

Shares in close company transferring assets at undervalue

Part 19-04-12

This document should be read in conjunction with section 589 Taxes Consolidation Act 1997

Document last reviewed May 2019

Does not reflect current Revenue position.

Executive summary

This section covers the situation where a close company (defined in [section 5](#) by reference to [section 430](#)), or a company which would be a close company if resident in the State, transfers an asset to any person other than by means of an arm's length bargain and for a price which is less than its market value. In any such case the difference between the consideration received for the asset and its market value is to be apportioned among the issued shares of the company so that, in the event of a disposal of any of those shares, the cost of acquisition of those shares is to be reduced by the proportionate part of that difference.

12.1 Transfers of assets otherwise than at arm's length

Where a company 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 (as respects transfers to employees or directors, see [Tax and Duty Manual Part 19-01-016](#), paragraph 4. Where the transferor is a "close company" adjustment of the value at which the asset was transferred has to be followed, if the avoidance of tax is to be wholly prevented, by a compensating adjustment in the value of the company's shares. Otherwise, the value of the company's assets will have fallen to the extent to which the asset was transferred at less than its market value, and this will affect the value of the shares. Thus, where an asset is transferred at an undervalue by a close company other than by way of a bargain at arm's length, the cost attributed to the shares in the company when they are disposed of should be reduced by a proportionate part of the difference between the consideration for the asset and its market value.

Example 1

In 2005, A buys 200 ordinary shares in a close company (of which the issued share capital is 1,000 ordinary shares) for €3,000. In 2010, the company sells to a "connected person" (as defined in [Section 10](#)) for €8,000 a chargeable asset whose market value at the date of sale is €20,000. The sale is deemed to have taken place at €20,000 and the chargeable gain of the company is computed accordingly.

In 2014, A sells the 200 shares for €4,500. The chargeable gain is computed as follows –

		€
Sale price of 200 shares		4,500
Cost of shares	3,000	
Less undervalue apportioned to 200 shares:		
€12,000 (20,000 - 8,000) x 200/1,000	<u>2,400</u>	
Adjusted cost of shares		600
Chargeable gain		3,900

12.2 Close companies

If the person owning any of the shares at the date of transfer is a close company or would be a close company but for the fact that it is not resident in the State the amount apportioned to the shares should be apportioned among the shares of that close company and so on, through any number of close companies in respect of shares in any one of those companies which were acquired before the transfer of the asset at undervalue. This is necessary because the value of each subsidiary share depends on the value of the assets of the first company and, consequently every shareholder in the chain is affected.

Example 2

Assume that the person A in the Example in **Par.1** is a close company with an issued share capital of 2,000 ordinary shares and that a shareholder B, who buys 100 of its shares in 2004 for €1,500, sells them in 2013 for €3,000 -

		€
Sale price of shares		3,000
Cost of shares	1,500	
Less amount apportioned to 100 shares		
€2,400 (see Example 1) x 100/2,000	<u>120</u>	
Adjusted cost		<u>1,380</u>
Chargeable Gain		1,620

If shareholder B in the second close company is also a close company (C), the amount apportioned to B (€120) must be apportioned similarly to shareholders of C.