CPA IRELAND | CERTIFIED PUBLIC ACCOUNTANTS

ADVANCED TAXATION

PROFESSIONAL 2 EXAMINATION - AUGUST 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

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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 practice in Cork. It is August 2016 and you met Barbara (55) and Herbie (62) Cassidy. Herbie has been a client of the practice for many years. He and Barbara have recently married. Prior to getting married, they were both widowed. Herbie has one daughter from his first marriage called Judith (27). Barbara does not have any children. As a result of their marriage, Barbara and Herbie would like to obtain some advice on their respective estates as they are both asset rich.

Herbie is the 50% shareholder (i.e. he owns 50 €1 ordinary shares) of Cassidy Plumbing Supplied Ltd (CPSL), a trading company that operates a number of plumbing retail outlets and more recently the company also sells plumbing supplies online. The company has been trading profitably for many years. Herbie inherited his shares in CPSL in October 1995 from his father. A 50% shareholding in the company was valued at €95,000 in 1995. The remaining 50% of the shares in CPSL are held by Herbie's brother Seamus. Herbie has been the full time managing director of the company for the past four years. Prior to this, he worked part-time as the company's technical director.

Judith, Herbie's daughter, has just graduated from college and she is looking for a job in an accountancy practice to undertake her CPA professional exams and training. Judith inherited €50,000 from her mother on her death. Herbie would like to gift Judith a 10% shareholding in the company immediately. A 10% shareholding in CPSL is currently valued at €200,000. Herbie intends to retire in the next five years. He currently does not have a pension fund but he has heard from a friend that the company should be paying into one for him and his brother. He would also like to increase the money he extracts from the company each year for the next five years so that he can build up his personal savings for retirement. In five years' time he intends to retire from the company but he will retain his shares and pass them to Judith on his death.

Barbara was widowed six years ago and she inherited all her husband's assets. Her husband, Barney, was a farmer. He bought a large farm near Tralee, Co. Kerry seven years before he died. The farm cost €150,000 and he farmed the land from the day he purchased it to the day he died. When he died, the land was valued at €250,000 and was transferred into Barbara's sole name at this time. Barbara has continued to farm the land since his death. She was only able to do this by getting the help of Barney's (blood) nephew, Ian (30). Ian has worked full time on the farm for the last six years and Barbara pays him an annual salary of €18,000. Barbara would like to make a once off gift of the farmland and some cash to Ian. Ian has never received any previous gifts/inheritances. The farmland has been valued recently at €350,000. Ian does not own any other assets except his tractor which is valued at €15,000. Ian is very excited about the prospect of being gifted the land and he has stated that he will continue to farm the land as his only source of income for the foreseeable future.

REQUIREMENT:

Draft a report for you manager so that he can then arrange a meeting with Barbara and Herbie Cassidy to discuss the following:

(a) The tax implications for Herbie of transferring the 10% shareholding in Cassidy Plumbing Supplies Ltd (CPSL) to Judith in August 2016. Your answer should include tax planning advice on how he could minimise his tax exposure.

(7 marks)

(b) The tax implications and reliefs available to Judith if she is gifted a 10% shareholding in CPSL in August 2016.

(8 marks)

(c) Relevant tax planning points in respect of Herbie's proposed retirement from CPSL in five years' time and his desire to fund for his retirement. Your answer should advise if it is suitable for him to take extra money from the company over the next five years as dividends and whether a company pension scheme should be set up and funded. You should also detail any exemptions and reliefs available on retirement so that he can obtain maximum funds in his personal name.

(10 marks)

(d) The tax implications for Barbara and Ian in respect of the transfer of farmland to him on 1 January 2017. In addition, you should calculate the maximum amount of cash Barbara can gift Ian at the same time she is transferring the farmland so that she will not jeopardise his claim to agricultural relief.

