

Debts

Part 19-01-13

This document should be read in conjunction with section 541 of the Taxes Consolidation Act 1997

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Table of Contents

Executive summary	2
13.1. Gain on disposal of debt by original creditor not chargeable	2
13.2. Bundle of rights	3
13.3. Debt on a security.....	3
13.4. Property acquired in satisfaction of debt	4
13.5. Loss on disposal of debt acquired from connected person.....	5
13.6. Trustees	5
13.7. Issue of certain debentures treated as a security	6

Executive summary

A debt is an asset for capital gains tax purposes (**section 532(a)**). However, where an original creditor disposes of a debt, no chargeable gain or allowable loss arises on the disposal. This treatment also applies where the disposal of the debt is made by the original creditor's personal representative or legatee. It follows, therefore, that only debts which have been purchased from the original creditor (or his/her personal representative or legatee) are regarded as chargeable assets.

The treatment outlined above does not apply to a debt on a security within the meaning of **section 585**. The term "security" as set out in that section includes any loan stock or similar security of any government or of any public authority or of any company, whether secured or unsecured, but excludes securities within **section 607** (for example, Irish Government stocks, loan stocks of Irish local authorities, etc.).

13.1. Gain on disposal of debt by original creditor not chargeable

Section 541(1) provides that no chargeable gain accrues on the satisfaction or the disposal of a debt by the original creditor or his personal representative or his legatee, except in the case of a "debt on a security" (see **Par. 3**).

The satisfaction of a debt in the hands of a person other than the original creditor should, however, be treated as a disposal by the creditor, giving rise either to a chargeable gain or allowable loss.

The exemption extends also to cases in which the original creditor is a trustee and the debt, when created, is settled property, with the substitution for the original creditor or his personal representative or legatee, of any person becoming absolutely entitled as against the trustee to the debt on its ceasing to be settled property, and that person's personal representative or legatee.

Section 44 Finance Act 2013 substituted "the currency of the State" for "Irish currency" in **section 541(1)** and **section 541(6)** as the concept of Irish currency no longer applies following the introduction of the euro on 1 January 1999. (**Section 541(6)** provides that the section will not apply to a debt owed by a bank which is not in euro and which is represented by a sum standing to the credit of a person in an account in the bank unless it represents currency acquired by the holder for the personal expenditure outside the State of the holder or his or her family, dependants or civil partner or any child of his or her civil partner including expenditure on the maintenance of any residence outside the State.)

Section 82 and **Sch 2(1)(z) Finance Act 2017** provides that a successor company will be deemed to be the **original** creditor in respect of a debt in a

case where that debt is transferred as a result of a merger or division under the Companies Act 2014 and the transferor company was the original creditor in respect of that debt.

13.2. Bundle of rights

In the British case of *Cleveleys Investment Trust Co. v. C.I.R.*, 1971, 47 T.C.300, there was an arrangement between that company and another (Falkirk) that a loan should be made by Cleveleys to Falkirk and that on a capital reconstruction of Falkirk there would be an allotment of 51 per cent of the share capital of that company to Cleveleys. Falkirk went into liquidation and the loan was written off. The Court of Session decided by a majority that the arrangement gave rise to a "bundle of rights", i.e. a composite series of rights conferring on Cleveleys incorporeal property (see (a) of Tax and Duty Manual [Part 19-01-01](#) Par 1). It was not possible to segregate the loan element from the other elements and the principle set down in **Par. 1** had no application. The whole of the loss suffered by Cleveleys was allowed (see Tax and Duty Manual [Part 19-01-06](#) Par 1).

Any case where it is argued that there is an arrangement giving rise to a "bundle of rights" and a claim for loss relief is pressed should be dealt with as follows:

- taxpayers and agents, where appropriate, may submit a query using the Revenue Technical Service (RTS) procedure (see Tax and Duty Manual [Part 37-00-00a](#) for further details); and
- Revenue staff should contact Revenue's CGT Unit (part of Business Taxes Policy & Legislation Division) using the RTS procedure (see [Tax and Duty Manual Part 37-00-00a](#) for further details).

13.3. Debt on a security

A "debt on a security" for the purposes of **Section 541(1)** should be regarded as comprising only the securities which are mentioned in **Section 585** (see Tax and Duty Manual [Part 19-04-01](#) Par 4). It does not include secured debts such as a debt secured by -

- (a) a charge on freehold property, or
- (b) the guarantee of a third party, or
- (c) a bill of sale over chattels.

The reference to loan stock in the definition of "security" in **section 585** should be regarded as meaning in general a class of debt the holdings in which are transferable by purchase and sale. The words "whether secured or unsecured" in the definition make the existence of a charge immaterial.

