Direct Tax Cases: Decisions from the Irish Courts and TAC Determinations

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	Topic	Court
01	**Tax Settlements: *Farrell & Sons (Garages) Limited v Revenue Commissioners* [2024] IEHC 553**	High Court
02	**Corporation Tax and Ireland–US Double Taxation Agreement: *Revenue Commissioners v Susquehanna International Securities Ltd. & Ors* [2024] IEHC 569**	High Court
03	**Offshore Funds Regime: Determinations 104–117TACD2024, 124–127TACD2024, 137–146 TACD2024, 152–159TACD2024**	Tax Appeals Commission
04	**Income Tax: Determination 148TACD2024**	Tax Appeals Commission
05	**Corporation Tax: Determination 59TACD2024**	Tax Appeals Commission
06	**Corporation Tax: Determination 149TACD2024**	Tax Appeals Commission

01 Tax Settlements: Farrell & Sons (Garages) Limited v Revenue Commissioners [2024] IEHC 553

The High Court in *Farrell & Sons (Garages) Limited v Revenue Commissioners* [2024] IEHC 553 considered whether a taxpayer could overturn two tax settlements that it had entered into with Revenue in 1995. The settlements had been entered on foot of a tax audit that had commenced in 1994 and related to payments made through certain bank accounts. The plaintiff argued that it had subsequently (after 2014) discovered that those particular bank accounts had been fraudulently opened by third parties and sought to set aside the tax settlements. The plaintiff grounded its action on various claims of breach of contract, negligence, fraud and duress.

The court, in dismissing the plaintiff's claims, held that:

- the plaintiff's action was statute barred;
- further found that, notwithstanding the statute of limitations, the claim ought to be dismissed as it disclosed no reasonable cause of action, amounts to an abuse of process, is bound to fail or has no reasonable chance of succeeding; and
- criticised the significant delay in taking the action, noting that key witnesses, including a Revenue officer involved in the 1994 audit, were no longer available to testify.

In relation to the "duress" point, the plaintiff had argued that the threat of withdrawal of its tax clearance certificate and the consequences for its business had pressured it into making the settlements. In this regard the court noted three points:

- First, it noted that "the pressure he considers he was placed under was **by his own advisers**. We do not have the benefit of their testimony and can only assume that they gave advice which they believed to be in their client's best interest, recommending the Settlement as being the best outcome he was likely to achieve. They would have been negligent if they had proceeded on any other basis, and I have seen no basis to suggest that they were negligent [emphasis in original]."
- Second, the court emphasised that the communications between the plaintiff and its advisers "were a matter between them alone. Revenue was not party to that professional relationship. The interaction between the Plaintiffs and their advisers could not constitute duress. Even if there was a deficiency with regard to the professional advice – and, in fairness to the advisors, I should note that I have seen no evidence to support such a suggestion – it would not avail the Plaintiffs. Revenue dealt with the Plaintiffs and their advisers in good faith."
- Third, the court accepted Revenue's submission that the granting of tax clearance certificates is governed by statute and that, as the plaintiff had disclosed that it was not compliant, it followed that "the risk to certification arose from the Plaintiffs' own acts and omissions rather than from any Revenue action. Revenue's reference to the certification issue did not constitute duress or undue influence."

02 Corporation Tax and Ireland–US Double Taxation Agreement: Revenue Commissioners v Susquehanna International Securities Ltd. & Ors [2024] IEHC 569

The High Court, in *Revenue Commissioners v Susquehanna International Securities Ltd. & Ors* [2024] IEHC 569, considered the interaction between the group relief provisions (s411 TCA 1997) and the Ireland–USA double taxation agreement (DTA). See also article by Martin Phelan "The Susquehanna Case: A High Court Reversal" in this issue.

The facts of the case are set out in the appealed Tax Appeals Commission (TAC) determination (17TACD2019). In summary, a US (Delaware) incorporated limited liability company (LLC) held shares in a number of Irish companies, including "SL" and "GL". GL purported to surrender losses to SL under the group relief provisions contained in s411 TCA 1997. In essence, that claim was challenged by Revenue on the basis that the group connection between the two companies was traced through the LLC. The taxpayers had been successful before the TAC, and Revenue appealed that determination to the High Court.

