

# Corporation Tax – General Background

## Part 02-02-01

This document is general in nature and should be read in conjunction with the relevant sections of the Taxes Consolidation Act 1997

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## 1. Charge to Corporation Tax:

A company resident in the State is, subject to some exceptions, chargeable to corporation tax on all its profits wherever they arise. A company's profits comprise its income and chargeable gains net of allowable losses. The charge covers profits accruing for the benefit of a company under any trust or arising under any partnership and extends to profits arising in its own winding up.

For corporation tax purposes the profits of a company are computed by reference to its "accounting periods". An accounting period is normally the period of 12 months for which the company makes up its accounts.

A non-resident company is not within the charge to corporation tax unless it carries on a trade in the State through a branch or agency (i.e. the concept of a "Permanent Establishment" \*). Where a non-resident company so carries on a trade, the company is chargeable on trading income arising directly or indirectly through or from the branch or agency, and on any other income arising from Irish sourced property or rights used by, or held by, or for the branch or agency. Corporation Tax may also be charged on certain chargeable gains. Income tax deducted from income forming part of a non-resident company's income is to be set off against any corporation tax liability on that income.<sup>1</sup>

\* Permanent establishment is defined in double taxation treaties, and in the OECD Model Convention on Income and Capital the term means "a fixed place of business through which the business of the enterprise is wholly or partly carried out."

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<sup>1</sup> This also applies to resident companies.

## 2. Rates of Corporation Tax:

The standard rate of corporation tax is 12.5% and generally applies to trading income. The standard rate also applies to certain foreign dividends (section 21B Taxes Consolidation Act 1997 (TCA 97)) and paragraph 8 of this instruction refers).

A 25% rate is charged on certain profits of companies. The 25% rate applies to non-trading income including income chargeable under Case III (e.g. discounts, interest, foreign income), Case IV (miscellaneous income) and Case V (rental income from land & buildings in the State) of Schedule D. Also included at this rate is income from activities which consist of working minerals, petroleum activities and dealing in or developing land, other than profits from construction operations (section 21A TCA).

## 3. Profits from dealing in development land:

Profits from a trade of dealing in development land (including residential development land) are subject to the 25% rate of corporation tax (section 21A TCA). Profits from dealing in development land include profits attributable to preparatory development work on land up to, but not including, laying of foundations. However, profits from a trade of dealing in fully developed land (i.e. land which is built on and cannot reasonably be further developed for at least 20 years) are subject to the 12.5 % corporation tax rate.

Gains realised on disposals of development land made on or after 6 December 2012 are liable to capital gains tax at the current rate of 33%.

#### 4. Company Capital Gains:

Companies' capital gains (other than gains from disposals of development land) are computed in accordance with capital gains tax principles. Companies' net chargeable gains are included in companies' profits for corporation tax purposes and are recalculated to give an amount which, when charged at the corporation tax rate, produces the same tax result as if the net gains were charged at the appropriate CGT rate (section 78 TCA).

#### 5. Company Residence:

A company resident in the State is liable to corporation tax on its worldwide profits, not just its Irish source profits. A company not resident in the State is not within the charge to corporation tax unless it carries on a trade in the State through a branch or agency (Permanent Establishment) and, where it does so, the company is chargeable to tax on all of its branch or agency profits, wherever arising. Foreign profits, within the charge to corporation tax, that suffer double taxation may be entitled to relief under Part 35 TCA.

The Finance Act 2014 introduced changes to the rules of residence for companies (section 23A TCA). As a result, different residence rules apply depending on when a company was incorporated.

##### **Company residence rules for companies incorporated after 1 January 2015**

Companies incorporated in Ireland on or after 1 January 2015 will be regarded as tax resident unless they are treated as resident in a treaty partner country by virtue of a Double Taxation Treaty.

**Company residence rules for companies incorporated before 1 January 2015**

For companies incorporated in Ireland before 1 January 2015, a transition period will apply until 31 December 2020. From this date they will be regarded as tax resident unless they are treated as resident in a treaty partner country by virtue of a Double Taxation Treaty. If, however, after 31 December 2014, there is both a change in ownership, and a major change in the nature and conduct of the business of the company then the company will be regarded as resident in Ireland from the date of the change in ownership.

