Tax Treatment of Specified Financial Transactions

Part 08A-01-01

This document should be read in conjunction with Part 8A Taxes Consolidation Act 1997

Document updated August 2026

Revenue
Cáin agus Custaim na hÉireann
Irish Tax and Customs

The information in this document is provided as a guide only and is not professional advice, including legal advice. It should not be assumed that the guidance is comprehensive or that it provides a definitive answer in every case.

Table of Contents

1 Introduction 4
2 Islamic Finance 4
2.1 Overview of the tax treatment of Islamic financial transactions 4
2.2 Concepts and Structures 5
2.2.1 Ijarah 5
2.2.2 Murabaha 5
2.2.3 Mudaraba 5
2.2.4 Wakala 5
2.2.5 Diminishing Musharaka 5
2.2.6 Sukuk 5
2.2.7 Takaful / Re-Takaful 5
3 Islamic Investment Funds 6
3.1 General 6
3.2 Tax Issues 6
3.2.1 Income Tax/Corporation Tax 6
3.2.2 Value Added Tax (VAT) 6
3.2.3 Stamp Duty 6
3.2.4 Taxation of service providers 7
4 Leasing and Hire Purchase (Ijarah) Arrangements 8
4.1 General 8
4.2 Ijarah Structures 8
4.2.1 Ijarah used for an operating lease 8
4.2.2 Ijarah used for a finance lease 8
4.2.3 Ijarah used for a hire purchase arrangement 8
4.3 Taxation of an Ijarah arrangement 9
4.3.1 Income Tax / Corporation Tax 9
4.3.2 Value Added Tax (VAT) 10
4.3.3 Stamp Duty 10
5 Insurance (Takaful) and Reinsurance (Re-Takaful) Transactions 11
5.1 Overview 11
5.2 Features of a General Takaful Arrangement 12
5.3 Features of Family (Life) Takaful Arrangement 13
5.4 Features of a Re-Takaful (Reinsurance) Arrangement 13
5.5 Taxation of Takaful and Re-Takaful Arrangements 13
5.5.1 Corporation Tax 13
5.5.2 Value Added Tax (VAT) 14
5.5.3 Stamp Duty 14
6 Overview of Specified Financial Transactions 15

6.1 Application of Part 8A 15
6.2 Parties to the transaction 15
6.2.1 Credit and Deposit Transactions 15
6.2.2 Investment Transactions 16
6.3 Terms of the Transaction 16
6.4 Election 16
7 Credit Transactions (Murabaha and Diminishing Musharaka) 17
7.1 Definition of Credit Transaction 17
7.2 Definition of credit return 18
7.3 Tax treatment of Credit Transactions 19
7.3.1 Application of Section 130 Taxes Consolidation Act 1997 19
7.3.2 Treatment of VAT and other charges included in consideration paid for an asset 20
7.3.3 Capital Allowances 20
7.3.4 Capital Gains Tax 20
7.3.5 Losses 21
7.3.6 Benefit in Kind 21
7.3.7 Borrowing to invest in other companies 21
7.3.8 Stamp Duty 21
8 Deposit (Mudaraba and Wakala) Transactions 22
8.1 Definition of Deposit Transactions 22
8.2 Tax Treatment of Deposit Return 22
8.2.1 Application of Section 130 Taxes Consolidation Act 1997 22
8.2.2 Deposit Interest Retention Tax 23
8.2.3 Tax treatment of Finance Undertaking 23
8.2.4 Tax Treatment of Depositor 23
9 Investment (Sukuk) Transactions 24
9.1 Definition of Investment Certificate 24
9.2 Definition of Investment Return 25
9.3 Taxation of the Investment Return 25
9.4 Application of Section 110 of the Taxes Consolidation Act 1997 26
9.5 Tax Treatment of the Certificate Owner 26
9.6 Tax Treatment of the Certificate Issuer 27
9.7 Stamp Duty Treatment of the Investment Certificate 27
10 Miscellaneous 28
10.1 Interest reporting 28
10.2 Transactions with non-resident persons 28
Appendix I – Schedule of key updates 29

1 Introduction

Specified financial transactions are credit transactions, deposit transactions and investment transactions. These can include financing arrangements that are compliant with the principles of Shari'a law as outlined in section 2. Such arrangements may or may not be treated in the same way as mainstream financial transactions which are similar in substance.

Specified financial transactions are based on Islamic financing however, a financing arrangement is not required to adhere to any faith-based principles to be considered a specified financial transaction.

The taxation treatment of specified financial transactions is set out in Part 8A of the Taxes Consolidation Act 1997 and guidance on the provisions is outlined in sections 6 to 9 of this manual.

2 Islamic Finance

The term Islamic finance refers to financial transactions that are consistent with the principles of Islamic law (Shari'a). One of the main principles of Islamic finance is that the payment and receipt of interest (riba) are forbidden. Other key principles include the following: the prohibition of activities based on speculation (maisir) or excessive uncertainty (gharar) and the prohibition on investment in businesses, products or services considered to be unethical. Islamic financial transactions are typically backed by or based on an identifiable and tangible underlying asset, and involve risk sharing between the investor and the investee.

To facilitate commercial transactions, Islamic financial structures have been devised that comply with the basic principles of Shari'a law. These products meet the same economic needs as conventional financial products by using familiar legal structures in an alternative way (insofar as debt is concerned) to achieve the financing objectives.

2.1 Overview of the tax treatment of Islamic financial transactions

The term Islamic Finance does not appear in tax legislation. In the case of Shari'a compliant transactions and structures within the funds, leasing and insurance industries, generally the Irish tax treatment is the same as that applying to conventional transactions. The tax treatment of these transactions is outlined in sections 3 to 5.

Although designed to cover certain Shari'a compliant structures, the legislation applies to any financing arrangement falling within the meaning of the term "specified financial transaction" regardless of whether the arrangement is, in fact, Shari'a compliant.

The return arising on a specified financial transaction is treated as interest for tax purposes and all relevant tax legislation pertaining to interest applies to that return. The legislation does not change the nature of the financial arrangements. It seeks to provide a level playing field for tax between certain types of economically equivalent, but differently structured, finance arrangements.

2.2 Concepts and Structures

The following structures are common in Islamic finance:

2.2.1 Ijarah

An Ijarah arrangement is similar to a lease. An Ijarah arrangement which is similar to a hire purchase arrangement is commonly referred to as Ijarah Muntahia Bittamleek. Its features are broadly similar to a normal Ijarah arrangement (an operating lease) but the lease concludes with the legal title in the leased asset passing to the lessee.

