CPA IRELAND | CERTIFIED PUBLIC ACCOUNTANTS

ADVANCED TAXATION

PROFESSIONAL 2 EXAMINATION - APRIL 2016

NOTES:
You are required to answer Question 1 and **any three** from Questions 2,3,4 and 5.
Should you provide answers to all questions, you must draw a clearly distinguishable line through the answer not to be marked. Otherwise, only the first three answers to Questions 2,3,4 and 5 will be marked.

TAX TABLES ARE PROVIDED

NOTE: IF YOU MAKE AN ASSUMPTION IN ANY QUESTION PLEASE STATE THAT ASSUMPTION CLEARLY

Time Allowed
3.5 hours plus **20 minutes** to read the paper.

Examination Format
This is an open book examination. Hard copy material may be consulted during this examination subject to the limitations advised on the Institute's website.

Reading Time
During the reading time you may write notes on the examination paper, but you may not commence writing in your answer booklet.

Marks
Marks for each question are shown. The pass mark required is 50% in total over the whole paper.

Answers
Start your answer to each question on a new page.

You are reminded to pay particular attention to your communication skills, and care must be taken regarding the format and literacy of the solutions. The marking system will take into account the content of your answers and the extent to which answers are supported with relevant legislation, case law or examples, where appropriate.

Answer Booklets
List on the cover of each answer booklet, in the space provided, the number of each question attempted. Additional instructions are shown on the front cover of each answer booklet.

THE INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS IN IRELAND

ADVANCED TAXATION

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Time Allowed: 3.5 hours, plus **20 minutes** to read the paper.
You are required to answer Question 1 and **any three** from Questions 2,3,4 and 5.

Note: You should ignore PRSI and USC in ALL questions.
If you make an assumption in any question, please state that assumption clearly.

Case Study

1. You are a recently qualified Certified Public Accountant working in a small practice in Cork. It is May 2016 and you have recently met Willie and Mary McGee. They have been married for 30 years. Willie is 58 years old and Mary is four years younger. They have one child, Malachy, who is 25 years old. The family have lived in Ireland all their lives. Malachy has recently qualified as an architect and he currently lives near the family farm on the outskirts of Cork City.

Willie has farmed for the last 16 years making a healthy profit each year from his trade. However, due to ill health he has decided that it is time for him and Mary to downsize to a smaller house in Cork City (which they currently own) and for him to retire from farming.

Below is a list of the assets which Willie wishes to transfer to Malachy. It is proposed that the transfer will take place on 1 October 2016 and that Malachy will move into the farmhouse on this date. He will then sell his current home. It is estimated that the trade payables of the farming trade on 1 October 2016 will be €55,000.

Farming Assets	**€**
Farmhouse*	250,000
Farm buildings*	50,000
Farm land*	220,000
Livestock	130,000
Farming machinery	120,000
	770,000

* All these assets were inherited by Willie on the death of his father on 1 January 2000. At the valuation date, the farmhouse was valued at €100,000, the farm buildings were valued at €40,000 and all the farm land was valued at €100,000. Willie and Mary have lived in the farmhouse since 1 October 2005.

Although Malachy has always helped his father with the farm trade, he is devoted to trying to build up his professional experience as an architect. He therefore hopes to continue working as an architecht full time (37 hours per week) and run the farming business in the evenings and weekends. Willie has stated that he does not want any of the assets let after the transfer nor does he want the assets sold to a third party. Recently he was approached by a neighbour, who made an offer to buy a small site from the farm. Willie did not accept the offer.

Malachy's current home on the outskirts of Cork City is worth €250,000. The mortgage attaching to this property is €230,000. Malachy built this house on a one acre site which was gifted to him by his mother in 2014 (market value of site at date of transfer was €100,000). Mary originally bought the site as an investment in 2002 for €50,000. No capital gains tax was paid by Mary on the transfer as a CGT relief was claimed. The only other assets Malachy owns are his car (market value of €10,000) and cash savings in the bank of €8,000.

Malachy received €20,000 on the death of his aunt in 2009. Each year, on his birthday (1 May), Mary and Willie gift him €1,000 each.

REQUIREMENT:

Draft a report to the Willie and Mary McGee providing appropriate advice on the following:

(a) The tax implications for Willie of transferring the assets to Malachy in September 2016. (12 marks)

(b) Malachy's capital acquisitions tax liability if agricultural relief is claimed. You should provide advice in respect of the conditions that need to be satisfied for agricultural relief and apply these to Malachy's specific circumstances. (10 marks)

(c) The capital acquisitions tax implications for Malachy if agricultural relief is not available. Your answer should cover any other capital acquisitions tax reliefs available. (10 marks)

(d) The stamp duty implications of the transfers for Malachy. (3 marks)

(e) The tax implications for Malachy of selling his current home. (3 marks)

Format and Presentation (2 marks)

[Total: 40 marks]

2. It is 1 May 2016 and you are Evelyn Friel, a recently qualified Certified Public Accountant. Your manager, Gabrielle, calls you into her office and says the following:

"As you have worked on the Ag Sugradh Ltd (ASL) case with me over the last few years, I think you are best placed to help me deal with an urgent query from two of the company's shareholders, Andrew and Sean Duncan. I met with them yesterday and they informed me that they are having major disagreements with Maria Finnegan, the company's marketing director.

As you are aware, ASL is a trading company which designs and manufactures bespoke outdoor children's play areas. ASL has been a very profitable company since it was incorporated in 2004 by its three shareholders: Andrew Duncan; Sean Duncan and Maria Finnegan. Andrew and Sean are brothers aged 55 and 51 respectively. Maria is a friend of Andrew since they shared a house at University together. Maria will turn 55 on 1 September 2016.

As Maria has a marketing degree, she was invited by Andrew to get involved in ASL when it was incorporated. She invested in ASL at the outset and has since been employed as the company's Marketing Director. Maria is adamant that ASL needs to target the American market in order to continue its profitable run. Andrew and Sean believe that this would be a wrong strategic move for the company. As they cannot agree on the way forward for ASL, Maria has decided to leave the company. She has offered Andrew and Sean the opportunity to buy her shares for €400,000.