Prior to the Finance Act 2014 changes, the 'central management and control' test (see below) was the general rule used to determine company residence. Under this rule, a company whose central management and control is exercised in Ireland (whether or not it was incorporated in Ireland) was regarded as resident in Ireland. Post Finance Act 2014, this rule will continue to apply on a transitional basis to Irish companies incorporated before 1 January 2015.

The central management and control rule was supplemented by rules introduced in Finance Act 1999 which provided that in certain circumstances, a company incorporated in Ireland would be regarded as tax resident in Ireland. Please see Tax and Duty Manual [Part 02-02-03](#) (Company Residence in the State) for further information.

**Company residence rules for companies that are not incorporated in Ireland**

The central management and control rule continues to apply to foreign incorporated companies. Accordingly, a company that is incorporated in a foreign country and is centrally managed and controlled in Ireland will be resident for tax purposes in Ireland.

### **The Central Management and Control Test**

The central management and control test came from decisions by the courts and has continued to exist alongside changes to the residence rules that have been introduced by the Finance Acts.

Where a company's central management and control lies is indicated by the highest level of control rather than normal day to day business transactions. Amongst the factors that may be taken into account are where the:

- important questions of company policy are determined;
- major investment decisions are made;
- negotiation of major contracts is undertaken;
- company's head office is; and
- majority of directors live.

A detailed explanation of the company residence rules may be found in Revenue's Tax and Duty Manual [Part 02-02-03](#) (Company Residence in the State).

## **6. Tax deductible expenses:**

When computing the amount of profits or gains to be charged to tax under Case I of Schedule D (trading income) a company is, in general, entitled to deductions in respect of revenue expenditure wholly and exclusively incurred for the purposes of its trade (section 81(2)(a) TCA). It is not, however, entitled to claim a deduction in respect of business entertainment expenses nor is it entitled to claim a deduction in respect of capital expenditure.

## 7. Capital Expenditure:

As a general rule a company is not entitled to claim a deduction in respect of capital expenditure. Where a company has depreciated capital assets for the purposes of computing its 'accounting' profit, the depreciation charges are added back when computing the profit for taxation purposes. However, the TCA provides relief in the form of capital allowances in respect of certain capital expenditure incurred. Capital allowances, usually in the form of wear and tear allowances and various types of industrial buildings allowances, are available for –

- industrial buildings (section 268)
- plant and machinery (section 284)
- energy-efficient equipment (section 285A)
- intangible assets (section 291A)
- dredging (section 303)
- vehicles (part 11C)
- commercial buildings in designated areas (part 10)
- third level education buildings (section 843)
- childcare facilities (section 843A)
- farm buildings (section 658)
- milk quotas (section 669B) (Please note that milk quotas were abolished with effect from 1 April 2015)
- mining and petroleum (part 24)
- scientific research (section 765)



- transmission capacity rights (section 769B)

Most of the property incentive schemes contained in Parts 9, 10 and 36 have been terminated, in so far as the termination dates for incurring qualifying capital expenditure have passed. There are two exceptions:

- The Living City Initiative (Chapter 13 of Part 10)
- Aviation Services Facilities (section 268(1)(n))

Capital allowances are given at different rates, depending on the particular asset, e.g. wear and tear allowances for plant and machinery are given at an annual rate of 12.5% of the capital expenditure over 8 years.

## 8. Dividends and other Distributions:

Dividends and other distributions made by a company (including certain types of interest) are not deductible in computing trading profits.

Dividends and other distributions made by Irish resident companies are subject to dividend withholding tax except where these are made to a non-resident person who is beneficially entitled to the distribution and who is within one of the categories of excluded persons set out in section 172D TCA.

Subject to certain exceptions (e.g. section 129A TCA), dividends received by Irish resident companies from other Irish resident companies are not chargeable to corporation tax.

