

[13.2.3] Loans to participators [section 438 TCA 1997]

1. Where a close company makes a **loan** or advances money to -
 - (a) an individual who is a participator in the company or
 - (b) an individual who is an associate of a **participator** in the company or
 - (c) a non-Irish resident company (confined to non EU resident companies if the loan was made on or after 6 February 2003) or
 - (d) a company which is acting in a fiduciary or representative capacity and is a participator or an associate of a participator in the close company.

then, unless the loan or advance was made in the ordinary course of the close company's business and that business includes the lending of money, the close company is obliged to account to Revenue under section 239 (as a "relevant payment") for income tax, at the standard rate for the year of assessment in which the loan or advance is made, on the grossed up equivalent of the loan or advance, as if that grossed up equivalent were an annual payment made by the company. This however, will not be allowed as a charge on the company's income within the meaning of section 243 ("Allowance of charges on income").

The charge to income tax is imposed on the company by "deeming" the company "to have paid ...an annual payment". This deeming is "for the purpose of section 438 only. Consequently, the "deemed" annual payment is not to be regarded as income in the hands of the borrower, and the borrower is not entitled to any credit for the income tax borne by the company in respect of the "deemed" annual payment.

As regards the treatment of the borrower where the loan or advance is released, see paragraph 9 of this Instruction.

As regards -

- (i) the meaning of “loan or advance”, see paragraph 2 below;
- (ii) the definitions of “participator” and “associate of a participator”, see paragraphs 3 - 11 of Tax Instruction 13.1.2;
- (iii) reciprocal arrangements, see paragraphs 4 and 5 below.

“Individual” includes “individuals” (section 11(a), Interpretation Act, 1937). Where, therefore, a close company makes a loan or advance to a partnership and one of the partners is a participator in the company, the other partners are his associates and the loan or advance, is within (a) and (b) above. Similarly, where a loan is made to trustees and any shares or obligations of the company are subject to the trust, the trustees are participators and/or associates of a participator and the loan is therefore within (a) and (b) above. Where the trustees are a “trust company” and that company is a participator or an associate of a participator, (d) above will apply.

Section 438 applies only if the company is a close company at the time the loan or advance is made.

2. Extension of ordinary meaning of the word “loan”

The ordinary meaning, of the word “loan” is extended by section 438(2) which provides that the cases in which a close company is to be regarded as making a loan to any person include the following:-

- (a) Where the person incurs a debt to the close company. This does not apply if -
 - (i) the debt is incurred for the supply of goods or services in the ordinary course of its trade of business, and
 - (ii) the credit given by the company to that person does not exceed six months or the period of credit normally given to the company’s customers, whichever is the shorter.
- (b) Where a debt due from the person to a third party is assigned to the close company.

Where (a) or (b) above applies, the company is regarded as making a loan equal to the amount of the debt.

3. Conditions to be satisfied for the exclusion of a loan or advance made by a close company to a director or employee of the close company

Where a close company makes a loan or advance for any purpose to a director or employee of the close company or of its associated company, that loan or advance is not within section 438, if all of the following conditions are satisfied:-

- (a) neither the amount of the loan nor that amount when taken with any other loans made by the close company or any of its associated companies to the borrower or to the spouse or civil partner of the borrower exceeds €19,050,
- (b) The borrower works full-time for the close company or any of its associated companies, and
- (c) the borrower does not have a material interest in the close company or any of its associated companies.

Where the borrower acquires a material interest (or an existing interest is enlarged so as to become material) at a time when any loan remains wholly or partly outstanding, the company is to be regarded as making to him a loan or loans equal to the amount or amounts so outstanding at the time when the material interest is acquired. The loans deemed to be so made are not excluded and the company is required to account to Revenue for tax in accordance with the provisions of section 438(1). Relief is therefore not given for loans intended to be used to increase substantially the borrower's stake in the company.

4. Interposition of an intermediary [section 438(5)]

A loan which is not directly within section 438(1), but which is part of an arrangement which includes a payment or transfer of assets to (or liabilities from) a participator or associate of a participator is deemed under section 438(5) to have been made to that participator for the purpose of section 438(1) (for example, a loan to enable an employee or trustees who are not participators to buy shares from an existing shareholder). The loan, however, may be exempted if the deemed borrower (i.e. the existing shareholder in the company) can show that the deemed loan to him satisfies the conditions in section 438(3).