When I met with Andrew and Sean yesterday, they told me that they had approached their local bank manager to organise a €400,000 personal loan which will be repayable over 10 years."

After you leave Gabrielle's room you look at ASL's file, you see that an extract of the statement of financial position has been prepared in draft format (See below for a copy).

Ag Sugradh Ltd
Extracts from draft Statement of Financial Position as at 31 March 2016

	Note	€	€
ASSETS			
Non-Current Assets	1		200,000
Current Assets			690,000
Total Assets			**890,000**
EQUITY & LIABILITIES			
Equity			
Ordinary share capital	2	50,000	
Retained earnings		400,000	
			450,000
Non-Current Liabilities			301,000
Current liabilities			139,000
Total Equity & Liabilities			**890,000**

Notes:
1. All trading assets.

2. 100 shares with a nominal value of €1 each. The shares are held as follows:

Andrew Duncan	35%
Sean Duncan	25%
Maria Finnegan	40%

REQUIREMENT:

Gabrielle has asked that you prepare a briefing memo for her meeting with Andrew and Sean tomorrow morning. Your memo should include the following:

(a) An appraisal of the tax consequences for Maria, Andrew and Sean of structuring Maria's exit by Andrew and Sean taking out a personal loan to buy her shares within the next week.

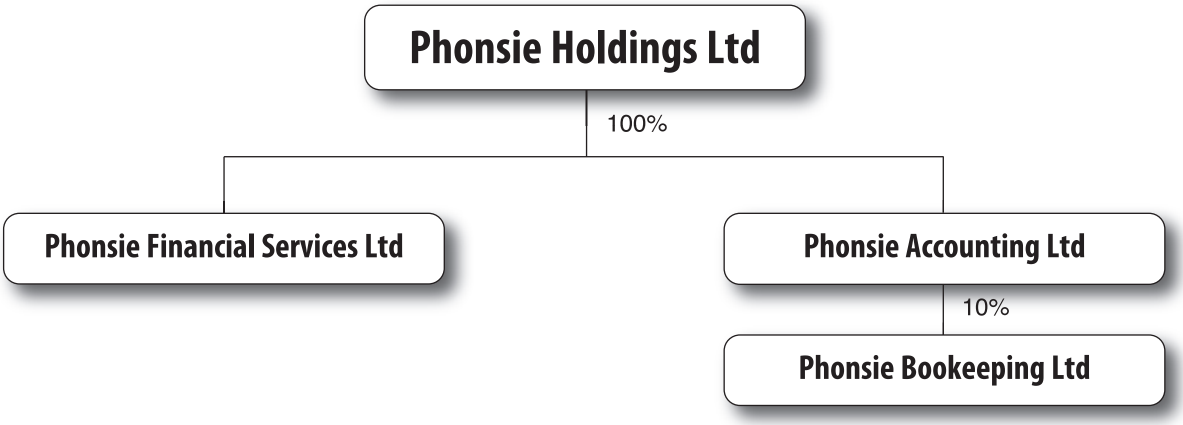
(7 marks)

(b) Advice for Maria, Andrew and Sean regarding a more tax efficient way by which Maria could obtain the money for her shares and exit the company. Details of the timing of any tax planning and also the conditions for any reliefs should be provided.

(13 marks)

[Total: 20 marks]

3. The Phonsie Consulting group is owned 100% by Alphonsus Harris. The group structure as at 31 March 2016 is shown below:



All companies are Irish incorporated and tax resident. Phonsie Holdings is purely a holding company for the group. Phonsie Financial Services Ltd (PFSL) offers investment and pension advice. Its activities are VAT exempt. Phonsie Accounting Ltd (PAL) and Phonsie Bookkeeping Ltd (PBL) are both VAT registered. PAL owns a 10% shareholding in PBL. All companies have employees. However, on a monthly basis PAL invoices PFSL for tax advice services that are provided by PAL employees for PFSL customers. The invoice raised is usually in the region of €7,000 plus VAT per month.

Alphonsus Harris is also a 10% shareholder in Phonsie Property Ltd (PPL), a property development company (his brother Frank Phonsie owns the other 90%). PPL has recently advertised for sale a property it owns near Dublin airport. The property comprises one commercial unit and six first floor apartments. The property is advertised for sale at €1,200,000 plus VAT (if applicable). The history of the property is outlined below:

- PPL acquired a site near Dublin airport in January 2008 for €1,000,000 plus VAT. PPL reclaimed all VAT incurred on this acquisition as it intended to develop the site.
- PPL then undertook the construction of a commercial unit with six first floor apartments on the site. This work was complete in October 2010 at a cost of €600,000 plus VAT at 13.5%. Again, all VAT was recovered on the costs associated with the construction.
- The location of the commercial unit has always proved desirable due to its close proximity to Dublin Airport and as a result it has been let on a regular basis since 1 December 2010. PPL carried out an extension to the commercial unit in February 2012 at a cost of €60,000 plus VAT.
- Each of the six apartments have been advertised for sale since October 2010 but there has been little or no interest in them. The apartments have never been let out. It is hoped that by offering the apartments for sale with the commercial unit, as one lot, that this will help entice prospective buyers.

PBL has been trading profitably in the Republic of Ireland (R.O.I) for many years but the company is always looking to expand its client base. The Finance Director has recently identified, outside the R.O.I., an opening for the company to provide its services in Omagh, Northern Ireland. The company has looked at a number of commercial rental properties and is due to sign a five year lease for a commercial unit in Omagh town centre next week.

REQUIREMENT:

(a) Alphonsus Harris has been told by his Finance Director that all companies in which he has a shareholding should be in a VAT group. John would like you to explain the criteria for Irish VAT grouping and confirm which companies in the group could form a VAT group.

(3 marks)

(b) What would be the implications of forming a VAT group? What particular advantage is associated with Phonsie Financial Services Ltd and Phonsie Accounting Ltd operating in the same VAT group?