2.2.2 Murabaha

A Murabaha arrangement is a form of cost-plus financing on deferred payment terms. This arrangement is used for the purchase and sale of assets and enables a business to acquire a fixed asset or raise capital. A finance provider buys an asset and re-sells it to a customer at a pre-agreed higher price, payable at a later date.

2.2.3 Mudaraba

A Mudaraba arrangement is a form of partnership, where profits are shared and losses are borne exclusively by the capital provider.

2.2.4 Wakala

A Wakala is a type of agency arrangement and involves a representative undertaking an investment transaction on behalf of a principal.

2.2.5 Diminishing Musharaka

This is a type of partnership where one partner gradually buys out the other. It is most commonly used in property transactions.

2.2.6 Sukuk

A Sukuk is equivalent to a bond.

2.2.7 Takaful / Re-Takaful

Takaful/Re-Takaful transactions are similar to conventional insurance and reinsurance transactions.

3 Islamic Investment Funds

3.1 General

The primary characteristic that distinguishes Islamic fund management from conventional investing is its compliance with Shari'a law. A Shari'a fund is required to appoint a Shari'a Board which provides guidance to the directors of the fund and to the investment manager on matters of Shari'a law and in particular whether the proposed investments of the fund are Shari'a compliant. The Shari'a Board should not be confused with the Board of Directors of a company, as a Shari'a Board only has an advisory role. In the context of a Shari'a compliant company, the Shari'a Board can be considered as a sub-committee of the Board of Directors of the company.

The arrangement between a fund and its service providers can either be based on a service fee or a share in the profits of the fund or a combination of both. If the fund sustains a loss, the loss is borne by the investors.

3.2 Tax Issues

3.2.1 Income Tax/Corporation Tax

The taxation of funds is governed by Part 27 of the Taxes Consolidation Act (TCA) 1997. Chapter 1A of that Part applies the gross-roll-up taxation regime to all funds set up after 31 March 2000. The regime does not impose an annual tax on the profits of the fund but requires the fund/fund manager to deduct and account for tax out of payments made to unit holders – except for certain classes of unit holder who can, by use of a declaration procedure, be paid gross. Provided the fund is constituted in accordance with Chapter 1A, these arrangements apply irrespective of whether the fund is a Shari'a compliant fund or a conventional fund.

3.2.2 Value Added Tax (VAT)

Paragraph 6(2) of Schedule 1 to the VAT Consolidation Act 2010 provides for the management of certain funds to be exempt from VAT**.** Where the management of the Shari'a fund qualifies for the exemption provided for in that paragraph and it can be demonstrated that the services rendered by the members of the Shari'a Board are an integral part of that overall management service, then the services supplied by the Shari'a Board to the fund will also be exempt from VAT.

3.2.3 Stamp Duty

A liability to stamp duty does not arise on the issuance or redemption of units/shares in a fund. In addition, the transfer of units/shares in a fund is not chargeable to stamp duty to the extent that the fund is an investment undertaking within the meaning of section 739B of the TCA 1997 or a common contractual fund within the meaning of section 739I of the TCA 1997.

3.2.4 Taxation of service providers

Income received by a service provider which is linked to the profits or performance of a fund should be treated as fee income where it relates to duties performed by the service provider.

4 Leasing and Hire Purchase (Ijarah) Arrangements

4.1 General

In principle, an Ijarah contract is similar to a conventional leasing arrangement. A normal Ijarah arrangement would generally refer to an operating lease. However, Ijarah arrangements can also be used to structure finance leases or hire purchase transactions.

4.2 Ijarah Structures

4.2.1 Ijarah used for an operating lease

The key features of an Ijarah arrangement that is similar to an operating lease are set out below:

- Under an Ijarah contract, a person (lessor) leases an asset to another person (lessee) for periodic rental payments (lease rentals). The lessor can be the owner of the asset or an intermediary lessor.
- During the lease period, the asset remains the property of the owner who would normally bear the burden of wear and tear.
- If the asset is to be insured, the lessor or the lessee may insure it but it must be at the lessor's expense. Such cost may however be implicitly factored into the calculation of the lease rental.
- The lease rentals are specified in the lease agreement and these can be fixed or variable amounts.
- Where a lease rental becomes overdue, the lessor does not charge any interest. However, the contract may require the lessee to make an additional payment towards a charitable cause.
- On the expiry of the lease term, the asset is handed back to the lessor.

4.2.2 Ijarah used for a finance lease

An Ijarah arrangement can also be used to structure a finance lease where the value of the asset is broadly recovered during the primary lease period and a nominal or token lease rental is charged during the secondary lease period.

4.2.3 Ijarah used for a hire purchase arrangement

An Ijarah arrangement which is similar to a hire purchase is commonly referred to as Ijarah Muntahia Bittamleek. Its features are broadly similar to a normal Ijarah arrangement (an operating lease) and is typically structured in one of two ways, which are set out below.

The key features of the first arrangement are:

- The parties enter into a normal Ijarah arrangement (an operating lease). Under a separate arrangement, the lessor promises to transfer the title to the asset to the lessee for a consideration or at a token value or by way of a gift. The transfer is subject to instructions from the lessee and may be contingent upon a particular event, such as payment of the remaining lease instalments. The promise to transfer the ownership is binding on the lessor only and the lessee has an option not to proceed with the transfer.
- The arrangement relating to the transfer of title is set out in a document separate to the lease contract.

The key features of the alternative arrangement are:

- Similar to the first arrangement, the parties enter into a normal Ijarah arrangement (an operating lease). Additionally, the lessee promises to acquire the lessor's interest in the asset over the lease term for an agreed price.
- Normally, the lessor's interest in the asset is divided into a number of units and the periodic lease rental payments are split between (a) the lease rental payment and (b) the payment for acquiring the interest (units) in the asset. The lessee's interest in the asset therefore typically increases over time.
- Normally, the legal title in the asset remains with the lessor until the final lease rental is paid.

4.3 Taxation of an Ijarah arrangement

4.3.1 Income Tax / Corporation Tax

4.3.1.1 Ijarah used for an operating lease

The provisions of the Taxes Consolidation Act 1997 (TCA) apply to an Ijarah arrangement which is used for an operating lease as if the arrangement were a conventional operating lease arrangement. In such case, where the lessor bears the burden of wear and tear on the asset, the lessor is taxable on the gross lease rental received. Where the asset is plant and machinery, the lessor is also entitled to claim the capital allowances due in accordance with Part 9 of the TCA. Where the lessee is carrying on a trade and the asset is used for the purpose of the trade, the lessee can claim an expense deduction for the gross lease rental.