Section 438(5) provides that:

“Where under arrangements made by any person otherwise than in the ordinary course of a business carried on by that person—

- (a) a close company makes a loan or advance which apart from this subsection does not give rise to any charge on the company under *subsection (1)*, and
- (b) some person other than the close company makes a payment or transfers property to, or releases or satisfies (in whole or in part) a liability of, an individual who is a participator in the company or an associate of a participator,

then, unless in respect of the matter referred to in *subsection (b)* there is to be included in the total income of the participator or associate an amount not less than the loan or advance, this section shall apply as if the loan or advance had been made to the participator or associate.”

This is subject to paragraph 5 of this Instruction below.

Example 1

X Ltd., a close company, instead of making a loan to A, an individual participator, makes it to an associated company, Y Ltd. The latter then passes the loan to A.

The loan by X Ltd. to Y Ltd. is treated as if it had been made direct to A.

Example 2

A Ltd., a close company, makes a loan to D, an individual who is a participator in B Ltd., but not in A Ltd. B Ltd., acting in concert with A Ltd., then makes a loan to E, an individual who is a participator in A Ltd. but not in B Ltd.

A Ltd and B Ltd are treated as if they had made loans to their own participators, i.e. E and D respectively.

5. Non-Applicability of Paragraph 4

The provisions in paragraph 4 above do not apply where, as a result of the payment, transfer, release, within section 438(5)(b), an amount not less than the loan or advance falls to be included in the total income of the recipient of the payment. This may happen, for example, where the payment to the recipient is treated as his income for income tax purposes, e.g. as a distribution within sections 130 - 135 or section 436.

6. Registered industrial and provident societies [section 438(8)]

For the purposes of this section, a registered industrial and provident society is treated as a close company if it would be such but for the exclusion of such societies contained in section 430(1)(b). Accordingly, loans and advances made to a participator in such a registered industrial and provident society (if it is a close company following the application of the rules contained in section 430 as modified by this provision) may be subject to a charge to tax under this section.

7. Repayment –section 438(4)]

Section 438(4) deals with the situation with regard to a possible repayment. The relevant period for claiming relief is 4 years. The section now reads:

- (4) (a) Where, after a company has been assessed to tax under this section in respect of any loan or advance, the loan or advance or any part of it is repaid to the company, relief shall be given from that tax or a proportionate part of that tax by discharge or repayment.
- (b) Notwithstanding any limitation in *section 865(4)* on the time within which a claim for a repayment of tax is required to be made, relief under this subsection shall be given on a claim which shall be made within 4 years from the end of the year of assessment in which the

loan or advance, or any part of it, as the case may be, is repaid to the company.

8. Section 239 applied for the purposes of the charge under section 438

Section 438(1)(b) applies section 239 (income tax on payments by resident companies) for the purposes of the charge, assessment and recovery of income tax under section 438. The formal procedure prescribed by section 239 applies to any amount which under section 438 is deemed to be an annual payment [section 239(1)(a)].

9. Section 439 (Effect of release, etc. of debt in respect of loan under section 438)

Where a company, which has been or is liable to be assessed under section 438 in respect of a loan or advance, releases or writes off the whole or part of the debt thus created, the person to whom the loan or advance was made is regarded, for the purposes of computing his/her total income, as having received at that time income of an amount which after deduction of income tax at the standard rate is equal to the amount released or written off (Section 439(1)(a)).

The income tax notionally deducted under this procedure is not repayable. [subsection (1)(b)].

The income tax so notionally deducted is not available to relieve the recipient of any obligation to account for tax on annual payments made by him/her [subsection (1)(c)].

In respect of any part of the amount released which is charged at less than the standard rate of income tax the tax credit is not to exceed the amount of tax charged, and in respect of any part of the amount released which is charged at standard rate or higher rate the tax credit is equal to tax at the standard rate on the amount so charged [subsection (1)(d)].

Where a loan to which section 438 applies was made to a person who has died or to the trustees of a trust which has terminated, and all or part of the loan is written off, the deemed income represented by the debt released is regarded as income of the estate or the beneficiary, as the case may be, at that time. Where the loan is written off to the benefit of the estate of a deceased person which is under administration, the income is treated as chargeable to income tax at the higher rate [subsection (2)].

Section 439 and section 438 are to be construed together [subsection (3)].

[Tax Instruction [13.2.4](#) refers]