13.4. Property acquired in satisfaction of debt

Where a debt is satisfied by the acquisition of property, the property should not be treated as having been acquired by the creditor or disposed of by the debtor for a consideration greater than its market value at the time (even if the amount of the debt is greater). If the acquisition of the property in satisfaction of the debt is not treated as a disposal of the debt by the creditor (because the creditor is the original creditor) any gain on the subsequent disposal of the property by the creditor should be reduced, so that it does not exceed the gain that would have accrued if the property had been acquired for a consideration equal to the amount of the debt. This maintains the principle that the original creditor cannot make a chargeable gain in respect of the debt.

Example 1

A manufacturer who has been obtaining his raw materials from a company runs into financial difficulties. The debt outstanding to the company stands at €250,000 and in satisfaction of the debt the company accepts a freehold property the market value of which is agreed as €230,000.

The manufacturer is treated as disposing of the freehold property for €230,000 and his chargeable gain is computed by reference to that figure.

The company's acquisition price of the property is €230,000. If the company subsequently sells the property and a computation on the ordinary rules shows a loss, that loss is allowable (as in (a) below). If; however, the company sells the property for an amount greater than €230,000 so that a gain arises, the amount of the chargeable gain is calculated by reference to an acquisition price of €250,000, i.e. the face value of the debt (as in (b) and (c) below) –

	(a)	(b)	(c)
	€	€	€
Sale price	220,000	240,000	260,000
Deemed cost	230,000	230,000	230,000
Allowable loss	10,000		
Gain	-	10,000	30,000
Gain if cost taken as €250,000	-	Nil	10,000
Chargeable gain	-	Nil	10,000
Allowable loss	10,000	Nil	Nil

13.5. Loss on disposal of debt acquired from connected person

Section 541(4) is an anti-avoidance measure providing that when the original creditor or his personal representative or legatee disposes of a debt to a "connected person" (see Tax and Duty Manual [Part 19.02.09](#) Par. 1) either directly or through other connected persons, any loss incurred on disposal of the debt by that connected person is not an allowable loss.

13.6. Trustees

Section 541(5) extends the exemption in subsection (1) and the loss provision in subsection (4) to cover the remainderman where the original creditor is a trustee and the debt is settled property. A disposal by the remainderman (or his personal representative or legatees) on becoming absolutely entitled as against the trustee to the debt on its ceasing to be settled property will therefore not be liable to charge nor can it give rise to an allowable loss.

13.7. Issue of certain debentures treated as a security

Section 541(7) provides that a debenture issued by a company in exchange for shares on a reorganisation of a company's share capital does not constitute a debt for the purposes of **section 541** but is, in fact a debt on a security as defined in **section 585**, which when subsequently disposed of, is chargeable to Capital Gains Tax. The circumstances in which a debenture will be deemed to be a debt on a security are those where the debenture: -

- (a) Is issued on foot of a reorganisation of share capital, i.e. (in an amalgamation, takeover, etc.) as provided for in **section 584(1)**. **Section 584(1)** describes what constitutes a reorganisation of a company's share capital. Basically, it arises where a person, whether for payment or not, is allotted shares in, or debentures of, a company in proportion to their holding of shares in the company. It can also arise where there is more than one class of shares and the rights attached to shares of any class are altered.
- (b) Is issued in exchange for shares in, or debentures of, another company where the requirements of **Section 586** are satisfied in relation to the exchange
- (c) Is issued under any such circumstances as are referred to in **Section 587(2)**.
- (d), (e) & (f) Is issued in the course of a transaction covered by the EU Council Directive on the Common System of Taxation applicable to Mergers, Divisions, transfers of Assets and Exchanges of Shares concerning Companies of Different Member States, which was implemented by **sections 630-638**.

This chapter provides relief for certain transactions covered by the Directive. For example, where a company of a Member State transfers a branch of its business to a company of another Member State and the consideration for the transfer consists of shares or debentures in the receiving company, there is no Capital Gains Tax on the disposal of branch assets and the company acquiring it is treated for capital gains purposes as acquiring it at its original base cost. The company which transfers the branch may receive shares or debentures in the receiving company.

- (g) Is issued in pursuance of rights attached to any debenture falling within paragraphs (a), (b), (c), (d), (e) or (f) above. The purpose of this paragraph is to ensure that the provisions of paragraphs (a), (b) and (c) are not subject to tax avoidance devices whereby a taxpayer could claim not to have received a debenture in exchange for shares on a reorganisation etc. but in fact receives benefits on foot of a debenture issued pursuant to the reorganisation.