The various points of appeal before the court were simplified to the following questions:

- Should the LLC be regarded as resident in the US for the purposes of the DTA and s411 TCA 1997?
- Does the fiscally transparent status of the LLC deprive it of the ability to rely on the anti-discrimination provisions of the DTA?
- Independently of the provisions of the DTA, does the fiscally transparent nature of the LLC mean that the taxpayers are not entitled to group relief under s411?

The court held, in allowing Revenue's appeal, that:

- The LLC could not be regarded as tax resident in the US for the purposes of Article 4 of the DTA because it was not liable to tax in the US by reason of its residence or

place of incorporation (as under US federal tax law it was treated as tax transparent).

- It followed that the anti-discrimination provisions of the DTA were not applicable to the treatment of the LLC. The court further held that those anti-discrimination provisions could not be relied on by the ultimate shareholders of the LLC (in this regard the court quoted *Klaus Vogel on Double Taxation Conventions*: "Article 24 (5) OECD and UN [Model Tax Convention] protects the enterprise against discrimination by the residence State...The shareholders resident in the other Contracting State, however, are not protected by [the Article]. The ownership non-discrimination provision does not prevent a Contracting State from taxing the income accruing to the non-resident shareholders in a different way than income accruing to domestic shareholders... The ownership non-discrimination provision only prevents 'other or more burdensome taxation' at the level of the enterprise, a mere indirect discrimination is not prohibited by Article 24 (5)...").
- As the LLC was not a resident of the US for the purposes of the DTA, the conditions of s411 TCA were not satisfied.

03 Offshore Funds Regime: TAC Determinations 104–117TACD2024, 124–127TACD2024, 137–146 TACD2024, 152–159TACD2024

These grouped Tax Appeals Commission (TAC) determinations on the status of an investment in a fund had been grouped together under the case management provisions. Each of the appellants had been an investor in a fund. They had each treated that investment as being subject to CGT treatment. Revenue had, however, treated the investments as subject to the "offshore funds" regime.

The TAC had previously decided the lead case in the grouped appeals against the taxpayer (42TACD2024). The determination in that lead case recorded that the taxpayer had sought to appeal the determination to the High Court.

These latest determinations record that the taxpayer in that lead case has since decided not to pursue its appeal to the High Court, and so the TAC had written to the other grouped appellants to query whether they wished to proceed to an oral hearing of their own appeals. Most of the determinations record that the appellants did not reply to the TAC's query, and so it proceeded to a determination based on the written submissions that it had previously received from them.

The TAC held, in dismissing each of their appeals (in line with its earlier determination, 42TACD2024), that the investment was an investment in an offshore fund for the purposes of s743 TCA 1997 and that the appellant held a "material interest" (under s743) as the appellant could realise the value of the investment within seven years on the basis that there was a secondary market for the fund investment.

04 Corporation Tax: TAC Determination 118TACD2024

In this matter the appellant was an Irish company that managed intellectual property assets for a global group. It licensed those assets to local operating companies in various jurisdictions and received royalties.

During the relevant years, the appellant received royalties that had been subject to foreign royalty withholding tax (RWHT). The appellant claimed a corporation tax deduction under s81 TCA 1997 for the foreign RWHT, arguing that it was a deductible expense incurred wholly and exclusively for the purposes of its trade. The appellant had been in a loss-making position in the period in question and so was not able to benefit from claiming

a credit for the RWHT against tax under Schedule 24 TCA 1997. In the absence of being able to avail of a credit under Schedule 24, the appellant argued that it ought to be able to claim the RWHT as a deductible expense under s81 TCA 1997.

Revenue denied this deduction, claiming that RWHT is a tax on income and not a deductible trading expense, and the company appealed.

The key questions before the TAC were:

- whether paragraph 7(3) of Schedule 24 precluded the appellant from claiming a deduction for the RWHT under s81; and
- whether the RWHT was incurred wholly and exclusively for the purposes of the appellant's trade.

The TAC held, in allowing the appeal, that:

- The appellant was not in a position to avail of a credit for the RWHT pursuant to Schedule 24 TCA 1997 (as it made no profit to tax). Furthermore, even if the appellant had been in a position to avail of a credit under Schedule 24, it had the right to elect not to allow the credit under paragraph 10. Since no credit was allowed on the facts, it followed that paragraph 7(3) of Schedule 24 did not prohibit the appellant from claiming a deduction for the RWHT if the conditions under s81 could be satisfied.
- The TAC found the RWHT was a cost that the appellant had incurred of doing business in the foreign jurisdiction and there was a direct nexus between that expense and the earning of its royalty income.