(3 marks)

(c) Advise on the VAT treatment of the sale of the commercial unit and six apartments by Phonsie Property Ltd, assuming that the sale will happen on 31 July 2016.

(8 marks)

(d) Advise on the tax implications of Phonsie Bookkeeping Ltd renting and operating from an office in Omagh, Northern Ireland.

(6 marks)

[Total: 20 marks]

4. Having successfully completed your Certified Public Accountants final admitting exams you have been transferred to the tax department of a medium sized accountancy practice in Tipperary. It is a Monday morning and you have a meeting at 11.00am with Colm Doherty, a prospective new client looking for tax advice. At the meeting, Colm provides you with the following details about his personal background and his business:

- He is 50 years old and is an engineer who has worked as an employee for a large scale water treatment company for many years. He is the general manager of the Dublin/Kildare division. His gross salary is €70,000 plus benefits.
- In 2013, Colm also started his own business, WATER EYE. Due to his engineering background and the experience he has gained from his employment, he has created a warning device for the water treatment industry. Up until the 2015 tax year, the business has been making losses. Colm has been offsetting these losses against his employment income and generating a tax refund each year. However, it looks like a major contract may be signed soon and if it is secured, the level of his self-employed income will spike dramatically. Projected profits are in excess of €250,000 for 2016, if this contract is signed.
- The latest statement of financial position as at 31 December 2015 shows the business to have net assets of €285,000. Just last week, one of the business' main customers offered Colm €500,000 for the business. He was pleasantly surprised by this offer. However, Colm declined the offer as he wants to grow the business further himself.

Statement of Financial Position as at 31 December 2015

	Notes	**€**	**€**
NON-CURRENT ASSETS			
Premises	1	200,000	
Plant & equipment	2	45,000	
			245,000
CURRENT ASSETS			
Inventories		25,000	
Trade receivables		15,000	
Cash at bank		45,000	
			85,000
Total assets			**330,000**
OWNER'S CAPITAL			
Closing capital			285,000
CURRENT LIABILITIES			
Trade payables			45,000
Total owner's capital & liabilities			**330,000**

Notes in respect of non-current assets:

1. The market value of the premises is €300,000. The building originally cost €250,000 in 2015.
2. The plant and equipment is valued at its net book value. This equates to the tax written down value and to the market value of the plant & equipment.

- Colm is concerned about the levels of income tax that he is going to pay and would like some advice on how to avoid paying more income tax at the top rates. He does not necessarily require any more income to fund his standard of living and would like to reinvest any profits in the business in the next few years.

REQUIREMENT:

Prepare a briefing memo for the next meeting with Colm which should include the following:

(a) Details of the tax consequences of Colm incorporating his trade and transferring all assets and liabilities of his sole trade business for shares in a new company, Water Eye Ltd. You should refer to the income tax, capital gains tax, stamp duty and VAT consequences of such a transfer.

(14 marks)

(b) Details of the capital gains tax consequences of Colm incorporating his trade and transferring all assets and liabilities in return for shares in a new company plus cash of €150,000.

(3 marks)

(c) Details of the capital gains tax and income tax consequences of Colm incorporating his trade but not transferring the building to the company and instead renting the building to Water Eye Ltd.

(3 marks)

[Total: 20 Marks]

5. It is May 2016 and you work for a small accountancy practice in Dublin. You have been asked to meet the daughter (Michaela) of a long standing client of the practice. Michaela is the only child of Tony and Mary Duncan. Tony is a retired company director who owns an extensive property rental portfolio in Ireland and in the UK. Tony and Mary have lived in Ireland all their lives. Michaela lived with them in Ireland before moving to London to study French at University. She remained in London after her graduation for approximately ten years where she was employed as a translator for a large multinational company headquartered in London.

Michaela moved back to Ireland on 2 January 2014 but continued to work in London three days per week. She travels back and forth to London by plane on a weekly basis, to carry out her employment duties there. She had no holidays outside Ireland in 2014 as she was tired of flying as a result of her weekly commute. When Michaela is in London she stays in a hotel as she no longer rents one of her father's London apartments. Since she returned to Ireland, she lives in a house which she bought while she was living and working in London. Having her own home in Dublin has meant that she is able to carry out some private French tuition. Her customers come to her house on the evenings she is in Ireland. Michaela earned approximately €8,000 in 2014 and €12,000 in 2015 from giving private French tuition to Leaving Certificate students. She continues to offer these services in Ireland in 2016.

Since returning to Ireland, Michaela has not registered for tax in Ireland and so she has not returned details of any income to Irish Revenue. She says that her father is going to gift her a house in Dublin and she does not want to have to pay any tax on this transfer in Ireland. A friend of Michaela's has advised her that she remains UK tax resident based on the number of days she works in the UK. Her friend also told her that if she remains UK resident she will not have to pay any taxes in Ireland on the gift of the house from her father. Michaela knows that her father will not have any taxes to pay on the transfer of this property to her, as the property's current value (€500,000) is less than what it cost him to buy in 2008. This is the first gift that Michaela has ever received from either of her parents.

REQUIREMENT:

Prepare appropriate advice for Michaela:

(a) On her tax residency position since 2014. Your answer should refer to how you would use the relevant provisions of the Ireland/UK tax treaty to decide where she is ultimately resident if both Ireland and the UK deem her to be resident under their respective domestic legislation.

(6 marks)

(b) About her income tax obligations in Ireland in respect of her income earned since 2014. (4 marks)

(c) As to whether the gift of the house in Dublin, from her father, will have any tax implications for her in 2016.

(4 marks)

(d) On how best she can mitigate any potential penalties she may face in Ireland as a result of not registering for taxes.

(6 marks)

[Total: 20 marks]

END OF PAPER

SUGGESTED SOLUTIONS

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SOLUTION 1

STRICTLY PRIVATE AND CONFIDENTIAL

Tax Report for the McGee family

The following report contains tax advice in respect of:

Section A Tax implications for Willie of transferring assets to Malachy

Section B Agricultural relief for Malachy

Section C Other CAT reliefs available to Malachy if agricultural relief not available

Section D Stamp duty implications of transfers

Section E Advice regarding the tax implications of Malachy moving out of his current home

Presentation (2 Marks)

Section A The tax implications for Willie of transferring the assets to Malachy in September 2016.