Alternatively, where the asset is a “specified asset” within the meaning of section 80A of the TCA and the lease does not exceed 8 years, a corporate lessor may claim to have the profits from the leased asset taxed in accordance with the provisions of section 80A as that section applies to operating leases.

4.3.1.2 Ijarah used for a finance lease

Similarly, the provisions of the Taxes Consolidation Act 1997 (TCA) apply to an Ijarah arrangement used for a finance lease as if it were a conventional finance lease. Accordingly, a corporate lessor that accounts for the transaction as a finance lease under generally accepted accounting practice, may be taxed in accordance with the provisions of section

76D of the TCA or, where he makes a claim in that regard, and the lease is a "relevant short-term lease", in accordance with the provisions of section 80A of that Act.

Where the lessee bears the burden of wear and tear on the leased asset, the provisions of section 299 will apply to claims for capital allowances by the lessee.

4.3.1.3 Ijarah Muntahia Bittamleek (Hire Purchase arrangements)

Again, the Taxes Consolidation Act 1997 (TCA) applies to an Ijarah Muntahia Bittamleek arrangement which is used for a hire purchase transaction as if it were a conventional hire purchase arrangement. A hire purchase arrangement would also fall within the definition of credit transactions in section 267N of the TCA so a finance undertaking entering into an Ijarah Muntahia Bittamleek arrangement may elect to have the provisions of that section applied to the arrangements (see section 7).

Where any of the lease contracts referred to above requires the lessee to make an additional payment towards a charitable cause in the event of a lease rental becoming overdue, the transaction will be treated as if the lessee had made the payment directly to the lessor and the lessor made the payment towards the charitable cause (which is in fact the normal sequence of payments). The lessee will be entitled to a deduction and the lessor will be treated as having received the income but will be entitled to a deduction under section 848A of the TCA, subject to the provisions of that section.

It should be noted that the tax treatment described above is limited to Ijarah that refers to the leasing of plant and machinery and other chattels. It does not apply to a lease of immovable property. Queries on the tax treatment of such leases should be emailed to rlsfinancialservices@revenue.ie.

4.3.2 Value Added Tax (VAT)

The VAT treatment of an Ijarah (Finance Lease and Hire Purchase) arrangement in relation to immovable property transactions will depend on the specifics of the agreements. Generally, such agreements are likely to be regarded as the supply of a freehold equivalent interest by the lessor to the lessee at the time the agreement is entered into.

As regards arrangements which cover goods other than immovable property, the normal VAT rules concerning leasing (a supply of services), transfer of title (supply of goods) or hire purchase (a supply of goods), as appropriate, would apply.

Previous guidance given by Revenue in relation to the taxation of conventional operating and finance leases and to hire purchase arrangements will, in substantially similar circumstances, also apply to the equivalent Ijarah transactions.

4.3.3 Stamp Duty

A charge to stamp duty will not arise in relation to Ijarah (Leasing and Hire Purchase) arrangements where the asset involved does not comprise immovable property or an interest in immovable property.

In contrast, a lease involving immovable property or an interest in immovable property will be subject to stamp duty under normal rules.

5 Insurance (Takaful) and Reinsurance (Re-Takaful) Transactions

Takaful or Re-Takaful arrangements are broadly equivalent to conventional insurance and reinsurance arrangements respectively.

5.1 Overview

Takaful is an arrangement amongst a group of persons participating in a scheme under which the Takaful members (policyholders) jointly indemnify each other against any loss or damage that may arise to any of them. To this effect, Takaful members pool funds by way of contributions. The resulting fund is used to make compensation (claim) payments for any loss or damage arising to any Takaful member. The claim payments are generally restricted to actual damage or loss and the opportunity costs (such as loss of potential income) are generally ignored. The entire arrangement relating to the receipt of contributions, claim payments and the management and operation of a Takaful fund is managed by a Takaful company.

Broadly speaking, a Takaful arrangement is similar to a mutual insurance arrangement with the difference that Takaful members are typically not shareholders/unit-holders in the Takaful company which operates the arrangement for the Takaful members. The operator company is paid a fee for the services rendered and/or is entitled to a share in the return received on the fund's investments. The term General Takaful is normally used as a reference to a general insurance arrangement while the term Family Takaful would normally refer to a life assurance arrangement.

A Takaful arrangement can be illustrated as follows:

