2 April 2025

Section 831B Taxes Consolidation Act (TCA) 1997
Feedback on the Participation Exemption for Certain Foreign Distributions

We refer to the email from the Department of Finance of 24 March requesting additional feedback on two areas raised in our submission dated 7 March in respect of section 831B TCA 1997. We outline below our response to the queries raised by the Department.

Deductible Dividends

1. **Department of Finance: You mention in your submission that there are circumstances where a dividend may be deductible under the terms of an anti-avoidance provision but not deductible generally against income tax. The scenario provided sets out how US personal holding company rules may subject a personal holding company tax. In relation to this scenario, can you please provide further clarification in the form of a hypothetical example how this can occur? If you have any additional information on how other jurisdictions account for the same that would be welcome.**

ITI Response

As noted in our submission of 7 March, for US federal corporate income tax purposes, in general a corporation will be considered a personal holding company if (a) at least 60% of the corporation's adjusted ordinary gross income for the tax year is from certain dividends, interest, rent, royalties, and annuities; and (b) at any time during the last half of the tax year, 5 or fewer individuals directly or indirectly own more than 50% in value of the corporation's outstanding stock.[1]

Under the US personal holding company rules, in addition to paying “ordinary” US federal corporate income tax, a personal holding company is subject to an additional tax (called a

[1] U.S. Code § 542

personal holding company tax) on its undistributed personal holding company income (as defined) equal to 20% of that undistributed personal holding company income. [2]

The relevant legislation[3] provides that a personal holding company's "*undistributed personal holding company income"* is its taxable income (subject to various adjustments) "minus" the dividends paid during the taxable year and certain other dividends.[4]

Applying the above to an illustrative example:

- Ire DAC holds 100% of the shares of US Corp (and has done for more than 5 years) and it receives a dividend from US Corp of $100,000 which is made out of US Corp's operating profits of $300,000. This distribution was not deductible in computing US Corp's (ordinary) federal income tax liability for the period (i.e., US federal income tax is paid on profits of $300,000).

- Ire DAC is wholly owned by Bob Smith making Ire DAC a close company for Irish tax purposes and US Corp a personal holding company for US federal income tax purposes.

- As a personal holding company, US Corp is subject to a personal holding company tax at a rate of 20% on its undistributed personal holding company income. This income comprises the company's taxable income (i.e. $300,000) but in computing the taxable amount certain adjustments are to be made, one of which is the deduction of the $100,000 dividend paid to Ire DAC during the year. Therefore, the amount subject to personal holding company tax is $200,000 (subject to any other prescribed adjustments).

- Ire DAC satisfies all of the requirements in section 831B TCA 1997; however, for the exemption to apply the dividend must be a 'relevant distribution'.

Sub-part (I) of the definition of 'relevant distribution' excludes any distribution which is *"deducted for the purposes of tax in any territory outside the State under the laws of that territory."*

[2] ibid
[3] U.S. Code § 545
[4] U.S. Code § 561, U.S. Code § 563

On a plain reading, the distribution to Ire DAC does not appear to meet the definition of a 'relevant distribution' because while the distribution was not deductible for US federal income tax purposes in general, it was deductible in computing the amount subject to the personal holding company tax.

As noted in our previous submission, the personal holding company tax is a counterpart to the Irish close company rules. Both regimes represent a policy choice to encourage closely held companies to distribute their profits to their owners (with the intention that those owners will then pay tax on those dividends). The Irish framing is slightly different in that it does not explicitly refer to a deduction from surchargeable income for distributions paid. Section 440 TCA 1997, which provides for a surcharge on estate and investment income, states:

> *"Where for an accounting period of a close company the [distributable estate and investment income] exceeds the distributions of the company for the accounting period, there shall be charged on the company an additional duty of corporation tax (in this section referred to as a "surcharge") amounting to 20 per cent of the excess."*

Whereas the US personal holding company legislation says that the taxable amount is the taxable income computed under ordinary US federal income tax rules "minus" dividends paid.

Despite the slightly different formulation the effect (and policy intent) is the same. It would seem unreasonable to preclude a dividend from qualifying for the Irish participation exemption in circumstances such as these given that the dividend is not deducted for general US federal income tax purposes but rather for a specific additional charge where the reason for allowing the deduction is to achieve the policy intent underpinning that charge i.e., to encourage closely held companies to distribute their profits and in doing so reduce the amount that would otherwise be subject to a surcharge.