Transfer of farmhouse
A gain on the disposal by an individual of a dwelling-house (including grounds of up to one acre) is exempt in certain circumstances. The exemption is available if, throughout the individual's period of ownership, the house had been occupied by the individual as his/her only or main residence.

It is understood that Willie and Mary have lived in the farmhouse as their main residence since 1 October 2005 and that the farmhouse was owned by Willie since 1 January 2000. Therefore, CGT of €16,993 will arise on the transfer to Malachy. See Appendix 1 for principle private residence relief and CGT calculations.

(5 Marks)

Transfer of farming assets
For CGT purposes, Willie will be treated as disposing of his farm business for €390,000 (€50,000 + €220,000 + €120,000). This is because S547 TCA 1997 states that where a person acquires an asset from a connected party or not for a bargain at arm's length, then market value must be substituted in place of consideration given.

Section 599 TCA 1997 provides for retirement relief from CGT on the disposal or transfer of qualifying business assets to a child of the disponer, such as Malachy, without any limit on the value of assets transferring where the disponer is aged less than 66. Where the disponer is aged 66 or over, an upper limit of €3,000,000 is imposed. As Willie is less than 66, no limit applies.

For retirement relief to apply, the disposal must be of qualifying assets, which are owned by the disponer for the qualifying period of 10 years.

Qualifying assets comprise actual assets used in a trade including:

- Land & buildings owned for at least 10 years and used for the purposes of the trade continuously throughout the 10 year period.
- Plant & machinery used for the purposes of the trade. Plant & machinery do not have to be owned for a 10 year period prior to disposal as they very rarely have a useful life up to 10 years. As plant & machinery are wasting assets, it is very rare for a capital gain to arise on their disposal.

Assets such as trade receivables or inventory are not chargeable business assets as they do not give rise to a chargeable gain on disposal.

As Willie has reached 55 years, has held the farm buildings and land for in excess of 10 years, RR should be available on their transfer.

The total deemed proceeds in respect of qualifying assets are:

	€
Farm buildings	50,000
Farm land	220,000
Farming machinery	120,000
	390,000

As a result of RR, no CGT liability should arise for Willie. (7 Marks)

(12 Marks)

Section B Advice in respect of the availability of agricultural relief for Malachy

If we assume that agricultural relief (AR) is available, then Malachy's CAT liability would be nil. See appendix 3 for calculations.

(2 Marks)

As you can see from the AR calculations in Appendix 3, AR will amount to a reduction of 90% in respect of the value attributable to relevant business property taken by the beneficiary, Malachy.

However, AR can only apply where the beneficiary qualifies as a 'farmer'. Therefore, Malachy must be a farmer as defined for AR to apply. Malachy will only qualify as a farmer if on the date of the gift his agricultural property comprises 80% of his total property after taking the gift. As you can see from Appendix 2, 95% of Malachy's assets after the gift will be agricultural assets. Therefore, Malachy passes the farmer test for AR.

(3 Marks)

From 1 January 2015, an additional test, the "active farmer" test, must be fulfilled for AR to apply. This test requires that the recipient must either:

1. hold a qualification in farm management (or attain such qualification within four years of the gift/inheritance) and farm the land with a "view to the realisation of commercial profit" for a period of at least six years from the valuation date, and
2. for at least six years from the valuation date, spend at least 50% of their "normal working time" farming the agricultural property on a commercial basis; or
3. lease the whole, or substantially all, of the agricultural property for a period of at least six years to an individual who will qualify under 1 or 2.

Revenue have provided guidance on "normal working time" (including on-farm and off-farm working time). They consider this to equate to approximately 40 hours per week.

Therefore, Malachy would need to spend a minimum of 20 hours working per week, averaged over a year, on the farm. It is unlikely that Malachy will be able to do this is he continues to pursue his architectural career. As an alternative, Malachy could obtain a qualification in farm management in the next 4 years. If he did this, then he would be able to pass the active farmer test.

The option of leasing the farm to an "active farmer" has not been explored due to Willie's stipulation that the land will not be leased out after the transfer.

A 6 year clawback period exists for AR. If development land, which has qualified for AR, is disposed of in the period commencing 6 years after the date of the gift and ending 10 years after that date, the AR granted will be clawed back in relation to the development value of the land at the original date of the gift or inheritance.

Therefore, in summary, if Malachy wants to continue working full time as an architect, he will need to obtain a farm management qualification within 4 years of 1 October 2016, if he wishes to avail of AR. He will also have to farm the land with a view to the realisation of a commercial profit.

The clawback provisions for AR will be a deterrent from selling off any sites of the farm post claiming AR for up to 10 years.

(5 Marks)

(10 Marks)

Section C Other CAT reliefs available to Malachy if agricultural relief not available.

Business Relief (BR) will amount to a reduction of 90% in respect of the value attributable to relevant business property taken by the beneficiary, Malachy. Only relevant business property will qualify for the relief. “Relevant business property” includes an interest in a business carried on by a sole trader. Willie has been carrying on his farming sole trade for the last 16 years.

Willie is going to gift his farming business to Malachy and not just individual assets. The farmhouse cannot qualify for BR.

To qualify for BR the relevant business property must have been owned for a continuous period of 5 years prior to the date of the gift by Willie. This condition is fulfilled as Willie inherited the farm in 2000.

(2 Marks)

In respect of a sole trade business, such as Willie’s farming trade, the value of the business for the purposes of BR is the net value. The net value is arrived at by reducing the market value of the assets used in the business by the market value of any liabilities incurred for the purposes of the business. See Appendix 4 for details of the assets qualifying for BR and those that do not qualify.