(13 marks)

Format and Presentation (2 marks)

[Total: 40 marks]

2. It is 1 July 2016 and you are a Certified Public Accountant who has just come back to work from your summer holidays. Your tax manager has called you to a meeting to discuss a number of your cases that she would like you to look at immediately. After asking how your holiday went, your manager outlines the following three cases:

Case 1: Brian Myer Bottling

You have worked on the income tax compliance case for Brian Myer for the last few years. A Revenue audit letter has been received by Brian stating that all records in respect of his 2014 income tax return are under investigation. This is the first Revenue audit that Brian has ever had and it is due to commence next week. Brian runs a bottling business as a sole trader. He prepares his accounts to 31 December each year and pays tax at a marginal rate of 52%. He rents the building from which he trades. When Brian's 2014 tax return was being prepared a review of his expenses was carried out and it was noted that the repairs expenses had more than doubled in 2014. You queried the deductibility of the expenses at the time but he confirmed, in writing, that all the repairs expenditure related to the commercial building from which his business trades.

As a result of the Revenue audit letter, Brian has now left in the invoices in respect of the repairs. One invoice for €40,000 is from a local builder in respect of an extension to Brian's private residence.

Case 2: Maeve McGrory

Maeve is a very wealthy widow who owns an extensive property portfolio. She purchased a commercial unit in January 2014 for €700,000 plus VAT. She reclaimed the VAT on purchase from the Revenue Commissioners. In January 2016, she finally got tenants to take over the unit. She agreed a €5,000 rent per quarter for the commercial premises and she has agreed that their rent will not increase for at least the next two years. Her tenants are a financial services company and they have told her that they are VAT exempt. Therefore, Maeve did not charge VAT on their invoice for January to March 2016 and she obtained a refund of €1,400 on her January-March 2016 quarterly VAT return. Maeve has asked your practice to complete her April to June 2016 VAT return as she has been told by a friend that she should be charging VAT on the rents to avoid having to pay back the VAT she initially recovered on the purchase of the commercial unit.

Case 3: Murphy Hotels Ltd (MHL)

MHL operates a number of hotels in the west of Ireland and has a 31 March year end. The company has made losses for the last number of years and therefore had trading losses forward of €300,000 on 1 April 2014. The company had taxable trading profits in the year ended 31 March 2015 of €100,000 but no corporation tax was paid due to the corporation tax losses forward being utilised. On review of the company's corporation tax computation for the year ended 31 March 2015, it appears that there was an increase of €50,000 in a pension accrual that was not adjusted for.

REQUIREMENT:

(a) Advise Brian on how he should approach the Revenue audit and the likely revenue view in respect of him claiming a private expense as a business expense.

(7 marks)

(b) Discuss Maeve's VAT position in respect of the rent from the commercial property. Where she has not been treating the rents correctly for VAT purposes to date, recommend how she should correct her position with Revenue.

(9 marks)

(c) Advise how the omission of the increase in the pension accrual should be rectified by Murphy Hotels Ltd.

(4 marks)

[Total: 20 marks]

3. You are a newly qualified Certified Public Accountant working in an accountancy practice in Carlow. You are currently working on the file of Eddie Devlin (45), a company director and carpenter by trade. In 2014 Eddie sold an investment property in Dublin and he made a €750,000 gain (after tax). Since he made this gain, he has been looking for a new business to invest in.

For the past 15 years, Eddie has been the 100% shareholder of Devlin Shop Furniture Limited (DSFL). He paid €100 for 100 €1 ordinary shares in DSFL and the company currently has a market value of €1,200,000. DSFL is a successful Irish resident trading company which specialises in making shop furniture for cosmetic and pharmacy businesses. This company has been trading profitably since incorporation and it pays over €10,000 in corporation tax on an annual basis.

Eddie has recently identified another Irish trading company which he would like to purchase called Garden Furniture Ltd (GFL). He has been provided with the company's last four years financial statements and corporation tax returns. The company has been loss making for the last four years with corporation tax trading losses forward of €90,000. The company is for sale for €500,000. With the experience he has gained in DSFL and the contacts and suppliers he has, Eddie feels that he can turn the trade of GFL around to make it profitable again and he anticipates that this process would take four to five years. In the medium term, he would consider selling GFL and using the profit on this to reinvest again in another struggling trading business.

You have advised Eddie that a holding company structure should be set up. Eddie has agreed that he will transfer his current shares in DSFL for shares in Devlin Holdings Ltd (DHL), the new holding company which will be incorporated. Eddie has agreed that he will then lend DHL €500,000 to purchase the shares in GFL. It is proposed that the restructuring and the purchase of GFL will all be in place by 1 October 2016.

