Transfers of value derived from assets (S.543)

Part 19-01-16

This document should be read in conjunction with section 543 of the Taxes Consolidation Act 1997

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Introduction

Section 543 of the Taxes Consolidation Act 1997 ("TCA 1997") provides that in certain types of transaction in which value or valuable rights pass from one person to another the transfer of value is regarded as a disposal and acquisition for the purposes of Capital Gains Tax ("CGT"). This rule applies even where there is no consideration involved. Where there is no consideration or the consideration is not for full value, the transaction is treated as a disposal made at market value.

16.1 Transfers otherwise than at arm's length

Where a person transfers an asset otherwise than at arm's length and for a consideration less than market value the asset is deemed to have been disposed of at market value and the chargeable gain or allowable loss computed accordingly (see, however, **para 16.4** as respects transfers to employees and directors). Certain transactions whereby value or valuable rights are transferred from one person to another are to be treated as disposals on which CGT is chargeable. Details of these are given in **para 16.5**.

16.2 Power to recover tax from the acquirer

Where the disponer of an asset transferred at an undervalue fails to pay all the tax on any gain arising on the disposal, Revenue has power to recover a due proportion of the tax from the acquirer as if the transaction were a gift of the asset to him or her - **section 978(2) TCA 1997**.

16.3 Transfer of assets by a close company at an undervalue

As regards the transfer of assets by a close company at an undervalue, see Tax and Duty Manual (TDM) Part 19-04-12.

16.4 Transfer of an asset at undervalue by an employer to an employee

The transfer of an asset at undervalue by an employer to an employee or director is a disposal for CGT purposes. Normally the consideration is deemed to be market value (**section 547(4) TCA 1997 -** see TDM Part 19-02-06) but if the employer is within Case I or II of Schedule D, the consideration for his disposal should be treated as the cash consideration, if any, received by him or her provided that the following conditions are satisfied:

(a) The employee or director is liable to tax under Schedule E on the excess of the market value over the cash consideration. This condition should be regarded as satisfied even though the excess, or part of it, is not actually charged under Schedule E as, for example, when **section 201(5) TCA 1997** applies.

(b) The transfer of the asset at undervalue is not in satisfaction of an antecedent debt for unpaid remuneration. Where there is such a debt, the cash consideration, if any, given by the employee or director for the asset should be regarded as increased by the amount of the debt.

Where the cash consideration payable by the employee or director is less than the cost of the asset to the employer, no allowable loss accrues to the employer because a deduction for his or her loss is given under Case I or II of Schedule D (TDM Part 19-02-05).

The employee's cost of acquisition is the market value of the asset.

If the employee or director is not charged on the excess under Schedule E but **section 130(3) TCA 1997**, applies in relation to the transfer at undervalue, then the company (the employer) should be treated as disposing of the asset at market value (**section 547(4) TCA 1997** – TDM Part 19-02-06).

16.5 Value or valuable rights

Where value or valuable rights are transferred from one person to another other than for full consideration, in circumstances such that there would otherwise be no occasion of charge, the transfer should be treated as a disposal and acquisition at market value, and as an occasion on which tax is chargeable. The provision is effective in the following situations:

(a) Where a person who has control of a company so exercises that control so that value or valuable rights are transferred from shares which he or she owns (or which are owned by persons connected with him or her) into other shares. Such a transfer should be treated as a disposal of the whole (or part) of the shares in question.

(b) Where the lessee of a property was formerly its owner and the terms of the lease are adjusted in favour, generally, of the lessor. Such an adjustment should be treated as a disposal of property by the lessee.

(c) Where a person is entitled to enforce a right over an asset, the extinction of that right by the person in question should be regarded as a disposal of the right.

Example 1

In 2013, A bought 2,000 €1 ordinary shares in XYZ Ltd., which gave him control of the company. The purchase price was €100,000.

In 2021, A arranged for the authorisation and issue at par of 1,000 of a new class of €1 "A" ordinary shares to his child. Immediately thereafter, the rights attaching to the original ordinary shares were reduced to the status of preference shares carrying only an 8 per cent dividend; and all other rights of voting, in profits, and on liquidation were passed to the "A" shares.

The value of the original shares was thus reduced and value passed to the new shares.