(2 Marks)

Appendix 5 shows Malachy’s CAT liability where business relief and the same event credit relief are claimed. Malachy was previously gifted a site from his mother with a market value of €100,000. He therefore has only €125,000 of his Group A threshold remaining. €1,000 of his annual CAT exemption is also utilised by the regular gifts from his mother on a yearly basis. The previous inheritance from his aunt is irrelevant for the Group A threshold.

As you can see, the CAT liability amounts to €37,279 after these reliefs are claimed.

(4 Marks)

There is a 2 year holding requirement where the CGT/CAT same event credit is claimed. This relief effectively gives Malachy some CAT relief for the CGT paid by Willie on the transfers.

BR clawback provisions also need to be considered. BR will be clawed back if:

1. The farm business, or any business which replaced it, ceases to trade within a period of 6 years after the date of the gift unless the business is replaced within 1 year by other relevant business property.
2. The land which qualified for business relief is disposed of in whole or in part, by Malachy, in the period commencing 6 years after the date of the gift and ending 10 years after that date, the relief granted will be clawed back in respect of the development value of that land at the date of the gift. If only part of the relevant business property ceases to qualify for the relief the claw back will relate only to that part.

Therefore, it is very important that Malachy continues to carry on the farming trade himself for the next 6 years. The BR will be clawed back if Malachy rents out the farm to another farmer, for example.

(2 Marks)

(10 Marks)

Section D Stamp duty position for Malachy

Stamp duty of 1% of the market value of farmhouse and 2% in respect of the farm buildings and land will arise for Malachy.

The livestock and plant & machinery can transfer by delivery and therefore no stamp duty should arise.

Total stamp duty will be €7,900 (i.e. €250,000 x 1% + €270,000 x 2%) and is due within 30 days of the transfer by way of an e-stamping return to Revenue. By concession, Revenue allow an additional 14 days to pay when a return is filed within 30 days. The amount of stamp duty paid can be deducted for CAT purposes when applying the reliefs.

(2 Marks)

It is worth noting that consanguinity relief may be available on the farm land and buildings between relations (including father to son) where the disponer has not reached the age of 67 (this is satisfied as Willie is 58).

Other conditions must be satisfied for the rate of stamp duty to be reduced to 1%:

1. The individual to whom the land is transferred/conveyed must either:

   a) farm the land for a period of not less than six years, or else
   b) lease it for a period of not less than six years to someone who farms the land.

2. The person farming the land must do so on a commercial basis and with a view to the realisation of profits. The person must also spend not less than 50% of their normal working time farming land, including the land transferred, or be the holder of one of the agricultural qualification.

(1 Mark)

(3 Marks)

Section E CGT position on previous site transfer to Malachy

Under s603A TCA 1997, a CGT relief exists where a parent transfers a site to a child to enable that child to build a principal private residence. As Mary paid no capital gains tax at the time of the transfer, this relief must have been claimed. The conditions of the relief include:

1. The value of the land must not exceed €500,000;
2. The size of the site must not exceed 1 acre, exclusive of the area on which the house is to be built and
3. The purpose for which the land is transferred to the child must be to enable the child to construct a dwelling on the land which will be occupied by the child as their principal private residence.

(1 Mark)

The legislation provides that a clawback of the relief will occur where the child does not construct a residence on the land and occupy it as their principal private residence for a period of 3 years. This clawback will impact Malachy if he moves from his home in Cork to take up residence in the farmhouse on 1 October 2016 as he will not have lived in the house in Cork for 3 years as his principal private residence.

(1 Mark)

If relief under s603A is withdrawn as Malachy is going to sell the property within 3 years of his commencement of occupation of the house then the clawback provisions will apply. As a result, the capital gain which would have been charged on his mother on the original transfer of the site to him in 2014 will be deemed to accrue to Malachy at the time of the disposal of his house. Therefore there exists a CGT exposure of €16,500 (€100,000-€50,000=€50,000 x 33%=€16,500). [Ignoring annual exemption and indexation]

(1 Mark)

(3 Marks)

Appendix 1
CGT on Farm House

Inherited 1 January 2000
Moved in 1 October 2005
Disposed of 1 October 2015

	Months	
Total period of ownership	201	
Number of months house was PPR	132	
	€	
Deemed disposal proceeds (MV)	250,000	
Less cost (ignoring indexation)	(100,000)	
Capital gain	150,000	
Less PPR relief	(98,507)	150,000 x 132/201
Gain left chargeable	51,493	
No annual exemption if retirement relief claimed	0	
CGT	**16,993**	

Appendix 2

Farmer Test for Agricultural Relief

	Total value €	Agricultural assets €	Non-agricultural assets €
Farmhouse	250,000	250,000	
Farm buildings	50,000	50,000	
Farm land	220,000	220,000	
Livestock	130,000	130,000	
Farming machinery	120,000	120,000	
Malachy's own house	20,000		20,000
Car	10,000		10,000
Cash at bank	8,000		8,000
	808,000	770,000	38,000

Appendix 3

CAT liability where AR claimed

	€
Market value of assets transferring	770,000
Less AR	(693,000)
Agricultural value	77,000
Less €2k of SGE remaining	(2,000)
Less group A threshold remaining (225k-98k)	(127,000)
Amount subject of CAT	Nil

Appendix 4

	Qualifying property €	Non-qualifying property €
Farmhouse		250,000
Farm buildings	50,000	
Farm land	220,000	
Livestock	130,000	
Farming machinery	120,000	
Less trade payables	(55,000)	
Taxable value before BR	465,000	250,000
Less BR	(418,500)	0
Taxable value	46,500	250,000

Appendix 5

CAT liability were BR claimed

	€	€
Property not qualifying for BR	250,000	
Less stamp duty payable	(2,500)	
		247,500
Property qualifying for BR	46,500	
Less stamp duty payable	(540)	
		45,960
Less group A threshold remaining (225k-98k)		(127,000)
Less €2k of SGE remaining		(2,000)
		164,460
CAT at 33%		54,272
Less CGT/CAT offset		(16,993)
CAT liability		37,279

SOLUTION 2

MEMO
TO: Gabrielle
FROM: CPA
RE: Ag Sugradh Ltd – Maria Finnegan exit

Andrew & Sean buy Maria's shares immediately

Maria will be subject to capital gains tax (CGT). If the sale happens before her 55th birthday, she will not be entitled to retirement relief.