The projected corporation tax position for DSFL for the year ending 30 September 2017 is:

Case I trading profit	€100,000
Case III interest income	€5,500

The anticipated corporation tax trading losses in GFL for the year ending 30 September 2017 is €140,000. GFL is also projected to have gross interest income of €2,500 for the year ending 30 September 2017.

REQUIREMENT:

Draft a report for Eddie which contains the following:

(a) The tax implications for him of setting up a holding company for Devlin Shop Furniture Limited. You should clearly state the taxes to be considered when setting up this structure as well as any reliefs that can be claimed.
(8 marks)

(b) Further details of the tax implications of him lending €500,000 to Devlin Holdings Ltd and the tax implications for him of getting this money back from the company.
(2 marks)

(c) The tax implications for the new holding company buying shares in Garden Furniture Ltd. (2 marks)

(d) The projected corporation tax liability of Devlin Shop Furniture Ltd for the year ended 30 September 2017, if all tax relief claims are made.
(4 marks)

(e) The tax implications for the group of the potential sale of Garden Furniture Ltd in four to five years. You should include details of any reliefs available.
(4 marks)

[Total: 20 marks]

4. It is August 2016 and you work for an accountancy practice in Cork. Your firm has recently revamped the tax section of its website and as a result a lot more queries are coming to the practice from individuals who are considering moving to Ireland. The following email has been received on 10 August 2016:

Dear Sir/Madam

By way of introduction, my name is Harold Smith and I am contacting you for some tax advice. My wife (Rose) and I have been living together in the UK for the last 10 years. I am English and have lived in Manchester all life. Rose is Irish and is originally from Donegal. Her father is Irish and still resides in Donegal. She only moved to the UK when we got married 10 years ago.

I have been offered a job in a financial services company in Letterkenny, Donegal and I have decided to the take the job as Rose has always wanted to return to live in Ireland. The job is due to commence on 10 January 2017. My 2017 gross salary has been agreed at €150,000. I am due to finish up my current UK employer on 30 November 2016 and I will have earned €125,000 gross from January 2016 to 30 November 2016. We plan to move to Ireland on 5 December 2016. We will remain in Ireland for the remainder of 2016. In addition, we have spent a total of 3 weeks holiday in Ireland to date in 2016. We will not be back in Ireland until we move there permanently in December 2016. In 2015, we spent approximately 28 days in Ireland on holidays.

Rose and I recently purchased a commercial building in Manchester. A tenant has agreed to rent the premises from 1 November 2016 for a monthly rent of £1,600 (i.e. €2,000).

Rose and I also have a rental property in Donegal. We have generated a combined rental profit €8,000 in 2016 to date. We intend to sell this property within the next month (i.e. by 30 September 2016) for €250,000. We will make a gain of €100,000 on this property. I also own a property in Liverpool worth €300,000. I plan to sell this next year (2017). With the way property prices are in Liverpool, I anticipate making a loss of €45,000 on this transaction. I may bring the sales proceeds into Ireland in 2017 to buy an investment property in Dublin.

Our family home in Newcastle is held in my name only as I was gifted it from my father five years ago. I do not intend to sell our family home in Newcastle. I am not fully intent on staying in Ireland permanently and would therefore like to hold onto the house as it has been in my family for four generations and I may move back to the UK in the future. I will rent this property out for €18,000 per annum. We intend to rent a house to live in in Ireland for a few years.

Rose and I have some money saved in a German bank and we each earn approximately €5,000 per annum in interest. My only other income is US and UK dividends which are approximately €15,000 per annum.

Rose has a job offer from an employer based in the U.K. in Derry, Northern Ireland. She is undecided as to whether she should take the job as she does not know the tax consequences. It would entail daily travel from Donegal to her prospective employer's premises and she would earn a gross annual salary of €25,000.

Any tax advice that you can provide us in respect of our plans to move to Ireland would be greatly appreciated. We are keen to understand how we will be taxed in Ireland in 2016 and 2017.

Best regards

Harold

REQUIREMENT:
Draft an email to Harold and Rose advising them of the following:

(a) Their Irish income tax position in 2016 and 2017 (no detailed income tax calculations required). (16 marks)

(b) The Irish tax consequences of the sale of the Irish property in 2016 and the UK property in 2017. (4 marks)

[Total: 20 Marks]

5. Gerard Lafferty (58) is a widower with two children, Emer (33) and Jimmy (27).

Gerard is thinking of transferring some of his assets to his children. He has been farming for the last 25 years but he is going to scale back his farming activities and start a new business which will manufacture heavy duty gates.