If the value of the old shares immediately before the arrangement in 2021 was agreed at €150,000 and immediately after that date at €20,000, the computation of the gain chargeable on A (subject to expenses) would be as follows:

Value of shares before the change	€150,000
Value of shares after the change	€20,000
Value passing from old to new shares	€130,000
Part cost allowable:	
$€100{,}000 \times \dfrac{€130{,}000}{€130{,}000 + €20{,}000} =$	(€86,667)
Chargeable gain	€43,333

The acquisition price of the "A" shares to his child would be:

€130,000 + €1,000 = €131,000.

Example 2

In 2013, RST Ltd., was formed with an authorised share capital of €10,000 in €1 ordinary shares. B subscribed for 7,500 shares at par and her spouse subscribed for 2,500 shares at par.

In 2021, B arranged for the authorisation and issue of 5,000 new €1 ordinary shares, 2,500 to be subscribed for by each of her two children at €1 per share.

Before the new issue, the value of B's shares was €50 per share. As a result of the new issue and due to her loss of control, the value of B’s shares after the new issue was €30 per share. After the new issue, the value of the three holdings of 2,500 shares (i.e. by the spouse and each of the 2 children) was €20 per share. The value of the original shares was thus reduced and some value passed from the old to the new shares. The computation of the gain chargeable on B (subject to expenses) is as follows:

	1st child	2nd child
Value of children's shares (2,500 at €20 per share)	€50,000	€50,000
Less price paid per share (1)	€2,500	€2,500
	€47,500	€47,500
Total value passing into new shares		€95,000

Value of B's shares before this issue of new shares (7,500 shares @ €50)	€375,000
Value of B's shares after the issue of new shares (7,500 shares @ €30)	(€225,000)
Value passing out of B's shares	€150,000

But the value passing out of B's shares is greater than that which passed into the new shares so that some restriction of the gain must be made.

The acquisition cost of the new shares is €50,000 in the case of each child, i.e. €2,500 cash subscription plus €47,500 value passing from the old shares.

The figure of disposal proceeds used in the computation of B's chargeable gain is restricted to the value passing into the new shares as follows:

Disposal proceeds	€95,000
Less portion of cost allowable	
$€7,500 \times \dfrac{€95,000}{€95,000 + €225,000} =$	(€2,227)
Chargeable gain	€92,773

Example 3

In 2013, C buys freehold property for €400,000.

In 2018, he gives the freehold to his child D subject to a 99-year lease reserved to C himself, the rent payable by C to his child being 5c per year, if demanded. The effect of this transaction is to leave C with virtually the whole property, since D is entitled only to a reversion at the end of 99 years and this has negligible value. (C has made a part disposal, but the value passing to his child is too small to warrant a computation of the gain on that part disposal).

In 2021, C agrees to pay to D a full economic rent for the remainder of the term of the lease. The real value has now passed out of C's leasehold interest, and he is treated as making a disposal at market value of the interest passed to D. If that value was €500,000, the gain chargeable on C (subject to expenses) is as follows:

Value transferred	€500,000
Cost of freehold	€400,000
Chargeable gain	€100,000

The acquisition price of D's interest in the property is €500,000.

Example 4

The owner-occupier of a farm which cost €800,000 in 2016, gives the farm to her child subject to the mother's continuing occupation of the farm under a lease. The mother is under 55 years of age. If the market value of the farm subject to that lease is €900,000, the gain chargeable on the mother at the date of the gift will be computed by reference to that value as a part disposal, the value of the right to occupy being included in the denominator of the part disposal fraction (see TDM Part 19-02-14).

If the mother subsequently gives up her lease, there is a further disposal by her (within the terms of **section 543(4) TCA 1997** of her rights in the property.

If the value of the right to occupy is €180,000 at the date of the gift and €150,000 at the end of the lease, the chargeable gains (subject to expenses and to relief for the principal private residence - see TDM Part 19-07-03) will be as follows:

On the gift:

Market value of farm subject to lease		€900,000
Part cost allowable -		
$€800,000 \times \dfrac{€900,000}{€900,000 + €180,000} =$		(€666,667)
Chargeable gain		€233,333
On the mother giving up the lease:		
Market value of the right to occupy		€150,000
Balance of cost €800,000 less €666,667	€133,333	
Part wastage (see below)	(€33,333)	(€100,000)
Chargeable gain		€50,000

The mother's right of occupation is a wasting asset (see TDM Part 19-02-16). If her expectation of life at the date of the gift (in 2016) was 20 years and the lease was ended 5 years later (in 2021), the part not allowable is:

$$\frac{5}{20} \times €133,333 = €33,333$$