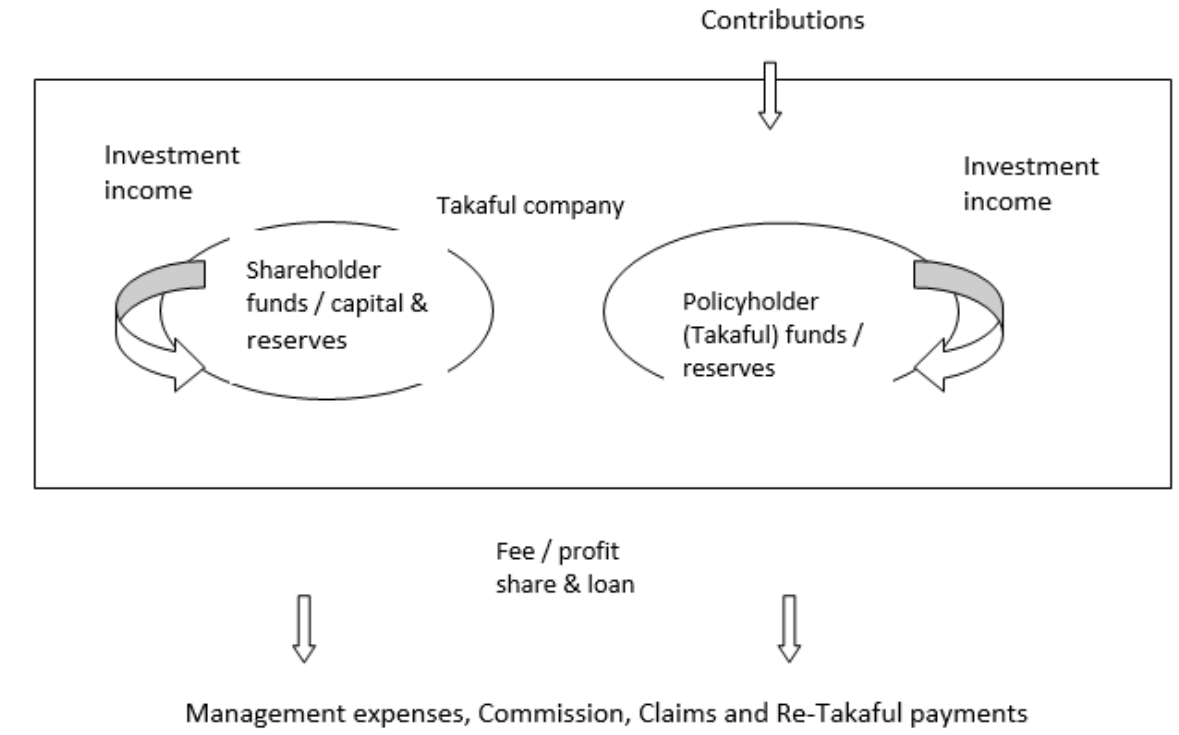

Figure 1 Takaful arrangement

A Re-Takaful (reinsurance) arrangement also works in a similar way where the Takaful companies take the role of the Takaful members and the Re-Takaful company takes the role of the operator of the scheme.

5.2 Features of a General Takaful Arrangement

The following are the key characteristics of a General Takaful arrangement.

- A company sets up a Takaful fund with contributions from the Takaful members (policyholders). The company records Takaful funds separately from its own share capital and reserves.
- The policyholders agree to compensate each other for any loss. This is normally set out in the insurance policy or other related documentation.
- The Takaful fund is used to make payments for any loss arising to a Takaful member (claim) and for any payments to a Re-Takaful operator (reinsurance payments). The surplus funds are invested by the company. The return on investments creates a reserve in the Takaful fund.
- The company would normally charge a fee for its services relating to the management and the operation of the Takaful fund. The fee may be fixed or a share in the returns on Takaful investments. It is also possible that the company is paid a fixed fee and is also entitled to a share in the return received on Takaful investments. The arrangement is normally set out in the insurance policy or other related documentation.
- Normally marketing and management expenses and commission payments are paid by the company out of its own funds.
- A loss relating to Takaful funds is normally charged to the Takaful fund and ring-fenced from the company's reserves. Likewise, a loss relating to the company's investments/activities is normally borne by the company and ring- fenced from Takaful funds.
- In case there is a shortfall in the Takaful fund, the company would normally make an interest-free loan to the fund. Generally, the loan is repayable only out of a future surplus arising in the Takaful fund.
- If there is a surplus in the Takaful fund, the surplus is used for repayment of any interest free loan owed to the company. Any remaining surplus can either be reserved for future losses or the company may decide to make a distribution to the policyholders. The distribution amount may be adjusted against the contribution payment relating to the following year.
- On dissolution or winding up of a Takaful fund, any surplus in the fund may be distributed amongst those who contributed to the Takaful fund or amongst those who are members (policyholders) of the fund on the day of dissolution or winding up. The surplus or any part thereof may also be given to charity. The Takaful funds cannot be diverted to the company.

5.3 Features of Family (Life) Takaful Arrangement

A Family (Life) Takaful arrangement works in a broadly similar way to a General Takaful arrangement. It is similar to a conventional life assurance or a savings scheme wrapped in a life policy. The following are the key differences:

- The amounts received from the Takaful members (policyholders) are split between (a) a Contribution Account; and (b) an Investment Account. The split is agreed with the policyholder at the time of issuance of the policy and is generally based on the actuarial valuation of the associated risks. The Contribution Account is generally reserved for life assurance claims. If the Takaful member survives the policy term, the member is only entitled to receive the amount paid into the Investment account and any accumulated profits attributable to such amount.
- The profit made on Takaful investments is apportioned amongst the policyholders (Takaful members) or retained as a reserve for the future. The arrangement is normally set out in the insurance policy or other related documentation, as is the case with conventional life assurance.

5.4 Features of a Re-Takaful (Reinsurance) Arrangement

A Re-Takaful (Reinsurance) arrangement broadly works in a similar way to a conventional reinsurance arrangement. Various Takaful companies participate in a Re-Takaful fund set up by a Re-Takaful company. The Re-Takaful company acts as the operator of the Re-Takaful arrangement. The distinction between the company's capital and reserves and Re-Takaful funds is maintained and both are ring-fenced from each other. The Re-Takaful company may be paid a service fee and/or a share in the profit made on investments made out of Re-Takaful funds. Where there is a shortfall in Re-Takaful funds, the Re-Takaful company would normally make an interest free loan to the Re-Takaful fund which is generally repayable only out of a future surplus arising in the fund.

5.5 Taxation of Takaful and Re-Takaful Arrangements

5.5.1 Corporation Tax

In relation to General Takaful and Re-Takaful arrangements:

- Contributions received by a Takaful company from policyholders (Takaful members) are to be treated as taxable income. Similarly, contributions received by a Re-Takaful company from Takaful companies, as members of the Re- Takaful arrangement, are to be treated as taxable income. Whether the income is on trading account will depend on the facts and circumstances of the case.
- The deductibility of expenses incurred by a Takaful company or a Re-Takaful company for management, marketing, claims and commissions and any provisions in respect thereof should be treated in the same way as such expenses where incurred by a conventional insurance or a reinsurance company with the same level of activity.

- The deductibility of a contribution payment paid to a Takaful or a Re-Takaful company is to be treated in the same way as an insurance or reinsurance premium for a conventional insurance policy or a reinsurance arrangement.

The provisions of sections 76 to 83 of the Taxes Consolidation Act 1997 (TCA) apply in respect of the taxation of a Takaful or a Re-Takaful arrangement as if such arrangements were conventional insurance or reinsurance arrangements respectively. In addition, the taxation of a Family (Life) Takaful company, which is an assurance company within the meaning of section 730A of the Taxes Consolidation Act 1997, and its members (policyholders) is to be determined under Chapters 4 and 5 of Part 26 of that Act. In this regard, an amount paid by an insured person is to be treated in the same way as a payment under a conventional life assurance policy is treated. Similarly, a maturity or claim amount paid by a Family (Life) Takaful company is to be treated in the same way as a claim or maturity payment under a conventional life assurance policy is treated.

As there are no existing Family (Life) Takaful arrangements in Ireland, the provisions relating to the taxation of old basis business should not apply to the Family (Life) Takaful arrangements.

5.5.2 Value Added Tax (VAT)

For the purposes of the VAT Consolidation Act 2010, Takaful (General and Family (Life)) and Re-Takaful arrangements are to be treated in the same way as conventional non-life and life insurance and reinsurance arrangements, i.e. the services rendered will be exempt from VAT under paragraph 8 of the Schedule 1 to the VAT Act to the extent provided in that paragraph.