Emer lives in Dubai with her husband. However, she would like to build a holiday home in Ireland. Gerard has agreed to gift her a one acre site on the farm which has a current market value of €100,000. The site she would like is one which Gerard bought in 2004 for €15,000. Gerard has carried out various fencing repairs around the site (at a total cost of €12,000) over the years. However, it is still essentially a green field which he has always used for his farming trade.

Gerard currently resides in the farmhouse on the farm with Jimmy. Gerard bought this farmhouse (for €55,000) with the 40 acre farm (€40,000) in 1991. He has lived in the farmhouse and farmed the land ever since its purchase. Gerard would like to gift the farmhouse to Jimmy. It currently has a market value of €300,000 including the half acre garden surrounding it. Gerard intends to build a small granny-flat on the farm for himself. Gerard does not wish to transfer any of the 40 acre farm to Jimmy until he is at least 35 years of age and married. Jimmy does not own any other property.

Neither Emer nor Jimmy have ever received any previous gifts or inheritances.

With regard to his new business venture, Gerard has already incorporated a new company, Lafferty Gates Ltd (LGL). This company will make and sell heavy duty gates for fields. He anticipates his sales in year one to be €70,000 and then €180,000 in year two. Gerard knows that the rate of VAT applying to the goods the company will be selling (i.e. the gates) is 23%. The company's raw materials will be bought from VAT registered businesses in Ireland and the UK. Most of LGL's customers will be VAT registered customers in Ireland and the UK. However, a small number will be non-VAT registered customers in Ireland and the UK also. Gerard anticipates that in year two and beyond, the USA will be the company's main market as he will market the specialised gates to large dairy farmers there.

REQUIREMENT:

(a) Advise Gerard of the tax implications for him and for his children of the proposed transfers. (8 marks)

(b) Advise Gerard on the implications of VAT registration for his business. Explain whether Lafferty Gates Ltd should register for VAT in advance of being required to do so?

(12 marks)

[Total: 20 marks]

END OF PAPER

SUGGESTED SOLUTIONS

THE INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS IN IRELAND

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PROFESSIONAL 2 EXAMINATION - AUGUST 2016

SOLUTION 1

TAX REPORT

TO: **Manager**
FROM: **CPA**
RE: **Tax Report for Barbara and Herbie Cassidy**
DATE: **August 2016**

Presentation (2 marks)

Section A The tax implications for Herbie on the transfer of a 10% shareholding to Judith

Herbie needs to consider his capital gains tax position on the transfer of his shares to Judith.

Market value will be imposed as it is a gift.

Consideration needs to be given as to whether retirement relief can be claimed by Herbie. The main conditions for retirement relief are:

- The individual making the disposal must have attained 55 years of age – YES
- The shares must have been held for ten years by the individual ending with the disposal. For full relief all of the capital assets of the company must be trade assets – YES
- The company must be a trading company – YES
- The shares must be held in a "family company".
  1. A family company is defined in section 598 (1) (a) TCA 1997 as a company where the individual must hold (a) at least 25% of the voting rights or (b) at least 10% of the voting rights where the family own 75% of the voting rights. – YES
- The individual must have been a working director for at least 10 years and a full time working director for at least five of those years. – NO AS HERBIE ONLY FULL TIME WORKING DIRECTOR FOR 4 YEARS.

As all of the above conditions are not satisfied, Herbie will not be eligible for retirement relief. (2 marks)

He will therefore have a CGT exposure of:

	€
Deemed proceeds	200,000
Less Cost (€95,000/50 x 10)	
X 1.277 (indexation)	(24,263)
Gain	175,737
Less annual exemption	(1,270)
Chargeable gain	174,467
Gain at 33%	57,574

(2 marks)

If Herbie transfers the shares before 30 November 2016, this CGT will be due on 15 December 2016. The gain should also be included in Herbie's 2016 income tax return (Form 11).

(1 mark)

Herbie should be advised to hold off transferring the shares for 1 year so that he can fulfil the 5 year full time director requirement.

