24 February 2025

Outbound Payments Defensive Measures
Feedback on Proposed Draft Amendments to Section 817U TCA 1997

We refer to the draft text of proposed amendments to section 817U TCA 1997 which was circulated by the Department of Finance on 17 February for feedback. We understand the intention of the proposed amendments is to ensure that two enterprises, which are associates of the same individual, are treated as associated enterprises of each other for the purposes of the outbound payments defensive measures. The draft amendments comprise a proposed new subsection 3(f) and a new subsection 3A into section 817U.

Section 10 TCA 1997

We are concerned with the use of the connected person definition from section 10 TCA 1997, as we consider it to be too broad in its scope and goes far beyond what may be necessary. We outline below two particular areas of concern in this regard.

Acting together

Section 10(8) provides:

> *"Any 2 or more persons acting together to secure or exercise control of, or to acquire a holding in, a company shall be treated in relation to that company as connected with one another and with any person acting on the direction of any of them to secure or exercise control of, or to acquire a holding in, the company."*

If this provision is applied in the context of the outbound payments defensive measures, we believe it will capture many scenarios which are presumably not within the intended scope of that legislation.

Take the example of an individual who owns a 1% shareholding in a company with a shareholders' agreement in place where the other shares are owned by unrelated third parties. In those circumstances, the individual (the 1% shareholder) could be considered to be connected with the company, even though the individual only owns 1% and is not connected with other third-party investors in that company. We do not believe the policy intention is that the rules should apply to such a case.

In addition, Revenue's Tax and Duty Manual (TDM) 35C-00-01 indicates that partners in a partnership can be deemed to be acting together simply by being in partnership together. If this interpretation is applied in the context of the outbound payment defensive measures, it would mean that each of the partners in a partnership would automatically be treated as connected parties under Section 10(8) TCA 1997. This in turn would mean that all partners' interests would be automatically aggregated. Therefore, each partner would automatically be an associated entity of any 50% subsidiary held by the partnership. Furthermore, it would also seem to be the case that the subsidiary would then become an associated entity of any other company in which any partner in the partnership separately had a 50%+ interest. It is for this reason that the following exclusion was included in section 835AVA (2) (c) TCA 1997 under the anti-reverse-hybrid rules:

> *"…two entities shall not be treated as acting together with respect to voting rights, share ownership rights or similar ownership rights solely because they are partners in a partnership."*

Partnerships

In addition to the impact on partners in the partnership of the acting together provisions outlined above, there is a specific rule relating to partnerships in section 10(5) TCA 1997, as follows:

> *"Except in relation to acquisitions or disposals of partnership assets pursuant to bona fide commercial arrangements, a person shall be connected with any*

person with whom such person is in partnership, and with the spouse [or civil partner or a relative of any individual with whom such person is in partnership.

The question of how partners in a partnership should be evaluated from an association perspective is addressed in Revenue's Tax and Duty Manual 35C-00-01 on the anti-hybrid rules which states the following (noting that for the purposes of the anti-hybrid rules the association test is 25% rather than the 50% in the outbound payments defensive measures):

"7.3 Application of the "associated enterprises" test to Irish partnerships

7.3.1 Having regard to the capital of the entity

Paragraph (a), (b) and (c) *–*

Where an enterprise (partner) directly, or indirectly, possesses or is beneficially entitled to not less than 25% of the ownership rights, voting power or rights to profits in an Irish partnership that enterprise (partner) and the Irish partnership shall be "associated enterprises" in respect of each other.

As an Irish partnership does not have separate legal personality, it cannot itself own assets. Irish partnership property is instead held by the partners as tenants in common. Under Irish partnership law, partners are not legally entitled individually to exercise proprietary rights over any of the partnership assets but rather they are collectively entitled to each and every asset of the partnership, in which each of them has an undivided share.

Therefore, in applying the "associated enterprises" test where an Irish partnership holds a subsidiary entity (or entities) it is necessary to look through the partnership to the partners when examining the ownership rights, voting rights and/or rights to profits in that subsidiary entity.

It follows that where a partnership holds an investment of 25 per cent or more in a subsidiary entity each partner and the subsidiary entity shall be regarded as "associated enterprises" in respect of each other.

The Irish partnership and the subsidiary entity shall be regarded as "associated enterprises" in respect of each other where paragraph (d) applies.

Paragraph (d) *–*

Where an Irish partnership holds an investment of not less than 25 percent in a subsidiary entity, each of the partners and that subsidiary entity shall be regarded as "associated enterprises" in respect of each other. Where one of those partners and the partnership are also regarded as "associated enterprises" in respect of each other where, for example, that partner owns not less than a 25 per cent investment in the partnership then it follows that the partnership and the subsidiary entity shall also be regarded as "associated enterprises" in respect of each other by virtue of their association with that partner."

It follows from the above extract that where a partnership has a 50%+ interest in a subsidiary company, then each and every partner in that partnership would be deemed to be an associated enterprise of the company. This would be the case even if the partnership had 100 different partners each of which only had a 1% interest in the partnership (and hence an indirect interest of only 1% in the subsidiary company). Furthermore, it would also seem to be the case that the subsidiary would then become an associated entity of any other company in which any partner in the partnership separately had a 50%+ interest.

We note the provisions in in new draft subsection (3A) whereby a threshold of 5% is provided, such that in the case where a partner has a less than 5% interest, this should not arise. However, we would suggest that this approach overlooks the fundamental point that had all of the partners held their shares directly in the company they would not be associates of each other and the only reason that they could become so is purely because of the existence of the partnership.