5.5.3 Stamp Duty

A liability to stamp duty under the Stamp Duties Consolidation Act (SDCA) 1999 will arise in relation to policies of insurance or policies of life insurance issued under Takaful (General and Family (Life)) and Re-Takaful arrangements where the risk is located within the State (section 61 of the SDCA).

6 Overview of Specified Financial Transactions

Section 39 of the Finance Act 2010 inserted Part 8A into the Taxes Consolidation Act 1997 (TCA) to set out the tax treatment to be applied to "Specified Financial Transactions". Specified Financial Transactions comprise credit transactions which are equivalent to credit sales or loans, deposit transactions and investment transactions and are defined as near as possible to equate to their Shari'a compliant counterparts (see paragraph 2.2). Essentially, where the legislation applies, the return (or profit) on any product defined as a "specified financial transaction" is treated as interest for all the purposes of the Taxes Acts.

6.1 Application of Part 8A

The legislation is very specific as regards the terms of the transactions and sets out various rules or conditions to be complied with before the provisions will apply. The rules also govern who can be parties to the transaction, the treatment of VAT and other charges included in the amount payable for an asset and provide for an election procedure.

6.2 Parties to the transaction

6.2.1 Credit and Deposit Transactions

A finance undertaking must act as the lender or deposit holder in the case of a credit or deposit transaction. The term "finance undertaking" is defined as meaning a finance company or a financial institution. These in turn are defined as:

Financial Institution

This has the same meaning as in Section 891B of the TCA i.e.:

(a) a person who holds or has held a licence under section 9 or an authorisation granted under section 9A of the Central Bank Act 1971, or a person who holds or has held a licence or other similar authorisation under the law of an EEA state, other than the State, which corresponds to a licence granted under the said section 9,

(aa) an agent appointed by the National Treasury Management Agency to carry out certain functions of the National Treasury Management Agency in relation to State savings products, or

(b) a person referred to in section 7(4) of the Central Bank Act 1971;

Finance Company

This is defined as a company whose income consists of income from:

- the leasing of plant and machinery,
- the carrying on of specified financial transactions, or
- a combination of both.

6.2.2 Investment Transactions

In order for an investment transaction to qualify for the treatment set out in Part 8A, the investment certificates must have been issued by a "qualifying company". This is defined in section 267N as a company that:

(a) is resident in the State,

(b) issues investment certificates to investors, and

(c) redeems the certificates after a specified period of time.

Although not defined in legislation, Revenue will accept that the words "specified period of time" mean the term or length of the transaction.

6.3 Terms of the Transaction

In order to qualify as a "specified financial transaction", section 267N requires that it must have been undertaken on terms that would reasonably have been expected to apply if the parties to the transaction were independent parties acting at arm's length (section 267N).

Section 267V also provides that the legislation will only apply to a transaction that has been undertaken for bona fide commercial reasons and does not form part of any arrangement for the avoidance of a tax liability. All taxes are covered by this provision including Stamp Duty, VAT and Capital Acquisitions Tax.

6.4 Election

Section 267U requires the finance undertaking or qualifying company to elect to have the legislation applied. This election must be made on the appropriate form (SFT 1 or SFT 2) and may be made either in respect of an individual transaction or a series of transactions of a similar nature.

The information to be supplied on the form includes:

- name, address and tax reference number of each party to the transaction in the case of a single transaction,
- a description of the transaction,
- the value of the transaction.

Where an election is made, the finance undertaking must notify the other party to the transaction and thereafter, the tax treatment outlined in the new Part 8A of the TCA will apply to that transaction or series of transaction.

Where an election is not made, the tax treatment to be applied to the transaction will depend on the legal form of the arrangements.

7 Credit Transactions (Murabaha and Diminishing Musharaka)

The term 'Credit transactions' cover credit sales, loans or mortgages which are equivalent to the Islamic financial transactions known as 'Murabaha' (which corresponds to a credit sale or loan of money) and 'Diminishing Musharaka' (which corresponds to a mortgage or other asset finance arrangement).

Essentially such a transaction involves the purchase of an asset by a finance undertaking which then sells on that asset to a customer on a deferred payment basis at a marked-up price. The customer either:

(1) retains the asset (this corresponds to a credit sale and is dealt with in paragraph (a) of the definition of credit transaction), or

(2) raises funds by selling the asset immediately for cash (this corresponds to a conventional loan and is dealt with in paragraph (b) of the definition of credit transaction).

In a mortgage type/ hire purchase equivalent transaction (dealt with in paragraph (c) of the definition of credit transaction) an asset is acquired jointly by a finance undertaking and a customer on terms on which the customer promises to acquire the finance undertaking's share in the asset over an agreed period of time. The asset is generally rented to the customer for an amount equal to the economic return on investment and which is equivalent to the interest payable in a conventional transaction.

7.1 Definition of Credit Transaction

"Credit Transactions" are defined in Section 267N.

Paragraph (a) of the definition describes a credit sale arrangement whereby a finance undertaking acquires an asset for the purpose of entering into a credit transaction and disposes of the full interest in that asset to a person (referred to as the borrower) where:

(i) the consideration paid or payable by the borrower exceeds the amount paid or payable by the finance undertaking for the asset,

(ii) all or part of the consideration due from the borrower is not required to be paid until a date later than the date of the disposal, and

(iii) the excess of the amounts paid or payable by the borrower over the consideration paid or payable by the finance undertaking for the asset equates in substance to the return on a loan of money at interest.

Paragraph (b) covers loans or other transactions whereby a finance undertaking acquires an asset and

(i) immediately disposes of that asset to the borrower at a marked-up price,

(ii) the borrower immediately disposes of the asset for a price which is at least 95 per cent of the price paid or payable by the finance undertaking for the acquisition of the asset (this generates cash for the borrower),

(iii) all or part of the consideration for the acquisition of the asset by the borrower is not required to be paid by the borrower until a date later than the date of the purchase of the asset, and

(iv) the excess of the amount paid or payable to the finance undertaking by the borrower in respect of the asset equates in substance to the return on a loan of money at interest.

