice was issued by Revenue entitled 'Corporation Tax Statement of Practice SP—CT 01/10 Treatment of Certain Patent Royalties Paid to Companies Resident Outside the State'. This provided for no withholding tax on patent royalties in certain circumstances.
>
> I would like to request information (letters, emails, records of internal and external communications, minutes of internal and external meetings, phone calls, submissions, memos and briefing papers to ministers) relating to the following:
>
> 1. the reasons behind the introduction of the measures outlined above, including where those measures were considered in tandem;
> 2. any representations made to the Department of Finance and/or Revenue relating to the desirability or otherwise of introducing the measures outlined above by any of the following: any semi-state entity such as the IDA, groups, associations, private individuals, professional services firms or corporate entities;
> 3. any consideration of the representations at 2 above by the Department of Finance (including the Tax Strategy Group) and/or Revenue."

Between 19 and 22 January 2021, responses were received from the Department of Finance and Revenue Commissioners releasing certain information. There was substantial overlap in the material released by both Finance and Revenue. The material released by Revenue was from the international tax division and the business tax policy and legislation division, each of which made separate responses to the FOI request. Both Finance and Revenue refused to release certain specified documents, admitted to be pertinent to the FOI request, but exempt from release on certain statutory grounds.

The grounds on which records were either refused or released with redactions were as follows:

Payments, Feedback Statement (July 2023), *https://www.gov.ie/pdf/?file=https://assets.gov.ie/262836/924831a4-6671-4b40-865d-a2cd28b5ad7e.pdf#page=null* [Accessed 14 February 2024].

[94] Council Recommendation of 20 July 2020 on the 2020 National Reform Programme of Ireland and delivering a Council opinion on the 2020 Stability Programme of Ireland [2020] OJ C282/07 para.23.

[95] See Finance (No.2) Act 2023 s.36.

1. records relating to the deliberative process of the public body;[96]
2. records for the purpose of negotiations to be carried out by the government or any FOI body;[97]
3. records subject to legal professional privilege;[98]
4. records containing information which was provided confidentially to the FOI body;[99]
5. records involving the disclosure of personal information; and[100]
6. records which could reasonably be expected to affect adversely the international relations of the State.[101]

The initial release of material by Finance and Revenue under the FOI request was followed by an internal review, on request from this researcher. Some more records were released or previously released records were released with fewer redactions. Revenue and Finance listed the material which was, and was not, released. Any relevant records which were not released were linked to statutory exemptions from the obligation to release under FOI legislation as set out at 1 to 6 above.

The data can be described as a mixture of internal and external emails, memoranda of meetings and drafts of legislation and administrative practice. These are listed in schedules produced by Finance and Revenue.

On receipt of the internal review by Finance and Revenue, it was clear that a number of pertinent documents had not been released or had been redacted. An appeal was made to the Office of the Information Commissioner, an independent statutory body, who in August 2022 ruled that the two public bodies were justified in not releasing the remainder of the material.

An appeal to the High Court from the decision of the Information Commissioner would be possible but expensive. The data in this article is, therefore, based on which the two government bodies in Ireland, Finance and Revenue, considered necessary to publish in accordance with FOI legislation. Table 2 enumerates the data released under the FOI process.

Table 2: Summary of data relevant to the FOI request to Revenue and Finance

Public body	Number of relevant documents	Documents released in full	Documents partly released (redacted)	Documents not released
Revenue: Business Taxes Policy and Legislation Division	29	8	12	9
Revenue: International Tax Division	140	42	59	39
Department of Finance	25	3	21	1

96 Freedom of Information Act 2014 s.29(1).
97 Freedom of Information Act 2014 s.30(1)(c).
98 Freedom of Information Act 2014 s.31(1)(a).
99 Freedom of Information Act 2014 s.35(1)(a).
100 Freedom of Information Act 2014 s.37(1).
101 Freedom of Information Act 2014 s.33(1)(d).