

[13-02-02] Examples of what constitutes a close company or not (Tax Instruction 13-01-02 refers)

Part 13, Chapter 1 TCA 1997

This document should be read in conjunction with section 430 et seq. TCA 1997

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For the purpose of illustrating whether a company is a **close company** or not (see Tax Instruction 13-1-2) ten **examples** are set out below. Each of the examples refers to a company having shares which are not dealt in or quoted on a stock exchange.

Example 1

Company X Ltd. has 1,000 issued shares of €1 held as follows:-

The two trustees of A's settlement	449
Mrs. A	60
Ten other shareholders	<u>491</u>
Total issued ordinary shares	1,000

The ten shareholders are not associated with each other or with A or Mrs. A.

Mrs. A and the two trustees of A's settlement are associated and the one composite person controls the company. It is a close company.

Mrs. A and the two trustees of A's settlement are associated (section 433(3) - see par. 8 of Tax Instruction 13-1-2) and the one composite person controls the company.

The company is a close company.

Example 2

The €1 issued shares in a company are owned as follows:-

Ordinary shares

Directors -	
A	4
B (cousin of A)	<u>4</u>
	8

12 individuals, none of whom is a nominee or associate

of any other shareholder.....	<u>4,992</u>
Total issued ordinary shares	5,000

5 per cent preference shares	
A (see above)	<u>5,000</u>
Total nominal and issued capital	10,000

The company is a close company because A possesses more than half the share capital whether issued or not (section 432(2)(a) - see par. 16 of Tax Instruction 13-1-2).

Example 3

The issued ordinary shares in a company carry one vote each but the "A" ordinary shares do not confer voting rights. The shareholders are as follows:-

	Ordinary	"A" ordinary
A (director)	280	
Wife of A	100	
B (brother of A, and director)	10	
Trustees of A's settlement	40	
X Ltd (controlled by A)	<u>80</u>	
	510	
Mrs. C (director) (daughter of B)	20	
10 other equal holdings - total	<u>470</u>	<u>500</u>
Total issued shares	1,000	500

The shares carry equal rights to a dividend. A's wife has made a loan of €20,000 to the company at 15% per annum interest. There is no share premium account or other comparable account.

- (a) Control by voting rights [section 432(2)(a)]
- (b) The associates of A are -
 - (i) his wife and his brother
 - (ii) the trustees of A's settlement
 - (iii) The rights and powers attributable to A are -
 - (A) the rights and powers of his associates, and
 - (B) the rights and powers of X Ltd.

As a total 510 votes are thus possessed by A or attributable to him,
the company is a close company controlled by one composite person.

- (c) Loan interest paid to Mrs. A

Section 437 (see par. 3) applies because -

- (A) the company is closely controlled,
- (B) A's wife is an associate of A, and
- (C) A is a director who has a material interest in the company.

The interest treated as a distribution, and not allowed as a deduction in arriving at the corporation tax profits for the accounting period, would be the excess of the interest paid over 13% per annum of €1,500. For example, for an accounting period of twelve months, the limit would be 13% of €1,500 = €195; for an accounting period of six months it would be $6/12 \times 13\%$ of €1,500 = €98.

Example 4

The authorised and issued share capital of X Ltd. is €1,000 in the form of 1,000 ordinary shares of €1 each, held as follows:-

A	200
B	100
C	50
D	50
E	40
Y Ltd	99
"Other shareholders"	<u>461</u>
Total issued ordinary shares	1,000

A is works manager and B and C are directors.

The issued capital of Y Ltd. is €100 in the form of 100 ordinary shares of €1 each, held by:

F (son of E)	60
G	40

The shareholders in X Ltd., other than Y Ltd., are all individuals and none are related or otherwise associated. No "other shareholder" holds more than 50 shares.

Control: The rights in the shares held by Y Ltd. in X Ltd. may be attributed to F who controls that company.

F is an associate of E but the rights attributed to F cannot be further attributed to E [see control provision under section 432(6)].

No group of five persons or fewer can control X Ltd. neither the directors or participators control it.

X Ltd. is not a close company.

Example 5

The facts are the same as in Example 4 except that F is the holder of one share in X Ltd. and is thereby a participator in X Ltd. and B, C and F are directors of X Ltd.

Control:- Rights can be attributed to F as follows:-

Shares held in own right	1
Shares held by E (an associate)	40
Shares held by Y Ltd. (controlled by F)	<u>99</u>
	140

Thus A, B, C, D and F hold (or have attributed to them) the rights in 540 shares and control X Ltd.

X Ltd. is a close company.