Paragraph (c) covers mortgage or hire purchase transactions under which

(i) a finance undertaking and another person jointly acquire an asset (i.e. this would apply to new purchases), or

(ii) a finance undertaking acquires an asset from the borrower in circumstances where the borrower retains an interest in the asset (i.e. a refinancing transaction) where:

(I) the borrower:

(A) has exclusive use of the asset immediately (in the case of a new purchase) or retains exclusive use immediately (in a case where s/he already owned the asset),

(B) is exclusively entitled to any income, profit or gain from the asset (including increases in its value), and

(C) agrees to make payments to the finance undertaking amounting to the sum of the amount paid or payable by that undertaking for the asset and any other consideration paid by the borrower for the use of the asset,

(II) the excess of the amount paid or payable (including rent or other amounts payable for the use of the asset) by the borrower to the finance undertaking over the amount paid by the finance undertaking for the asset equates in substance to the return on a loan of money at interest, and

(III) the finance undertaking's interest in the asset passes either immediately or by the end of a specified period to the borrower for a consideration which exceeds the consideration paid by the finance undertaking for the asset.

Although not defined in legislation, Revenue will accept that the words "specified period of time" mean the term or length of the transaction.

7.2 Definition of credit return

This is also defined in section 267N.

Paragraph (a) of the definition deals with the credit sales or loans falling within paragraphs (a) and (b) respectively of the definition of credit transaction and defines the credit return in such transactions as the excess of the amount paid or payable by the borrower over the amount paid by the finance undertaking for the asset.

Paragraph (b) deals with the credit return in a Diminishing Musharaka transaction (paragraph (c) of the definition of credit transactions) and states that in such cases, the credit return is the excess of the consideration paid or payable to the finance undertaking by the borrower (including any consideration paid or payable for the use of the asset) over the amount paid by the finance undertaking for the asset.

7.3 Tax treatment of Credit Transactions

The credit return is treated as interest for the purpose of the Tax Acts. This means that all of the provisions in the Tax Acts that apply to interest (including deeming the interest to be a distribution in accordance with the provisions of section 130 of the TCA) apply to a credit return. As credit transactions generally involve the purchase of an asset, questions can arise as to:

- the amount payable for the asset,
- which party to the transaction would be entitled to the capital allowances due on that asset,
- how the return or interest on the transaction is treated in the hands of the borrower and the lender.

Sections 267N, 267O and 267P sets out the rules for dealing with these issues.

7.3.1 Application of Section 130 Taxes Consolidation Act 1997

Section 130 provides that an interest payment can be deemed to be a distribution in certain circumstances. One of the circumstances outlined in the section (subsection (2)(d)(iii)), is where the interest payment is to any extent dependant on the results of the payer's business. Certain Shari'a compliant credit transactions may be structured so that the amount repayable to the finance undertaking may be linked to a certain extent to the results of the borrower and so conflicts with section 130. In such cases, the borrower would not be entitled to a deduction for the amount paid to the finance undertaking.

In general, Revenue will not regard the return as being dependent on the results of the borrower and consequently section 130 will not apply, where all of the following conditions are satisfied:

- where the amount of the credit return equates in substance to a commercial return on a loan of money,
- the expected return on the credit transaction is determined at the time of entering into the agreement and forms part of the agreement,
- the rate of expected return is comparable with the rate of interest charged on a conventional loan, and
- the expected return amount is not altered during the course of the transaction.

Where these conditions are not satisfied, the provisions of section 130 will apply so as to re-categorise the full amount of the return as a distribution.

7.3.2 Treatment of VAT and other charges included in consideration paid for an asset

Section 267N provides that references to the consideration paid or payable in respect of an asset are not to include any amount in respect of which a borrower or finance undertaking may claim a deduction or a refund of VAT.

The section also provides that any amount chargeable by a finance undertaking in respect of fees, charges or similar payments are not to be regarded as part of the consideration paid for the asset for the purposes of Part 8A and are thus not taken into account in the calculation of a credit return. Such fees, charges or similar payments will be taxable or deductible under normal taxation rules. For instance, where a financial institution has charged an arrangement or other fee in respect of a mortgage and included that amount in the price charged for the asset, the amount on which mortgage interest relief would be due would not include that fee. However, the financial institution would be taxable under general Corporation Tax rules in respect of that fee income.

7.3.3 Capital Allowances

Section 267P provides that a finance undertaking will not be entitled to capital allowances on any asset acquired for the purpose of a credit sale transaction.

A borrower is not entitled to a deduction for any capital repayment made to the finance undertaking. However, where the borrower carries on a trade and the asset is used for the purposes of the trade, the borrower will be entitled to claim the capital allowances due on the asset where he otherwise complies with the conditions set out in Part 9 of the TCA.

In the case of a new asset acquired under a Diminishing Musharaka type transaction (paragraph (c) of the definition of credit transaction), the borrower is deemed to have acquired the full interest in that asset at the outset of the transaction. As a result, the acquisition by the borrower of the interest in the asset when the final instalments are paid will not qualify for capital allowances.

In a refinancing situation, a borrower disposes of part of his interest in the asset to the finance undertaking. Section 267P provides that this disposal will not give rise to a balancing allowance or charge.

The amount of the credit return is not to be regarded as expenditure on an asset for the purpose of calculating a capital allowance, balancing allowance or charge due on that asset.

7.3.4 Capital Gains Tax

A charge to Capital Gains Tax could arise where a finance undertaking disposes of an asset acquired for the purpose of entering into a credit sale transaction. In order to prevent this, section 267P provides that the acquisition/disposal of an asset in these circumstances will be regarded as made in the course of the trade where the finance undertaking is carrying on a trade that consists of or includes specified financial transactions.

In the case of the borrower, the amount of the credit return is not to be regarded as expenditure on an asset for the purpose of section 552. This ensures that the amount of

the credit return will not be included in the purchase price of an asset for the purpose of computing a capital gain on a subsequent disposal of the asset.

7.3.5 Losses

In the case of credit transactions undertaken in order to raise cash for the borrower, the asset acquired from the finance undertaking is normally sold for a price which is less than the price paid to the finance undertaking. In order to prevent claims for loss relief where in fact there is no loss (the difference in price is effectively the return or profit of the finance undertaking), section 267P provides that the borrower is not regarded as having incurred a loss on the disposal of the asset acquired from the finance undertaken.

7.3.6 Benefit in Kind

A credit transaction is treated as a loan for the purposes of section 122. This brings the transaction within the Benefit in Kind provisions. This means that a charge to tax will arise in any case where the borrower in a credit transaction is an employee of the finance undertaking and the return on the transaction is either nil or at a rate lower than normal commercial rates.