(1 Mark)

Her CGT computation is as follows:

	€	
Disposal proceeds	400,000	
Less cost		
€50,000 x 40%	(20,000)	
Gain	380,000	
Less annual exemption	(1,270)	
Gain subject to CGT	378,730	
CGT liability	124,981	(2 Marks)

Andrew and Sean will have to pay stamp duty on the acquisition of the shares of €4,000 (€400,000 x 1%).

(2 Marks)

The biggest issue for Andrew and Sean is that that they are going to have to service the repayments on the €400,000 borrowings from their after tax income.

Tax relief for money borrowed to invest in shares in a trading company (S248 TCA 1997) has been phased out. Assuming Andrew and Sean are top rate taxpayers, they will need to extract the finds via dividend or salary from ASL which may be subject to a marginal rate of tax as high as 52% (40% income tax + 8% USC + 4% PRSI).

(2 Marks)

(7 Marks)

Share buyback by ASL

The possibility of structuring Maria's exit from ASL as a share buyback by ASL should be explored. This option would mean that Andrew and Sean do not need to borrow €400,000 in their own names and then have the personal difficulty of repaying the loan from after-tax funds.

(1 Mark)

The main share buyback conditions are as follows:

- ASL must be a trading company;
- The trade benefit condition – the share buyback must be made wholly or mainly for the benefit of the trade. As there has been a disagreement between the shareholders the Revenue are likely to accept that the redemption is for the benefit of the trade;
- Maria Finnegan is resident and ordinary resident in Ireland and she will be when the share buyback takes place;
- The share buyback will result in a substantial reduction in Maria's interest in ASL. This condition is satisfied as Maria will own no shares in ASL after the buyback.
- Maria will not be connected with the company after the share buyback.

(2 Marks)

As all of the above conditions are satisfied, Maria will be subject to CGT on the share buyback (not income tax).

(1 Mark)

Per the statement of financial position, ASL has sufficient distributable reserves to enable the share buyback.

(1 Mark)

Stamp duty of €4,000 will also be saved by opting for the share buyback option.

(1 Mark)

If the share buyback is postponed until after Maria turns 55 (i.e. 1 September 2016) she should be entitled to retirement relief. Retirement relief provides for a complete exemption or a reduction in CGT payable (due to marginal relief) on the disposal of certain qualifying assets.

A number of conditions must be satisfied in order for retirement relief to apply,

1. The claimant (Maria) must be an individual

2. She must be at least 55 years of age at the date of disposal – hence the need to wait until Maria is 55 on 1 September 2016.

3. The relief is available in respect of "qualifying assets". Shares in a family company fall within the definition of qualifying assets. The company must be trading and the shares must have been owned by the individual for at least 10 years ending with the disposal and in which the individual has been a working director for at least ten years and a full-time working director for at least five of those years. These conditions are all satisfied.

(2 Marks)

As all assets on the statement of financial position are trading assets, full retirement relief should be available. Maria CGT computation under this scenario is detailed below.

CGT computation	€
Proceeds	400,000
Cost	(20,000)
Chargeable gain	380,000
Retirement relief	(380,000)
Net gain	0

A tax saving of €124,981 can therefore be achieved by simply waiting until 1 September 2016 to undertake the buyback.

(4 Marks)

(13 Marks)

SOLUTION 3

(a) Revenue will generally allow a VAT group where the following conditions are met:

- There are two or more persons/companies established in the Republic of Ireland and at least one of them is a taxable person
- The businesses/companies are closely bound by financial, economic and organisational links
- The group is necessary or appropriate for the efficient administration of VAT

(2 Marks)

Revenue should allow Phonsie Holdings Ltd, Phonsie Financial Services Ltd (PFSL) and Phonsie Accounting Ltd (PAL) to form a VAT group. PFSL is allowed to join the VAT group despite having VAT exempt activities. Revenue may not allow Phonsie Book-keeping (PBL) or Phonsie Property Ltd (PPL) to join the group due to the 10% shareholding relationship – a 10% shareholding may not be sufficient to show organisational links. The granting of a VAT group registration is at the discretion of Revenue.

(1 Mark)

(3 Marks)

(b) The implications of forming the VAT group include the following:

1. No VAT would arise on transactions between members in the VAT group (except for certain property transactions)

2. All companies would continue to issue VAT invoices using their individual VAT numbers

3. Only one VAT return would be filed of the entire group member

(1 Mark)

As PAL and PFSL are not currently in a VAT group, PAL is charging VAT of €1,610 (€7,000 x 23%) each month to PFSL however, PFSL cannot reclaim this VAT as they are VAT exempt. However, if both companies are in the same VAT group, there would be no need to a VAT invoice to be raised. This would result in a substantial saving for PFSL of approximately €19,320 per year (€1,610 x 12).

(2 Marks)

(3 Marks)

(c) The property was complete in October 2010 and the sale on 31 July 2016 will be the first sale of the property since its completion. For the purposes of advising on the VAT implications on the sale of the whole property, we firstly need to look at the VAT implications on the sale of the commercial unit and the apartments separately.

(1 Mark)

Commercial unit sale

The five year rule is relevant for establishing if the property is to be considered 'new' for VAT.

(1 Mark)

Over five years have lapsed since the property's completion and therefore the property would not be considered new. However, the development work carried out to the commercial unit in February 2016 needs to be considered. If this development can be considered 'minor development' then it will not make the property new again for VAT purposes. It is assumed that the development cost of the commercial unit is less than 25% of the sale price of the commercial unit (i.e. the sale price associated with the unit is greater than €240,000). Therefore, the development is minor and therefore does not make the property new for VAT.

