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Minister Regina Doherty, T.D.
Department of Employment Affairs and Social Protection
Aras Mhic Dhiarmada
Store Street
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D01 WY03

17 October 2018

Dear Minister

Re: PRSI on deemed income arising on debt release on trading land

We are writing to you regarding the PRSI charge that can arise on the release of a debt, in circumstances where the debt relates to borrowings used for the purchase or development of land.

Following a change to tax legislation[1] in 2013, an anomaly can now arise in cases where there is a release of a debt on borrowings used to fund the purchase or development of land, which was previously held as trading stock. The released debt is deemed a receipt of income in the year the debt is released and as a result, the amount of the debt released is treated as reckonable income for PRSI purposes for that year and subject to income tax and USC.

We understand that this matter was previously raised with the Department in 2016, following discussions at the Tax Administration Liaison Committee (TALC) and in several Pre-Budget submissions at that time. It was hoped that an amendment to the social welfare regulations would be forthcoming. However, this issue remains unaddressed and continues to cause significant hardship to those affected, who incur a substantial PRSI liability, without the corresponding income to discharge the liability due.

The purpose of the 2013 amendment[2] was to ensure that a borrower could only obtain a tax deduction for the economic cost of their borrowings (i.e. a tax deduction for the financial cost incurred, rather than the full amount of the borrowings).

Unused trading losses carried forward from the same activity can be offset against the deemed income created by the debt release for tax purposes. As a result, any income tax and USC

[1] Section 87B TCA 1997
[2] ibid.

liability on the deemed income is in most situations not payable, as demonstrated in the example below. However, as unused trading losses carried forward cannot be used to reduce reckonable income for PRSI purposes, PRSI at 4% arises on the amount of the debt released. This results in a unique situation where an individual crystallises a PRSI liability without realising any income.

The issue is best illustrated by way of an example.

Example:

An individual purchased land in Longford 10 years ago for €600,000 which was financed by bank borrowings. Because of the downturn, the land has been written down to its current market value of €100,000. After lengthy negotiation, the bank agrees that the borrower can sell the land for its market value of €100,000, provided that the proceeds on the sale are paid to the bank. The bank will then release the balance of borrowings due of €500,000.

From an income tax and USC perspective, the borrower will have a trading loss forward of €500,000 (that reflects the diminution in value of the land since it was purchased). This loss can be offset against the deemed trading receipt of €500,000 (the amount of debt released).

As such, no income tax or USC liability will arise. However, a PRSI charge of €20,000 will arise, even though the individual has not received any income from the release of the debt, out of which to pay the PRSI bill.

It is important to consider that the reason why a debt, or part of a debt, is released is because the borrower cannot repay it. Due to a decline in the value of the land held as security, the full amount owing to the financial institution cannot be recouped on a sale. As illustrated by the example above, the individual concerned in such a scenario, does not receive any funds on the release of the debt. In fact, the person will often have to provide additional funds from their own personal resources before the bank will release the debt.

Institute's recommendation

In our view, a specific amendment to social welfare legislation or regulation is required to address this issue, to ensure that income to which Section 87B TCA 1997 applies is not regarded as reckonable income for the purposes of the Social Welfare Consolidation Act 2005.

Your truly

Marie Bradley

Marie Bradley
President