Foreign dividends received by Irish companies are generally chargeable to corporation tax under Case III of Schedule D and such income is chargeable at the 25% rate of corporation tax. However, foreign dividends received by a company within the charge to Irish tax are chargeable to corporation tax at 12.5% where such dividends are received from a publicly quoted company or a company owned directly

or indirectly by such a company or, paid out of the trading profits of a non-resident company that is resident for tax purposes:

- (i) in an EU Member State,
- (ii) in a country, other than an EU Member State, with which Ireland has a tax treaty,
- (iii) in a country with which Ireland has signed a double taxation treaty which has yet to come into force,
- (iv) in a country, other than an EU Member State or a Treaty country, that has ratified the Joint Council of Europe/OECD Convention on Mutual Administrative Assistance in Tax Matters, or
- (v) in a non-treaty country where the company is owned directly or indirectly by a quoted company (section 21B TCA).

Notwithstanding that a dividend is not fully paid out of trading profits, the full amount of the dividend is treated as paid out of trading profits where -

- (i) 75% of the dividend paying company's profits are trading profits, either trading profits of that company or dividends received by it out of trading profits of lower tier companies that are resident in a country referred to in (i) to (iv) above; and
- (ii) An asset condition is satisfied on a consolidated basis by the company receiving the dividend and all companies that are its subsidiaries. The aggregate value at the end of the period concerned of the trading assets of those companies must not be less than 75% of the aggregate value of all their assets.

Special rules apply to the taxation of foreign dividends received by companies that are portfolio investors. A portfolio investor is an investor with a holding of not more than 5% of the share capital of the dividend paying company. Portfolio investors may, in general, treat a dividend received as being paid out of trading profits of the dividend paying company and this will be taxable under Case III of Schedule D at

12.5%. Dividends received from portfolio investments that form part of the trading income of a company are exempt from corporation tax.

## 8.1 Foreign Dividends – Additional Foreign Credit

Paragraph 9I of Schedule 24 TCA provides, in certain circumstances, for an additional credit for tax on foreign dividends. The credit is applicable to certain dividends paid directly out of the profits of companies resident in EU/EEA treaty-partner countries. Credit is also available for tax paid in third country jurisdictions if those profits are paid to Ireland via an EU/EEA treaty-partner resident company. The computation of the additional tax credit is based on the nominal rate of foreign tax which applies in the paying company's jurisdiction, rather than the effective rate of tax to which the profits, out of which the dividend is actually paid, are liable. Where the dividend received by the Irish company derives from untaxed profits of a paying company and is attributable indirectly through other dividend-paying companies to profits that have suffered foreign tax, the additional foreign credit is calculated by reference to the nominal rate of tax applicable to the profits of the company that have been subject to tax.

The total credit, including the additional credit, cannot exceed the Irish corporation tax attributable to the income. The additional credit is not eligible for pooling of credits or for carry forward of relief. Revenue will apply the provisions of paragraph 9I of Schedule 24 as respects foreign dividends paid on or after 1 January 2013.

### **Dividends paid out of untaxed income:**

Where a foreign dividend received by an Irish resident company is paid from untaxed profits of the paying company in an EU/EEA treaty-partner state and those profits are attributable through other dividend-paying companies to profits that have suffered tax, then the additional foreign tax credit is to be computed by reference to the rate per cent of tax applicable to the profits of the company that have been subject to tax. This situation could occur, for example, where the dividend income was not taxed in the hands of the paying company because it was received as

franked investment dividends in the foreign country concerned, or as cross-border dividends qualifying for the exemption method of double tax relief.

**Example:**

A UK company's after-tax profits are paid as a dividend to a Dutch company (where an exemption method of double tax relief is used), and subsequently paid by dividend to an Irish-resident company.

- The UK trading profits are taxed at 20%.
- The additional foreign tax credit is calculated by reference to the UK rate per cent of tax.

**“Subject to tax”:**

While the use of the phrase “subject to tax” is generally interpreted as imposing a requirement that tax is actually levied on income, where the profits of the paying company are extinguished by a group relief claim, the rate per cent of tax for the purposes of calculating the additional foreign credit is the nominal rate of tax, that corresponds to corporation tax in the State, in the paying company's jurisdiction.