These circumstances are clearly very different to a situation where a foreign company is able to reduce its general corporate income tax liability by means of making distributions out to its members. We note that the impact of the restriction in circumstances such as these is likely to be predominantly borne by privately owned Irish groups rather than large multinational groups.

We recommend that the legislation is amended to provide that a distribution will still be a relevant distribution where it is taken into account (by means of deduction, reduction, or otherwise) in computing a tax that corresponds to a close company surcharge in the State so long as it is not deducted for the purposes of a tax in a foreign territory which corresponds to corporation tax in the State (other than a surcharge levied under Part 13).

Acquisition of Shares

2. **Department of Finance: In relation to the acquisition of shares you mention you have sought clarification in Revenue's TDM that it can be accepted for the purposes of section 831B, the terms 'business' and 'assets used for the purposes of a business' do not include shareholdings in another company. It is set out that such an interpretation would be appropriate in a section 831B context where neither the transferor nor the transferee entities held or hold the shares as trading assets. In order to allow us to better understand this fully, can you please provide a worked hypothetical example of this?**

ITI Response

In our submission of 7 March, we sought clarity on the policy intention that, for the purposes of condition (b), the terms "business" and "assets used for the purposes of a business" do not include shareholdings in another company. We have included two examples below which illustrate the points raised, as requested.

Example 1: 100% shareholding in DTA-resident subsidiary acquired by DTA-resident subsidiary from third party Irish resident company

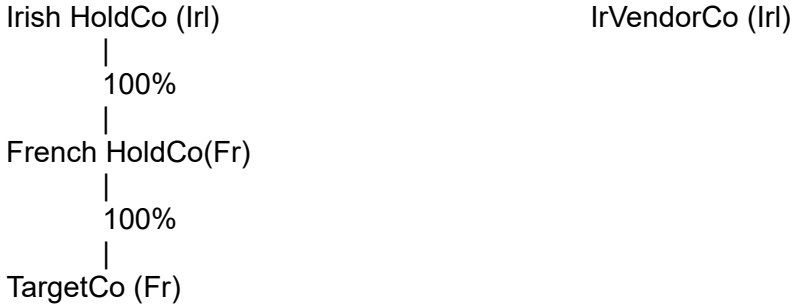
Facts

- Irish resident disposing third-party company (IRVendorCo) has held French resident target company (Target Co) for a number of years and qualifies for section 831B on dividends from TargetCo.
- Irish HoldCo owns an existing French intermediate HoldCo (French HoldCo) as its local investment platform through which it makes its French nexus investments. Prior to the proposed acquisition below, Irish HoldCo currently qualifies for section 831B treatment in respect of dividends from French HoldCo.
- French HoldCo intends to purchase TargetCo from (IRVendorCo) for full market value.

- Post the acquisition of TargetCo by French HoldCo, the Irish HoldCo expects to continue to be able to qualify for section 831B treatment on dividends from French HoldCo.

Pre-acquisition position

Post-acquisition position



If the shareholding in TargetCo is considered a “business” or “assets used for the purposes of” a business of the Irish Resident vendor, then Irish HoldCo will not qualify for section 831B for at least 5 years in respect of dividends it receives going forward from its existing French subsidiary (French HoldCo) as it will have acquired either a “business” or “assets used for the purposes of” a business by a resident of a non-relevant territory (i.e. from an Irish resident vendor). If the vendor was a French or Dutch resident instead of being Irish resident then the question of whether or not the shares constitute a “business” or “assets used for the purposes of” a business is inconsequential as it would not be an acquisition from a non-relevant territory resident.

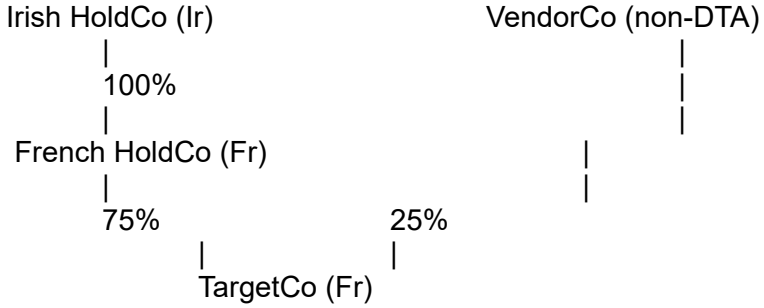
There would appear to be no policy rationale to interpret “business” or “assets used for the purposes of” a business as including shares in the above context. It is unclear exactly what ‘mischief’ such a restriction is being aimed at if the policy intention was to have “business” or “assets used for the purpose of” a business as including shares.

