Irish Tax Monitor

Interest Limitation Rules

With new reporting requirements around interest limitation rules required for accounting periods from 1st January 2022, what steps could corporates be taking to meet obligations under the rules?

Conall Brennan-McMahon, Tax Consultant, Maples Group: The interest limitation rules aim to restrict a company's interest deductions to 30% of its EBITDA. Ireland was required to implement the rules in accordance with Council Directive (EU) 2016/1164, and they are contained in Part 35D of the Taxes Consolidation Act, 1997.

Many Irish companies have now filed a corporation tax return for the financial year ended in 2022 based on the new rules and are already taking steps to manage their ongoing obligations. Practically, auditors and tax compliance providers expect companies to obtain written advice on how the rules apply to the most recent set of accounts. It is likely that some form of this advice will be required for each future accounting period.

We have advised a number of Irish corporate and investment structures on the new rules and have seen companies take several approaches to managing them. Given that interest rates continue to rise – and so does the risk associated with the rules – it is worth considering whether the strategy adopted in 2022 remains appropriate for 2023 and beyond.


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From a policy standpoint, there are two main ways to protect the tax base from excessive interest deductions. One is to apply a maximum interest-to-EBITDA ratio, which is vulnerable to interest rate changes. The other is to apply a maximum debt-to-assets ratio, which encourages gearing up to the allowable level. The debt-to-assets ratio is the approach favoured in New Zealand and, until recently, Australia.

When the EU Member States agreed to adopt an EBITDA-based interest limitation measure in 2016 (following the OECD's recommendation), the European Central Bank's main lending rate was exactly 0%. Today, it is 4.5%.

The effect of that movement on private debt, including transfer-priced intercompany debt, devalues the rules' €3m de minimis exemption. By way of rudimentary example, €3m of interest expense at a 3.5% rate equates to €86m of debt. With an 8% rate and the same amount of interest expense, the debt is €38m. A company could reduce the size of its debt between 2022 and 2023 and yet have a worse outcome under the rules. This is not just a remote possibility, as we are seeing banks' appetite to lend into the corporate and real estate markets decline in the second half of 2023.

Where companies exceed the €3m de minimis threshold, we expect to see greater reliance on measures relating to groups. These measures include elections to:

- form a domestic interest group treated as a single entity under the rules;
- replace the 30% company-level EBITDA limit with the worldwide group's ratio of interest expense to EBITDA; or
- exempt a company whose ratio of equity to total assets is no more than 2% below that of the worldwide group.

The last of these measures effectively switches the rules into applying a debt-to-assets ratio. However, the concept of a worldwide group requires careful consideration. It is defined by reference to an accounting consolidation test. Companies should consider what information they need to gather from other entities globally to access the relief, especially where they have a complex multinational structure.

We are also seeing companies engage with their lenders on the terms of existing debt. Borrowers may seek amendments to loan facility agreements in order to address issues such as loan to value covenants. The loans may predate the advent of the rules (in June 2016), so the amendment risks removing the loan from the exclusion for legacy debt. Amendments and restatements need close attention to avoid an unintended application of the rules.

We have acted on a number of transactions where the rules have featured as a covenant or warranty in facility agreements. Typically, the borrower agrees to report on any impact to the lender or to provide the lender with copies of advice, sometimes in advance, on whether the rules cause additional tax liabilities to arise. The breach of such covenants could cause a dispute with the lender, especially if the lender has concerns on other issues such as the borrower's solvency.

For companies whose net interest expense remains below €3m, availing of the de minimis exemption provides a complete defence from the rules. Companies that benefited from this exemption in 2022 should continue to monitor interest expense and interest income to calculate whether the exemption is still available for 2023. Unless an election is made to form an interest group, the de minimis exemption applies on a company-by-company basis. There may be merit in considering whether certain activities may be carried out in a separate company.

Although the rules are not entirely fit for purpose, they are unlikely to change in the near future. As time goes on, companies will at least become more accustomed to managing them. When viewed together with the implementation of Pillar Two and other areas of international tax reform, the rules make having appropriate tax processes and controls as relevant as ever.