Certain jurisdictions operate dividend participation exemption regimes based on exemption of 95%, or most, of the dividend concerned. The definition of “tax” in the legislation ensures that tax paid on such dividends will not give rise to an entitlement to an additional foreign tax credit based on the full value of the dividend at the nominal rate applicable in the paying company's jurisdiction.

**What is the position if the dividend paid to the Irish company is derived from various incomes of the paying company?**

Where the dividend received by an Irish company is derived from various incomes of the paying company, including its own earned profits that have been subject to tax as well as dividends received from one or more sources, then for the purposes of calculating the additional foreign credit the dividend is disaggregated into its

component parts which are treated as separate dividends. The appropriate rate per cent of tax applicable to the profits that have been subject to tax for each separate dividend is to be used in the formulae in paragraph 9I (4).

For example, if Irish Co. receives a dividend of €100,000 from Dutch Co. and the profits of the Dutch Co. are made up as follows:

Dividend from UK company 1 (no tax paid due to group relief)	€20,000
Dividend from UK company 2 (tax paid at 20%)	€30,000
Dutch investment income (taxed at 25% in The Netherlands)	€50,000

Each part is treated as a separate dividend.

- In the case of the UK company 1 dividend; the nominal rate to be used is the UK rate.
- For the UK company 2 dividend; the rate to be used is the also the nominal rate (20%).
- For the final “separate dividend”; the rate to be used is the Dutch nominal rate (25%).

Revenue will apply the provisions of subparagraph (4A) of paragraph 9I of Schedule 24, to foreign dividends paid on or after 1 January 2013 (the date from which the additional foreign tax credit under paragraph 9I is applicable).

## 9. Relief for pre-trading expenditure:

Expenditure which is wholly and exclusively laid out for the purposes of a company's trade or profession in a three-year period before commencement is allowed as a deduction in calculating the trading income of that trade or profession following commencement (section 82 TCA).

## 10. Exemptions from Corporation Tax:

Provisions of the Income Tax Acts conferring an exemption from income tax have a like effect for corporation tax so far as is consistent with the Corporation Tax Acts. Thus, a company which would be exempt as a charity from income tax on its income is also exempt from corporation tax.

Part 7 TCA Chapters 2 and 3 exempts income from certain bodies from corporation tax. Chapter 3 (section 227 TCA) refers to the exemption from corporation tax of "Certain income arising to specified non-commercial state-sponsored bodies". A full list of these bodies is contained in Schedule 4 to the TCA.

## 11. Tax relief for new start-up companies (section 486C TCA):

Section 486C TCA provides relief from corporation tax for new start-up companies for the first 3 years of trading. The relief is provided in respect of profits of a new trade and chargeable gains on the disposal of assets used in the trade. Relief applies where the total corporation tax payable for an accounting period does not exceed €40,000, with marginal relief available where total corporation tax payable is between €40,000 and €60,000.

Finance Act 2011 modified the existing relief so that the value of the relief will be linked to the amount of employers' PRSI paid by a company in an accounting period, subject to a maximum of €5,000 per employee and an overall limit of €40,000.

Finance Act 2011 also excludes a trade set up by a new company, the activities of which, if carried on by an associated company of the new company, would form part of an existing trade carried on by that associated company.

Finance Act 2013 provided for enhancement of the relief by allowing any unused relief arising in the first 3 years of trading, due to losses or insufficient profits, to be carried forward for use in subsequent years. The amount of relief is restricted by reference to the total employers' PRSI contributions for each year in respect of the company's employees (subject to an overall limit of €40,000 in any one year).

Finance Act 2015 extended the relief to companies which commence a trade at any time in the period beginning on 1/1/09 and ending on 31/12/18.