(2 Marks)

In respect of the sale of the commercial unit, as it is now an 'old' property, the sale will be exempt from VAT. However, the property remains within its capital goods scheme life. Therefore, to ensure that HPL does not suffer a clawback of VAT reclaimed on the site purchase and construction of the commercial unit, HPL should seek agreement from any purchaser to exercise the joint option to tax the sale. If this joint option to tax is exercised, HPL will not suffer any clawback on the sale of the commercial unit and the purchaser will self-account for 13.5% VAT on the sale.

(2 Marks)

Six apartments
As the apartments are residential, VAT must always be charged on the sale where they are sold by the developer (i.e. HPL).

Therefore, VAT at 13.5% must be charged on the sale of the apartments. The purchaser will pay across the VAT on the sales proceeds relating to the apartments and HPL will then pay this VAT to Revenue with their VAT return that covers the period of the sale.

(2 Marks)

(8 Marks)

(d) By renting an office in Omagh, PBL will be creating a permanent establishment (PE) in Northern Ireland. A UK branch of PBL will be established.

(1 Mark)

As a PE is established in Northern Ireland, as defined under the UK/Ireland double taxation agreement, the UK will have primary taxing rights on any profits attributable to the PE. However, Ireland will also look to tax the branch profits as it is merely an extension of the Irish company's trade.

Separate books and records will be required for the UK branch to enable the preparation of a statement of profit or loss which will be used to prepare the UK tax return.

(2 Marks)

The UK branch profits will be taxed in the UK at the UK corporation tax rate. A credit will be provided in Ireland (up to a maximum of the Irish effective rate of tax on the branch profits – 12.5%).

(1 Mark)

Where the UK branch is profitable, the incorporation of a UK company (as opposed to operating as a branch) should be considered. Irish tax will only then be considered when dividends are paid from the UK company.

(2 Marks)

(6 Marks)

SOLUTION 4

MEMO
TO: Colm Doherty
FROM: CPA
RE: WATER EYE

(a) Tax consequences of Colm incorporating his trade and transferring all assets and liabilities of his sole trade business for shares in a new company

Income tax consequences
The transfer of the WATER EYE trade to Water Eye Ltd will mean a cessation of the sole trade for Colm. Where the sole trade ceases in 2016, Colm will be subject to the cessation rules in 2016. The taxable profits of the year prior to the year of cessation may be revised to an actual basis if those are higher than previously assessed. Terminal loss relief will not be an issue based on the expected results for 2016. Ideally, the sole trade should be incorporated before the new contract is signed and the increased revenue is generated. However, generally speaking, it is best to time the incorporation of a business for January, the 1st month in the tax year, where profits are increasing. A January cessation date should minimise any extra income tax due as a result of the penultimate year review rules on cessation.

No balancing allowances or charges should arise on the incorporation as the TWDV is similar to the market value of the plant and machinery transferring.

(3 Marks)

CGT consequences
The transfer of the chargeable assets, including the property, goodwill and plant & machinery of the sole trade business, WATER EYE, to a new company, Water Eye Ltd, may give rise to a CGT liability for Colm.

Market value will have to be imposed for the purposes of CGT as Colm and Water Eye Ltd are connected (s547 & 549 TCA 1997).

No CGT should arise in respect of the transfer of the trade receivables or cash to Water Eye Ltd. No CGT should arise on the transfer of the plant & machinery as their net book value (which is lower than cost) is equal to their market value.

Therefore, the potential CGT exposure is on the premises and the goodwill inherent in the business is calculated below:

CGT calculation on incorporation

		Market value	Base cost	Gain
		€	€	€
Premises		300,000	250,000	50,000
Goodwill	(Note1)	160,000	0	160,000
				210,000
Less annual exemption				(1,270)
				208,730
CGT at 33%				68,881

Note 1

The total value transferring to Water Eye Ltd is:

	MV of assets transferring
	€
Premises	300,000
Property, plant & equipment	45,000
Inventories	25,000
Trade receivables	15,000
Goodwill	160,000
Less trade payables	(45,000)
Total assets and liabilities	500,000

Retirement relief is not available to Colm as he is not 55 years old.

However, incorporation relief (s600 TCA 1997) may be an option. This relief allows the CGT arising on the disposal of business assets to a new company to be deferred. Incorporation relief is available provided that the business and all its assets other than cash are transferred as a going concern in consideration for the issue of shares in Water Eye Ltd to Colm. The deferred CGT will crystallise when Colm eventually disposes of his shares in Water Eye Ltd. Colm's future base cost in the shares in Water Eye Ltd will be reduced by the amount of the gain deferred (i.e. €68,881).

Therefore, where all assets are transferred to Water Eye Ltd, no CGT should arise for Colm.

It should be noted that the transfer of trade payables/creditors to the company is concessionally treated by Irish Revenue as not to be consideration other than for shares for the purposes of the s600 incorporation relief.

(5 Marks)

Where s600 TCA 1997 is claimed on incorporation, John's period of ownership of the sole trade will count towards the minimum 10 year ownership and working/director period required under s598/599 TCA for retirement relief on any future disposal of the shares in Water Eye Ltd by Colm.

(1 Mark)

Stamp duty consequences

Water Eye Ltd will incur stamp duty on the transfer of assets to it. A 2% rate of stamp duty will apply to the transfer of the premises, goodwill and trade receivables.

(1 Mark)

VAT consequences

The VAT consequences associated with the transfer of the trade need to be considered. A VAT exemption is available where a trade and its assets are transferred as a going concern (s20(2)(c) and s26 of VAT Consolidation Act 2010 (VATCA)). This relief is commonly referred to as the transfer of business relief. The relief is only available where the following conditions are satisfied:

- The purchaser (Water Eye Ltd) is a VAT registered person – therefore before the transfer of the trade takes place, Water Eye Ltd should be registered for VAT; and
- Is entitled to claim a full (i.e. 100% recovery) input credit for any VAT charged to it; and
- The transfer must constitute an undertaking or part of any undertaking capable of being operated on an independent basis.

Where the transfer of business relief is available, it effectively deems that the transfer is not a supply of goods and therefore it falls outside the scope of VAT.

