Debt cancellation not taxable in Ireland

Ireland's tax court recently ruled that debt cancellation was not a taxable event in Ireland, even where it resulted in income being brought into account in a taxpayer's income statement. The case involved an Irish company which carried on an active treasury trade. The trade was financed by a USD 264,991,232 parent company loan which was formally repayable on demand, which was ultimately waived by the parent company. This resulted in USD 264,991,232 of income being recognised in the taxpayer's income statement. The Irish tax authorities argued this amount was taxable as a trading receipt because an Irish company generally calculates trading profits following generally accepted accounting practices. The taxpayer argued that the computation of its profits is subject to adjustments required by law. This required adjustments for capital items which did not properly arise from trading activities and required removal of the USD 264,991,232 amount from its tax computation.

Cancellation of debt income

Ireland does not have specific cancellation of debt income rules. There has been some longstanding uncertainty as to the tax treatment of debt cancellation which results in income being brought into account in a taxpayer's income statement. In practice, advisors have historically concluded that such 'income' is not taxable where it is clearly on 'capital' account (the debt having a degree of permanence). This is consistent with the taxpayer's position.

Capital amounts not taxable

The Irish tax court concluded that the cancellation of debt did not generate a taxable trading receipt. The amount taken into account was capital in nature and could not be said to arise from the taxpayer's normal trading activities, which involved earning interest and other income from the lending of money. The court concluded that the capital amount should be deducted from the profits recognised by the taxpayer under generally accepted accounting practices to determine the taxable profits arising solely from its trade.

The key features pointing to capital treatment were:

- the loan was capital used to fund the entirety of the taxpayer's business.
- the loan was permanent, as the parent confirmed it would not seek repayment in practice, even though it was formally repayable on demand.
- the loan represented the largest component of the taxpayer's capital structure and was not temporary or fluctuating in nature.
- the taxpayer was not in a position to repay the loan without a capital injection.
- the waiver amount was fixed, exceptional in nature and not recurring.

Comment

The decision is welcomed and reflects advisors' advice to industry on point. It provides certainty on the tax treatment of restructurings where debt cancellation or forgiveness is required. Further aspects of debt cancellation remain uncertain in Ireland, particularly with respect to income which arises from open market intervention by a taxpayer's treasury teams in its own financial instruments (such as bond buy-backs and subsequent cancellation). Please feel free to contact the authors below if you would like to discuss debt cancellation or reach out to your usual Matheson contact.

Contacts

Kevin Smith
Partner
E: kevin.smith@matheson.com
T: +353 1 232 2045

Aisling Egan
Senior Associate
E: aisling.egan@matheson.com
T: +353 1 232 2394

Finn Kelly
Senior Associate
E: finn.kelly@matheson.com
T: +353 1 232 2596