Example 2: 25% shareholding in DTA-resident subsidiary acquired by DTA-resident subsidiary from third party non-DTA resident company

Facts

- Non-DTA resident disposing third party company (Vendor Co) has held the 25% interest in a French resident target company (Target Co) for a number of years as part of a joint venture arrangement with existing French intermediate holding company (French Holdco).
- Irish HoldCo owns French HoldCo as its local investment platform through which it makes its French nexus investments. Prior to the proposed acquisition below, Irish HoldCo currently qualifies for section 831B treatment in respect of dividends from French HoldCo.
- French HoldCo intends to purchase the 25% stake held by Vendor Co in TargetCo such that it becomes the 100% shareholder in TargetCo going forward.
- Post the acquisition of the additional 25% stake in TargetCo by French HoldCo, the Irish HoldCo expects to continue to be able to qualify for S831B treatment on dividends from French HoldCo.

<u>Pre-acquisition position</u>



<u>Post-acquisition position</u>

If the 25% shareholding in TargetCo held by a non-DTA resident vendor is considered an "asset used for the purposes of" a business bythat non-DTA resident vendor, then French HoldCo will not qualify for section 831B for at least 5 years as it will have acquired an "asset used for the purposes of" a business by a resident of a non-relevant territory. There would appear to be no policy rationale to interpret "assets used for the purposes of" a business to include a 25% shareholding in the above context.

It is unclear exactly what 'mischief' such a restriction is being aimed at if the policy intention was to have "business" or "assets used for the purposes of" a business as including shares.

Recommendation

If the policy intention is not to include the type of scenarios outlined, and indeed we have not identified a basis for a contrary policy, we would welcome clarity either by way of a legislative amendment or by way of affirmation in Revenue guidance. A technical basis supporting any policy intent that share acquisitions should not impact on an entitlement to the participation exemption is outlined below should the guidance route be preferred.

Guidance might specify that although shares are arguably the subject matter of an investment made by a holding company in the course of its business of being a holding company (that being an investment business), those shares should still not be considered assets "used for the purposes of the business" in the context of section 831B as that term is more appropriately applicable to the assets that form the apparatus of the business as opposed to assets which are the subject matter of the business. The distinction is an important one if section 831B is to operate in line with its stated intended policy objectives.

Examples of assets used for the purpose of a holding/investment company business might include know-how (such as industry knowledge in assessing whether or not to invest or divest), capital (i.e. the means by which shares are acquired), business infrastructure arrangements (e.g. human capital such as employee arrangements to carry out functions/activities of the business, real estate such as access to office space for employees/directors, etc.). Such assets are part of the apparatus by which the business operates and thus may be regarded as assets "used for the purpose of" that business.

We would submit that shares, whilst being the subject matter of the business of investment, might not be categorised in the same way as the above mentioned types of assets which

form the infrastructure of a business such that they too are considered “used for the purpose of” the investment business in a section 831B context.

Support for the above interpretation of the term “business” in any Revenue guidance and the view to be taken of assets “used for the purposes of” a business in the context of holding companies and their shareholdings can be found in section 247 TCA 1997, a section which is of particular relevance given that it applies to holding companies in respect of borrowings to fund shareholding investments.

Section 247 can have application to a company “whose business consists wholly or mainly of the holding of stocks, shares or securities” where that company uses borrowed funds to acquire ordinary share capital in companies carrying on particular activities. Paying particular attention to the underlined terms, the approach of the draftsperson of section 247 was to view the “business” of such holding companies to be the “holding of … shares”.

In other words, the subject matter of the “business” of the company is the shares but the “business” of the company is not the shareholding. The structure of section 247, a provision primarily of relevance to holding companies (in the same way section 831B is primarily of relevance to holding companies) therefore is to take the approach that the business of a holding company is to be viewed as that of holding shares and not to view the shareholdings held by such a company as themselves being the “business”.

A similar approach to that of section 247 TCA 1997 has been adopted elsewhere in section 83 TCA 1997, a provision which is relevant to investment companies, where reference is made to it applying to a “company whose business consists wholly or mainly of the making of investments”. Again, the emphasis therein being on the business being the activity (i.e. the act or acts of making investments) with the subject matter of those acts (i.e. investments), such as shares, being something separate to the “business” or indeed the assets used for the purpose of the making of those investments.