(4 Marks)

(14 Marks)

(b) CGT consequences of Colm incorporating his trade and transferring all assets and liabilities for shares in a new company plus cash of €150,000

Where cash is received by Colm from Water Eye Ltd in addition to shares, the amount of any CGT that can be deferred is limited to:

$$\frac{\text{Consideration in the form of shares (500,000)}}{\text{Total gross value of assets taken over (650,000)}} \quad \text{x} \quad \text{Chargeable gain}$$

Therefore, if €150,000 of cash is received then the amount of the gain that can be deferred is:

€500,000/€650,000 x €208,730 = €160,562

So the taxable gain for Colm in this situation will be €208.730 - €160,562 = €48,168. Ignoring the annual exemption, this equates to a CGT liability of €15,895.

(3 Marks)

(c) Tax consequences of Colm incorporating his trade but not transferring the building to the company and instead renting the building to Water Eye Ltd.

CGT consequences

S600 TCA 1997 incorporation relief is not available unless all assets (except cash are transferring to the company. Therefore, where the premises is not transferring, Colm will be subject to CGT of €52,381 ((€160,000 - €1,270) x 33%).

Income tax consequences

The income tax consequences of the cessation of the trade would remain the same as outlined above. However, Colm may consider taking a director's loan from his company in respect to the assets he is transferring in (including the goodwill). Colm's director's loan account in Water Eye Ltd will mean that at a later date when the company has surplus cash, he can withdraw funds from the company without any tax implications.

In addition, where Colm continues to hold the premises personally and rent it to his newly incorporated company, income tax on the rental income will need to be considered.

(3 Marks)

(20 Marks)

SOLUTION 5

(a) Michaela will be treated as Irish tax resident in 2014 if she spends 183 days in Ireland in 2014 or if she spends a total of 280 days in Ireland between 2013 and 2014. Based on the details regarding her movements since she returned to Ireland on 2 January 2014, it is likely that she will breach the 183 days in Ireland in 2014. This is on the basis that if we assume she is in Ireland for 4 days per week, then in a year this would equate to 208 days.

Based on what Michaela's friend has advised her, it appears that the UK is also treating Michaela as being UK resident.

(2 Marks)

The Ireland/UK tax treaty does not allow for the concept of dual residence but does contain a tie-breaker clause for individuals. The tie-breaker test is carried out by establishing the answer to a series of questions as follows:

- Where is the individual's permanent home or centre of vital interests?
- Where does the individual have his/her habitual abode?
- Is the individual a national of either state?
- If none of these questions gives an indication of the individual's tax residence, then residency is to be determined by mutual agreement between the Revenue authorities.

It appears that Michaela only has a permanent home in Ireland. When she travels to London for work, she stays in a hotel.

(2 Marks)

In summary, even though Michaela is tax resident in both Ireland and the UK under their respective domestic legislation, the treaty tie-breaker clause confirms that Ireland is where she is tax resident on the basis that she has a permanent home available to her there.

(For a clear summary of the position) 2 Marks

(6 Marks)

(b) UK employment income – subject to tax in the UK as her duties are carried out there.

(1 Mark)

In Ireland, Michaela should be able to claim the Cross-Border Worker Tax Relief (i.e. Transborder Relief) as she is exercising the employment in a treaty country (the UK) and she commutes weekly to her work in the UK returning to Ireland each week. If Michaela had no income other than her UK employment income, she would have no further Irish tax liability. However, her tuition income in Ireland will have to also be returned to Irish Revenue and this will lead to further tax due in Ireland.

(2 Marks)

In respect of her self-employed tuition income, she needs to return her tax adjusted trading profit to Irish Revenue for each year in which she was running the business in Ireland (i.e. 2014 and subsequent years). She will be entitled to claim a tax deduction for the normal trading expenses which are incurred wholly and exclusively for the purposes of the trade.

(1 Mark)

(4 Marks)

(c) Michaela will need to consider capital acquisitions tax (CAT) and stamp duty on the gift of the house from her father.

Irish CAT applies where:

- The donor is Irish resident
- The donee is Irish resident or
- The property is located in Ireland.

Therefore, the transfer of the Dublin property from her father will be subject to Irish CAT and the donor and the donee are Irish tax resident and the property is located in Ireland.

(1 Mark)

Irish stamp duty will also have to be paid on the transfer of the Dublin house. A rate of 1% will apply (i.e. €5,000).
(1 Mark)

Michaela's CAT liability will be
€500,000 - €3,000 (annual exemption) - €5,000 (stamp duty) - €225,000 = €267,000 x 33% = €88,110.
(1 Mark)

Michaela's CAT liability could be mitigated if she and her father hold off on the transfer until such times when she can qualify for the CAT dwelling house exemption.

(1 Mark)

(4 Marks)

(d) Michaela should have been filing tax returns in Ireland since 2014. Therefore, it is the 2014 and 2015 income tax returns that are now due, The 2015 income tax return will not be classed as late until 31 October 2016.
(1 Mark)

It is likely that Irish Revenue would view Michaela's behaviour of note filing and registering for tax as deliberate default.

Michaela may not have an option to self-correct as she failed to submit a return by the required deadline. Where Revenue do not accept self-correction, Michaela should make a qualifying disclosure in relation to 2014. This will be an unprompted qualifying disclosure as she has not been contacted by Irish Revenue to date.
(1 Mark)

Her unprompted qualifying disclosure must:

- Contain a full disclosure of complete information in relation to all matters giving rise to the tax;
- Be made in writing;
- Be signed by or on bePALPFSLf of her.
- Be accompanied by: a declaration, to the best of her knowledge, information and belief, that all matters contained in the disclosure are correct and complete and payment of the tax and interest on late payment of that tax.

(1 Mark)

By making an unprompted qualifying disclosure she can avoid publication.
(1 Mark)

An unprompted qualifying disclosure will also help Michaela mitigate the tax geared penalties from 100% to 10% where this is her first unprompted qualifying disclosure.

(2 Marks)

(6 Marks)