In the context of what the outbound payments defensive measures are attempting to achieve from a tax policy perspective, we believe it is unreasonable to deem two otherwise unconnected partners to be associates simply because they happen to have invested in the same partnership.

Specific observations on the draft text

Section 817U(3A)(a)(i):"Ownership rights"

We believe that the reference to "ownership rights" in section 817U(3A)(a)(i) TCA 1997 is too vague when assessed in the context of an individual's interest in a partnership.

It addresses instances where the first mentioned *individual's "interest in the ownership rights of the partnership"* is less than 5%. Ownership rights is already referred to in the proposed new section 817U(3)(f) in respect of an entity which is an entity not having share capital, but it is unclear as to how such ownership interests can arise with respect to a partnership.

As an Irish partnership does not have separate legal personality, it cannot itself own assets. Instead, Irish partnership property is held by the partners as tenants in common. Under Irish partnership law, partners are not legally entitled individually to exercise proprietary rights over any of the partnership assets but rather they are collectively entitled to each and every asset of the partnership, in which each of them has an undivided share.

While a partner in a partnership has a right to the profits in line with their profit-sharing ratio, such a ratio cannot be accurately described as being an ownership interest akin in the same manner as, for example, share ownership. The point is succinctly illustrated by Twomey on Partnership at 19.04[i] where it was noted that the share of each partner is only the share of the clear surplus which would remain after the payment of all of the debts.

We have recommended below an alternative as to how to define the connected individual provisions in section 817U. However, if the approach proposed in the draft text is retained, we believe it would be more appropriate to frame the test by reference to the individual's interest in the profits of the partnership.

Section 817U(3A)(a)

We consider the proposed amendment does not adequately cater for a scenario where an individual is a partner in multiple partnerships. A scenario could arise where two individuals meet the conditions of section 817U(3A)(a)(i) and (ii) when viewed in isolation but fail the test by virtue of being limited partners in a separate partnership arrangement (due to the individuals being connected under section 10). In our view, this outcome would seem counterintuitive where the individuals are acting as limited partners in the partnerships.

Section 817U(3A): 5% interest in the partnership

We believe the requirement that an individual's interest in the partnership be less than 5% is overly restrictive. We have recommended below an alternative as to how to define the connected individual provisions in section 817U. However, if the approach in the draft text is retained, where an individual is acting as a limited partner, we believe that section 817U(3A) should apply in circumstances where the limited partner does not have an entitlement to more than 50% of the profits of the partnership.

Institute Recommendations

Definition of connected person

We believe that there should only be an attribution to the individual of the interests of his/her spouse, brother, sister, ancestor and lineal descendants. As such, the amendment could be framed without a reference to section 10 and instead, provide that:

An individual shall be connected with another individual if that person is the individual's husband, wife or civil partner, or is a relative, or lineal descendant of that person.

If policymakers deem it absolutely necessary to adopt the provisions of section 10 TCA 1997 in general, we suggest that the proposed subsection 3A be replaced with the following:

(3A) Notwithstanding Section 10, for the purposes of subsection (3):

a) *An individual shall be connected with another individual if that person is the individual's husband, wife or civil partner, or is a relative, or lineal descendant of that person.*

b) *Where the shares or ownership rights of an entity are held through a partnership, the percentage of voting rights, share ownership rights or similar ownership rights that a partner in that partnership is treated as holding in that entity shall be the same as their equivalent rights in the partnership.*

c) *Two or more entities or individuals shall not be treated as acting together with respect to voting rights, share ownership rights or similar ownership rights solely because they are partners in a partnership.*

If the above general carve-out for partnerships cannot be adopted, we recommend that the existing provisions of the proposed subsection 3A be revised to take account of the specific observations made above. This might include:

(3A) (a) For the purposes of subsection 3(f), an individual (in this paragraph referred to as 'the first-mentioned individual') shall not be treated as connected with another individual with whom such person is in partnership where –

(i) the first-mentioned individual's interest in profits, if any, of the partnership or partnerships is not more than 50 per cent, and

[…]

Commencement

We believe that the proposed amendment to the definition of an associated entity in section 817U(3)(f) TCA 1997 should apply on a prospective basis (i.e., to arrangements entered into on or after the date on which the amendment is passed). We suggest the following amendment is considered:

This subsection shall apply in respect of arrangements entered into on or after [date amendment is passed] in respect of which there is a payment of interest or royalties, or the making of a distribution.

Conclusion

We would welcome confirmation from policymakers of an indicative timeline for the enactment of the proposed draft amendments to the outbound payments defensive measures. Please contact Anne Gunnell at agunnell@taxinstitute.ie or (01) 6631750 for any further information in relation to this submission.

[i] Extract from Twomey on Partnership 19.04: "*While taxation legislation refers to a partnership share in this manner for convenience, in truth, a partner cannot be said to be entitled to any particular item of partnership property. Instead, each partner has a beneficial interest in the entirety of the partnership property and in this sense a partnership share is a bundle of the different property rights included within the assets of the firm, such as real property, personal property, choses in action, etc. However, a partner does not have a right to any particular partnership asset, to the exclusion of the other partners. 12 This is reflected in the fact that during the life of the partnership, each partner is entitled to require the partnership assets to be applied for partnership purposes and not for the exclusive use of one partner. 13 Similarly, when the partnership comes to an end, the partnership assets must be used to pay off the firm's debts and liabilities, with the surplus being shared between the partners. 14 Thus, in addition to his being entitled to the entirety of the partnership property, a partner's share can be described, as it was by Joy CB in Stuart v Ferguson, 15 as follows: 'the share of each partner is only the share of the clear surplus which would remain after the payment of all the debts.*'