## 12. Loss Relief:

Trading losses, other than terminal loss relief, must be claimed within two years of the end of the period in which the loss is made. A company incurring a trading loss in an accounting period can:

- offset the loss against other trading income of the company for the current accounting period,
- carry the loss back for offset against trading income of its immediately preceding accounting period,
- any excess may be used on a value basis against the corporation tax chargeable on the company (see 12.1. below)
- any excess may be carried forward for offset against trading profits (of the same trade) in subsequent accounting periods,
- any excess may be offset against the trading income of another group member for the current accounting period (group defined by reference to 75% ownership/ control, (see section 11 TCA).

- any excess may be offset on a value basis against the corporation tax chargeable on another group company.

## 12.1 Value Basis Relief

Where a company has losses, these losses may be offset on a value basis against corporation tax for the current accounting period and the previous accounting period of the same length (section 396 TCA 1997). To the extent that the excess amount consists of a 12.5% trading loss, corporation tax for the company is reduced by 12.5% of that loss.

### Example of value basis relief

Chargeable gain	100,000
Tax on chargeable gain (100,000 x 33%)	33,000
Unused trading loss	100,000
Relief on a value basis	<u>12,500</u>
Net liability	20,500

## 12.2 Terminal loss relief

Where a company incurs a loss in its final period of trading, terminal loss relief is available under which trading losses in the last 12 months of the trade may be set off against trading income of the preceding 3 years (section 397 TCA).

## 12.3 Case IV & V losses

A Case IV loss may be offset against other Case IV income of the same accounting period and then carried forward against future Case IV income (Section 399 TCA).



Case V (i.e. rental) losses may be carried back and offset against Case V income of the preceding period and any remaining loss may be carried forward for offset against future Case V income.

#### 12.4 Other losses

It should be noted that specific provisions apply to losses from dealing in residential development land (section 644AA and 644C TCA).

The availability of loss relief is restricted in the case of certain trades and activities (for example sections 403, 404, 405, 406, 407, 687, 753 & 1013 TCA).

In the case of losses incurred by a foreign branch of an Irish resident company, such losses are included in the Irish company's tax computation as an Irish resident company is chargeable to tax on its worldwide income.

### 13. Group Relief:

Trading losses, and other amounts such as excess management expenses and charges on income and trading losses incurred by non-resident companies and other amounts not otherwise eligible for relief from corporation tax, may be surrendered by a company which is a member of a group of companies and the relief given to another company in the same group. This is termed "group relief".

### 13.1 What are the conditions to claim the relief?

Two companies are members of the same group if one is a subsidiary of the other or both are subsidiaries of a third company, the parent/subsidiary relationship being determined according to the test of not less than 75% per cent ownership of the ordinary share capital. Section 411 TCA sets out the criteria for a group relationship.

Originally, to be in a “group”, all of the companies had to be Irish resident. However, this was held to be discriminatory under EU law in a landmark UK case (ICI V Colmer). In order to meet the requirements of that case, Finance Act 1999 extended group relief for trading losses to situations where the parent company was EU/EEA treaty-partner resident.

The legislation was further expanded in Finance Act 2012 to allow a group relationship exist where a parent is listed on recognised stock exchange and all other members of the group are resident in EU/EEA treaty-partner countries or countries with which we have a treaty. It should be noted that the stock exchange criteria do not extend to subsidiary companies in a group. The extension to allow companies listed on exchanges into the group was limited to the parent company of a group only, and all other members of the group must be EU/EEA treaty-partner resident, or resident in country with which we have a treaty.

## 14. Deposit Interest:

The general position in relation to deposit interest is that it is *prima facie* passive income and is assessable as Case III/IV income (25%). However, Revenue will accept that deposit interest arising in two specific circumstances is assessable as Case I income. These are in relation to:

- (a) where a Regulatory Capital Requirement exists,

for example, where a company is required by Irish or foreign regulatory authorities to retain a certain level of permanent capital in the business, any deposit interest which derives from the investment of such regulatory capital is assessable as Case I, and

(b) where Capital is integral to the trade – for example where deposits are regarded as integral to the trades of banking, insurance and some classes of financial services companies.

## 15. R&D Credit relief:

Please see Tax and Duty Manual [Part 29](#) for further information in relation to relief available for R&D.