Example 6

The authorised and issued share capital of X Ltd. is as in Example 4 but is held as follows:-

A	1
B (brother of A)	100
C (son of A)	100
D	100
E	50
F	50
G	50
H	50
"Other shareholders"	<u>499</u>
Total issued ordinary shares	<u>1,000</u>

A is the works manager but not a director in name.

B, C, D, E, F, G and H are directors of X Ltd.

(a) Status of directors etc. - rights can be attributed to A are as follows:-

Shares held in own right	1
Shares held by B (an associate)	100
Shares held by C (an associate)	<u>100</u>
Shares attributed to A	<u>201</u>

Thus A with his associates controls 20% of the ordinary shares and being a manager of the company is a "director" [section 433(4)].

- (b) Control: the company is not controlled by five or fewer participators but the shares held by "participators" who are directors [section 430(1)] including the shares attributed to A (as at (a) above) [section 432(6)] are as follows:-

Rights of participators who are directors

Shares held by (or attributed to) A	201
Shares held by D	100
Shares held by E	50
Shares held by F	50
Shares held by G	50
Shares held by H	<u>50</u>
	<u>501</u>

Thus, the company is controlled by "participators" (more than five in number) who are "directors" and is therefore a close company.

Example 7

A company has authorised capital of €4,500 in €1 ordinary shares, of which €3,000 is issued as follows:-

A	150
B	150
C	150
D	250
E	250
F	250
20 other shareholders (no one holder having over 100 shares)	<u>1,800</u>
Total issued ordinary shares	<u>3,000</u>

The 20 other shareholders are individuals and none of the shareholders is an associate of any other.

A, B, and C are directors. They each enter into a service agreement providing that they are to remain directors for five years from 1 January 2014 and that on 31 December 2018 they shall each have the right to purchase 500 €1 shares in the company at par.

Control	A, B, and C each exercises or is entitled to acquire rights in 650 shares [section 432(2)(a) and (4)]
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Thus A, B, C, D and E together constitute a group which is “able to exercise or is entitled to acquire control” of the company (with 2,450 shares out of 4,500) (section 432(2) and (3)]. The company is a close company as from 1 January 2014.

Example 8

The authorised and issued capital of an investment holding company is €33,000 and is owned equally by eleven individuals who are not associated. Two of them are directors.

There are two loan creditors as follows:-

A (director) - €35,000 at 16 %

B (not a shareholder)- €13,500 at 14 %

Neither A nor B is a banker. B is not an associate of a director.

In a winding-up the value of the net assets distributable among members including loan creditors would be €120,000 as follows:-

	€
Deposits with finance houses, etc.	30,000
Market value of quoted investments (representing the remainder of the assets)	<u>110,000</u>
	140,000
Deduct sundry creditors for management expenses	300
bank overdraft	<u>19,700</u>
Value of net assets	<u>120,000</u>

- (a) Control. - The company cannot be shown to be controlled by five or fewer participators. In a liquidation, the assets would however be distributed as follows:

A as loan creditor	35,000
B loan creditor	13,500
Shareholders (€6,500 each)	<u>71,500</u>
	120,000

More than half of this sum would be received by three persons, i.e.,

A (€35,000 + €6,500)	41,500
B	13,500
Any shareholder other than A	<u>6,500</u>
Distribution to three persons	<u>61,500</u>

The company is therefore a close company by reference to section 432(2)(c) because the inclusion under section 433(1)(b) of loan creditors as participators shows that it is controlled by three participators.

(b) Interest paid. - The interest paid is dealt with as follows :

- (i) The excess of the loan interest paid to A (a director) over a sum equal to interest at 13 % per annum is a distribution.
- (ii) The loan interest paid to B (a participator but not a director or a director's associate) is not a distribution.

Example 9

The issued ordinary capital of a trading company (other issued capital having no voting rights) is held as follows:-

A Ltd. (not a close company)	280
B. Ltd. (a close company)	270
C Ltd. (not a close company)	230
D (director)	40
E (director)	30
F (an individual)	30
20 others	<u>120</u>
Total issued ordinary shares	1,000

Control - The requirements of section 430(4)(a) - see par. 20 of Tax Instruction 13-1-2) are regarded as satisfied because -

- (a) upon one combination of shareholdings, control is in the hands of A Ltd. and C Ltd., and
- (b) it cannot be treated as a close company except by taking either A Ltd. or C Ltd. as one of the five or fewer participators requisite for its being treated as a close company .

The company is not a close company.

See, however, Example 10 below.

Example 10

The ordinary shares are held as in Example 9. G, an individual, holds redeemable loan stock and would receive in a winding-up more than half the assets available for distribution among the participators.

Control: as G is in control of the company by reference to section 432(2)(c), the requirements of section 430(4)(a) are not met and, irrespective of the ownership of the ordinary shares, the company is a close company.