7.3.7 Borrowing to invest in other companies

Section 267P also provides that a credit transaction is to be treated as a loan for the purposes of Part 8. Essentially this means that a borrower who enters into a credit transaction in order to raise funds to invest in or lend to another company is entitled to claim relief under section 247 in respect of the amount of the credit return paid to the finance undertaking provided the other conditions of that section are complied with.

7.3.8 Stamp Duty

The legislative provisions introduced under the Finance Act 2010 for Specified Financial Transactions do not extend the stamp duty treatment of “credit transactions” as defined in section 267N. Accordingly, stamp duty will arise under normal rules on the documentation executed in connection with such transactions.

8 Deposit (Mudaraba and Wakala) Transactions

Section 267Q deals with the tax treatment of 'deposit transactions'. It is designed to cover Shari'a compliant banking deposit arrangements structured as "Mudaraba" and "Wakala" contracts. In order to obviate the need to pay interest, the transactions are structured as quasi partnership arrangements whereby an investor provides money to a financial institution in return for a share in the profits (or losses) generated by the institution from the use of the money.

Section 267Q treats this profit share return (i.e. the deposit return) as if it were interest payable on a conventional bank deposit.

8.1 Definition of Deposit Transactions

The definition in section 267N sets out two conditions which must be fulfilled in order for a transaction to be treated as a deposit transaction. These are:

- a person must deposit a sum of money with a relevant deposit taker (as defined for DIRT purposes) on terms on which it or any part of it may be repaid either on demand or in circumstances agreed by or on behalf of the person making the deposit and the relevant deposit taker.
- the relevant deposit taker must make or credit a payment or series of payments (referred to as the "deposit return") to the depositor from profits resulting from the use of the money deposited and in proportion to the money deposited.

8.2 Tax Treatment of Deposit Return

8.2.1 Application of Section 130 Taxes Consolidation Act 1997

Because Islam prohibits the payment of interest, a deposit transaction must be structured as a type of agency/partnership agreement between the deposit taker and the customer in order to be Shari'a compliant. As a result, it may seem as if the deposit return is dependent on the results of the business. This in turn could trigger the provisions of section 130 which ensure that dividends are not paid out in the guise of interest to investors.

Where section 130 applies, the payment of interest is treated as the payment of a dividend with the result that the person paying the interest is not entitled to a deduction for the amount paid.

Certain Shari'a compliant deposit transactions may be structured so that the amount payable to the depositor may be linked to a certain extent to the results of the business and so conflicts with Section 130. In such cases, the financial undertaking would not be entitled to a deduction for the return paid to the depositor.

In general, Revenue will not regard the return as being dependent on the results of the business and consequently section 130 will not apply, where all of the following conditions are satisfied:

- The amount of the return equates in substance to a commercial return on a deposit of money.

- The expected return on the deposit transaction is determined at the time of entering into the arrangement and forms part of the agreement.
- The expected return is equivalent to a conventional deposit return.
- The deposit return is paid annually or more frequently.
- The expected return amount is not altered during the course of the transaction except insofar as the amendment equates with movements in interest rates applicable to similar conventional bank deposit arrangements.

Where all of the conditions are not satisfied, the provisions of section 130 will apply so as to re-categorise the amount of return payable as a distribution.

8.2.2 Deposit Interest Retention Tax

If section 130 does not apply (see paragraph 8.2.1 above), the finance undertaking (i.e. the relevant deposit taker) is treated for tax purposes as if it were paying interest on a deposit of money. This brings the transaction within the Deposit Interest Retention Tax (DIRT) regime. As such, the deposit taker will be obliged to deduct DIRT from the return paid to the depositor unless the transaction falls within one of the exceptions such as where the recipient is a non-resident or is aged 65 or over or is permanently incapacitated.

8.2.3 Tax treatment of Finance Undertaking

For corporation tax purposes, the finance undertaking will be treated as having made a payment of interest to the depositor and will be entitled to deduct the amount as an expense of its trade - however see paragraph 8.2.1 above in this regard.

Where the finance undertaking charges an agency fee, this will be treated as income for tax purposes and the undertaking will be liable to Corporation Tax on the fee as it would in respect of any other amounts charged to the customer for its services.

Section 267Q also provides that the deposit taker will not be regarded as carrying on a trade in partnership with the beneficial owner of the deposit merely by virtue of the arrangement. This is necessary because the Islamic equivalents of deposit transactions have some of the characteristics of a partnership.

8.2.4 Tax Treatment of Depositor

The depositor is taxed on the return on the same basis as if s/he derived interest income from a normal bank deposit. Thus where the depositor is an Irish resident individual, the amount of DIRT deducted from the return will satisfy the individual's tax liability on that income and s/he will have no further income tax liability in this regard.

Where the depositor is a company, the interest income would generally be chargeable to Corporation Tax at the 25% rate in line with the rules relating to the taxation of deposit interest.

9 Investment (Sukuk) Transactions

An investment transaction equates to the purchase of securities and is similar to a securitisation or other structured finance arrangement. Unlike a conventional securitisation or structured finance transaction, an investor in an investment certificate holds a share or interest in the asset underlying the arrangement and which is managed by the company issuing the certificates. There is no entitlement to interest on the certificate, instead the investor shares in the profits and losses derived from the exploitation of the underlying assets by the certificate issuer. Section 267N defines an investment transaction as a transaction whereby a person acquires an investment certificate and receives an investment return. It is designed to cover both acquisitions from the original issuer and acquisitions on the secondary market. In Islamic finance the structures dealt with in this provision are known as Sukuk.

9.1 Definition of Investment Certificate

An investment certificate must meet four conditions to qualify for the treatment outlined in the legislation. The conditions are as follows:

Paragraph (a) requires that the certificates be issued to a person in order to establish the claim of that person over the rights and obligations represented by the certificate. Essentially this means that the certificate evidences the investor's rights to a share in the ownership of the underlying assets;

Paragraph (b) requires that the certificate should entitle the owner to an amount which is equivalent to a share in the profits or losses derived from the underlying asset and which is in proportion to the number and value of certificates owned;

Paragraph (c) requires that the certificates not be issued to "specified persons"[1]. The certificates are not required to be listed on a Stock Exchange;

Paragraph (d) requires that the certificates should be treated under Generally Accepted Accounting Principles as a financial liability of the issuing company in its accounts.

The terms of sukuks have evolved such that it is not uncommon that they grant an ownership interest to the holder of the investment certificate not in the underlying assets of the qualifying company but instead in an underlying asset which is a financial liability of the counterparty that ultimately underpins the sukuk arrangement and its related cash flows (referred to as the ultimate obligor below). In such cases, the qualifying company's obligations in respect of the investment certificate issued by it may be considered to relate to underlying assets that it manages on behalf of the investors in the investment certificates issued by it.