On this basis a disposal of a shareholding may generally be said not to constitute a disposal of its business or part of its business as the “infrastructure” of the business will remain behind in the holding company post sale and it can continue that business in an unabated manner if it so wishes. The point was made in the UK case of Baytrust Holdings Limited v IRC (50 ATC 136) as follows:

"*A greengrocer's business is no doubt to sell fruit, but the pound of apples which you buy can hardly be described as a purchase of part of the greengrocer's business.*"

To interpret the meaning of the terms "business" and "assets used for the purposes of a business" otherwise than in the above manner would potentially mean that EU resident companies that acquire shares from Irish resident companies cannot qualify as a 'relevant subsidiary' of a 'parent company' for five years post any such acquisition.

Appendix 1
Extracts from U.S. Code dealing with personal holding companies

U.S. Code § 541 - Imposition of personal holding company tax

In addition to other taxes imposed by this chapter, there is hereby imposed for each taxable year on the undistributed personal holding company income (as defined in section 545) of every personal holding company (as defined in section 542) a personal holding company tax equal to 20 percent of the undistributed personal holding company income.

U.S. Code § 542 - Definition of personal holding company

(a) General rule

For purposes of this subtitle, the term “personal holding company” means any corporation (other than a corporation described in subsection (c)) if—

(1) Adjusted ordinary gross income requirement

At least 60 percent of its adjusted ordinary gross income (as defined in section 543(b)(2)) for the taxable year is personal holding company income (as defined in section 543(a)), and

(2) Stock ownership requirement

At any time during the last half of the taxable year more than 50 percent in value of its outstanding stock is owned, directly or indirectly, by or for not more than 5 individuals. For purposes of this paragraph, an organization described in section 401(a), 501(c)(17), or 509(a) or a portion of a trust permanently set aside or to be used exclusively for the purposes described in section 642(c) or a corresponding provision of a prior income tax law shall be considered an individual.

U.S. Code § 545 - Undistributed personal holding company income

(a) Definition

For purposes of this part, the term “undistributed personal holding company income” means the taxable income of a personal holding company adjusted in the manner provided in subsections (b), (c), and (d), minus the dividends paid deduction as defined in section 561. In the case of a personal holding company which is a foreign corporation, not more than 10 percent in value of the outstanding stock of which is owned (within the meaning of section 958(a)) during the last half of the taxable year by United States persons, the term “undistributed personal holding company income” means the amount determined by multiplying the undistributed personal holding company income (determined without regard to this sentence) by the percentage in value of its outstanding stock which is the greatest percentage in value of its outstanding stock so owned by United States persons on any one day during such period.

U.S. Code § 561 - Definition of deduction for dividends paid

(a) General rule

The deduction for dividends paid shall be the sum of—

(1) the dividends paid during the taxable year,
(2) the consent dividends for the taxable year (determined under section 565), and
(3) in the case of a personal holding company, the dividend carryover described in section 564.

(b) Special rules applicable

In determining the deduction for dividends paid, the rules provided in section 562 (relating to rules applicable in determining dividends eligible for dividends paid deduction) and section 563 (relating to dividends paid after the close of the taxable year) shall be applicable.

U.S. Code § 563 - Rules relating to dividends paid after close of taxable year

(a) Accumulated earnings tax

In the determination of the dividends paid deduction for purposes of the accumulated earnings tax imposed by section 531, a dividend paid after the close of any taxable year and on or before the 15th day of the fourth month following the close of such taxable year shall be considered as paid during such taxable year.

(b) Personal holding company tax

In the determination of the dividends paid deduction for purposes of the personal holding company tax imposed by section 541, a dividend paid after the close of any taxable year and on or before the 15th day of the fourth month following the close of such taxable year shall, to the extent the taxpayer elects in its return for the taxable year, be considered as paid during such taxable year. The amount allowed as a dividend by reason of the application of this subsection with respect to any taxable year shall not exceed either—

(1) The undistributed personal holding company income of the corporation for the taxable year, computed without regard to this subsection, or

(2) 20 percent of the sum of the dividends paid during the taxable year, computed without regard to this subsection.

(c) Dividends considered as paid on last day of taxable year

For the purpose of applying section 562(a), with respect to distributions under subsection (a) or (b) of this section, a distribution made after the close of a taxable year and on or before the 15th day of the fourth month following the close of the taxable year shall be considered as made on the last day of such taxable year.