Notes:

1. The assessments in question pre-date the introduction of s81(2)(p) by Finance Act 2019, which now prohibits a deduction for "any taxes on income".
2. The determination records that Revenue has sought to appeal the decision to the High Court.
3. The TAC, in determination 119TACD2024, reached a similar conclusion in respect of dividend withholding tax (again, before the Finance Act 2019 introduction of s81(2)(p)).

05 Income Tax: TAC Determination 148TACD2024

The first appellant in this case was a UK-based entrepreneur and sole director/shareholder of the second appellant, an Irish company incorporated in 2020. In 2021 the second appellant (company) made payments totalling €290,468.22 to the first appellant (director/shareholder). Those payments were recorded as a director's loan. No loan agreements were entered into; however, the payments were documented as loans in the second appellant's accounts. Benefit-in-kind (BIK) at 13.5% was also accounted for on payments as if they were preferential loans, and the tax arising on the BIK was paid to Revenue. The loans were subsequently repaid through the payment of dividends.

Revenue recategorised the payments as disguised salary payments and raised alternative assessments against both the first appellant (in the sum of €213,852.44) and the second appellant (in the sum of €296,314.96).

The questions before the TAC were:

- whether the first appellant was an employee of the second appellant;
- whether the payments to the first appellant constituted loans or disguised salary/emoluments under s112 TCA 1997; and
- whether the lack of loan documentation affects the characterisation of the transactions.

The TAC held, in allowing the appeal and setting aside the two alternative assessments, that:

- The payments were intended as loans and were evidenced by accounting records and financial statements.
- The first appellant was (although its sole director) not an employee of the second appellant. The Commissioner reached this determination after applying the first three steps of the Supreme Court's five-step test from *The Revenue Commissioners v Karshan Midlands Ltd T/A Domino's Pizza* [2023] IESC 24. The Commissioner found as a question of fact that: (1) no work-for-wage agreement existed, (2) the first appellant had not agreed to provide services to the second appellant and (3) the first appellant was not under the control of the second appellant. The Commissioner was satisfied that the *Domino's* test was the correct test and rejected Revenue's assertion that the first appellant was an "employee director".
- The preferential nature of the loan triggered a tax charge under s122 TCA 1997 (benefit-in-kind), which liability the appellants had already accounted for and paid.
- In reaching these conclusions the Commissioner also dismissed Revenue's argument that the payments could not be loans because of a breach of the Companies Act 2014 (the loans exceeded 75% of the company's assets yet no summary approval procedure had been conducted). The Commissioner, citing an earlier TAC decision (90TACD2022), held that the payments were loans because "whether or not it was *ultra vires* the powers of the company, was not a relevant consideration, because even if it was *ultra vires*, the director nevertheless incurred a debt to the company".

06 Corporation Tax: TAC Determination 149TACD2024

The appellant, a close company, appealed against Notices of Amended Assessment for corporation tax liability (arising from s440 TCA 1997 close company surcharges) totalling €396,000. The company had filed its corporation tax returns late, and Revenue raised assessments for the close company surcharge, asserting that the s434(3A) TCA 1997 election can be made only in a corporation tax return that has been filed on time.

The key question before the TAC was whether an election under s434(3A) is valid if it is made in a return that has been filed late.

The Commissioner, dismissing the appeal and upholding Revenue's assessments, held that the appellant's failure to file its returns on time invalidated its election under s434(3A). In reaching this decision, the Commissioner held that:

- Section 434(3A) is a relieving provision and, per the principles of statutory interpretation, tax provisions must be interpreted strictly, particularly where they provide relief.
- Section 434(3A)(c) explicitly requires the election to be included in returns made under Chapter 3 of Part 41A TCA 1997, which mandates timely filing.
- The appellant failed to comply with s959I(1) TCA 1997, which requires returns to be filed on or before the "specified return date". As a result, the returns did not comply with the requirements of Chapter 3 of Part 41A, and so the election made in them did not meet the statutory requirements.
- The Commissioner rejected the appellant's argument that s434(3A) lacks a specific time limit, holding that the mandatory language in s434(3A)(c) links the validity of the election to compliance with the broader filing requirements in Chapter 3, which include timeliness.

The TAC determination notes that the taxpayer has sought to appeal the decision to the High Court.