[1] Refer to Tax and Duty Manual (TDM) TDM 04-09-01 for details on who is a specified person.

For accounting purposes, the qualifying company's interest in the assets may be treated in a manner that is analogous to that which applies under a bare trust arrangement i.e. for accounting purposes, the qualifying company that has issued the investment certificate to investors may be regarded as holding its interest in the underlying assets not on its own behalf but on behalf of the investors. As such an arrangement would not typically result in the recognition of the underlying assets or related financial liability on the balance sheet of the qualifying company, such arrangements may therefore not meet the requirement of paragraph (d) that the investment certificate **be 'wholly or partly treated in accordance with generally accepted accounting practices as a financial liability of the qualifying company that issued the certificate'.**

Provided the investment certificate is a *bona fide* sukuk, paragraph (d) will be treated as satisfied where it would be reasonable to consider that the underlying asset is a financial liability, within the meaning of IAS32, of the ultimate obligor counterparty.

In relation to this requirement, it is noted the qualifying company and investor in a sukuk are unlikely to be in a position to know the accounting treatment adopted by the ultimate obligor in respect of the sukuk arrangement. They should treat a *bona fide* sukuk as an investment certificate unless, based on the terms of the sukuk, they have reason to know that it would not be a financial liability within the meaning of IAS32.

9.2 Definition of Investment Return

The 'investment return' is defined as:

(a) the excess of the amount paid by the certificate issuer on redemption of the certificate over the amount paid in respect of the certificate by the original beneficial owner of the certificate, and

(b) the amount of any other periodic payments made by the Sukuk issuer to the certificate owner from profits or gains derived from the asset.

Effectively, the investment return equates to the amount which would be equivalent to interest on a conventional bond and includes any premium payable on redemption whether that amount is payable to the original purchaser or to an investor who purchased the certificate on the secondary market (paragraph (a)) together with any other periodic payments made by the issuing company from profits or gains derived from the underlying asset (paragraph (b)).

9.3 Taxation of the Investment Return

Where an investment transaction meets the conditions of 267N (1) as outlined above, section 267R provides that the investment return will be treated for the purposes of the Taxes Acts as interest on a security and the return will be chargeable to tax accordingly. The section is made subject to section 130 of the TCA 1997 in order to ensure that any investment return which is similar to a distribution will not be treated as interest.

Shari'a compliant investment transactions may be structured so that the amount of the investment return may be linked to a certain extent to the results of the issuer and so conflicts with section 130. In such cases, the issuer would not be entitled to a deduction for the amount of the return paid to the investor.

In general, Revenue will not regard the return as being dependent on the results of the business and consequently section 130 will not apply, where all of the following conditions are satisfied:

- the amount of the return equates in substance to a commercial return on an investment,
- the expected return on the investment is determined at the time of entering into the transaction and forms part of the agreement,
- the expected rate of return is equivalent to a rate of interest on an equivalent conventional investment, and
- the expected return amount is not altered during the course of the transaction except to the extent that any variation equates with movements in interest rates applicable to conventional bank deposit arrangements of similar amounts.

Where all of the conditions are not satisfied, the provisions of section 130 will apply so as to re-categorise as a distribution the full amount of the investment return.

9.4 Application of Section 110 of the Taxes Consolidation Act 1997

An election to be taxed under Part 8A of the Taxes Consolidation Act 1997 does not in itself, preclude a company from being a qualifying company within the meaning of section 110 of the TCA. Where the company issuing the certificates is also a qualifying company within the meaning of section 110, the company should:

- firstly, submit the appropriate election form SFT 1 or SFT 2 to their Tax Office, and
- secondly, submit a section 110 notification form to Revenue.

9.5 Tax Treatment of the Certificate Owner

The certificates confer a share in the ownership of the underlying asset to the certificate owner. In order to remove any doubts as to whether the certificate owner or the issuing company is entitled to capital allowances on the asset and as to which of the parties would be chargeable to tax on the income and gains from the asset, section 267S provides that:

- for the purposes of the Tax Acts, the certificate owner is not regarded as having a legal or beneficial interest in the assets held by the qualifying company,
- income, profit, gains or losses arising from the underlying asset in an investment transaction will be regarded as income, profits, gains or losses of the certificate issuing company, and
- the certificate owner will not be entitled to capital allowances on the underlying assets in the transaction.

9.6 Tax Treatment of the Certificate Issuer

Section 267S provides that income, profits, gains or losses arising from or attributable to the assets held by the certificate issuing company (including any increase or decrease in the value of the asset) shall be income, profits, gains or losses, as the case may be, of that company and that company shall be chargeable to corporation tax accordingly. The issuing company may also treat investment returns payable in respect of investment certificates it has issued as expenses and such investment returns shall be deductible in computing its profits for tax purposes to the same extent as they would be deductible if they were interest payable by that company.

9.7 Stamp Duty Treatment of the Investment Certificate

Section 85A of the Stamp Duty Consolidation Act (as inserted by section 137 of the Finance Act 2010) provides for an exemption from stamp duty on the issue, transfer or redemption of an investment certificate as defined in section 267N.

10 Miscellaneous

10.1 Interest reporting

Section 267T of the TCA 1997 applies the interest reporting provisions of Part 38 of the TCA 1997 to a credit return, a deposit return and an investment return as if that return were a payment of interest.

10.2 Transactions with non-resident persons

In certain circumstances, the nature of some Islamic financial transactions could be such as to make it seem as if the finance undertaking constitutes a permanent establishment for the customer. This is particularly so in the case of Wakala and Mudaraba arrangements where the legal nature of the transaction is that the customer appoints the financial institution as his agent. In these cases, Revenue is prepared to agree that a non-resident customer who enters into such an arrangement with a financial institution in the State will not have a permanent establishment in the State merely by virtue of that arrangement.

Appendix I – Schedule of key updates

November 2018	Clarification re the accounting treatment of sukuks (8.1) and the tax treatment of the Certificate issuer (6.8).
August 2026	Update to title of Tax and Duty Manual. Introductory wording included under section "Introduction" (1). References to the VAT Act 1972 have been updated to the VAT Consolidation Act 2010. Update to wording of section "Overview of the tax treatment of Islamic financial transactions" (2.1). Update to definition of "financial institution" under section "Credit and Deposit Transactions" (6.2.1) following amendment to definition of "financial institution" under section 891B TCA 1997 by Finance (No.2) Act 2023.