(2 marks)

(7 marks)

Section B CAT and stamp duty for Judith on immediate disposal

Business Relief (BR) will amount to a reduction of 90% in respect of the value attributable to relevant business property taken by the beneficiary, Judith. Only relevant business property will qualify for the relief. "Relevant business property" includes shares in a trading company.

The following conditions must be satisfied for business relief to apply. Judith must satisfy one of the following conditions after taking into account the shares which she is gifted:

1. She must control more than 25% of the voting rights – NOT SATISFIED
2. The company is, after taking the gift, under the control (i.e. more than 50%) of the recipient and her relatives. RELATIVES INCLUDES FATHER AND UNCLE SO CONDITION SATISFIED
3. He must control at least 10% or more of the aggregate nominal value of all issued shares and securities of the company and has worked full time in the company or the group throughout the period of 5 years ending on the date of the benefit – NOT SATISFIED

In addition, in order for business relief to apply, Herbie must have held the shares for a minimum of 5 years prior to the gift. As Herbie has held his shares since 1995, this condition is satisfied.

(3 marks)

Judith's CAT position with be as follows:

	€
Value of shares	200,000
Less stamp duty	(2,000)
	198,000
BR	(178,200)
	19,800
Less SGE	(3,000)
Plus previous group A	50,000
	66,800
Less Group A threshold	(225,000)
Balance of Group A	158,200

(2 marks)

As there is no CAT liability for Judith, no CGT/CAT same event credit can be claimed. (1 mark)

BR clawback provisions also need to be considered. BR will be clawed back if CPSL ceases to be a trading company within 6 years or if Judith sells the shares within 6 years.

(1 mark)

Judith will have a stamp duty liability of €200,000 x 1% = €2,000. (1 mark)

(8 marks)

Section C Tax planning and cash extraction

My advice would be for Herbie to tax extra salary from CPSL rather than dividends. The reasons for this are outlined below:

1. Salary is tax deductible for the company whereas dividends are not. As CPSL has been trading profitably for many years the company is most likely paying corporation tax every year. A salary will benefit for 12.5% corporation tax relief as a business expense.

2. When a salary is voted all taxes (income tax/PRSI and USC) are paid by the company and therefore Herbie should have no further tax liability on the extra salary when filing his annual tax return. When this is compared to the position where dividends are received, they will be received with only 20% dividend withholding tax (DWT) withheld by CPSL. The 20% DWT is allowed as a tax credit in the income tax computation. Where Herbie is a top rate taxpayer, additional tax will be due (i.e. another 20%) as the top rate of tax is 40%. PRSI and USC will also be due.

3. Extra salary increases the potential for pension contributions and termination payment amounts on retirement.

The disadvantages of paying salary as opposed to dividends include:

1. Employer PRSI will be due on a salary for Herbie as he is not a controlling shareholder. No employer PRSI is due on dividends.

2. Paying additional salary on a monthly basis may put some strain on the cash flow position of the company. Dividends on the other hand do not need to be paid until after the company has traded for the year and the profit position is known.

As noted above, where Herbie's salary is increased, one of the main benefits is that the company has scope to make increased pension contributions and also the amount of tax-free termination payment available to Herbie may be increased.

(4 marks)

Termination payment planning
Termination payments offer a tax-efficient method of extracting funds from CPSL. The tax-exempt portion of a termination payment is computed using the highest of the following options:

1. the "basic exemption" of €10,160 plus €765 for each complete year of service
Herbie will have worked in CPSL from 1995 to 2021 i.e. 26 years. Therefore, the basic termination payment amount will be €10,160 + €765 x 26 = €30,050.

2. the "increased exemption" is 1. Above plus €10,000, less any tax-free payment received or receivable from a pension scheme. See below for advice regarding the funding of an occupation pension scheme. Any lump sum from this scheme will reduce the €10,000 increase. E.g. If Herbie becomes entitled to a lump sum of €15,000 from his pension scheme, the increased basic exemption will be €30,050 + 0 = €30,050

or

3. the standard capital superannuation benefit (SCSB). This is calculated by

$$\frac{\text{Average remuneration over last 3 years x no. of years of service}}{15} - \text{pension lump sum}$$

The SCSB will be reduced by any tax fee lump sum received from a company pension scheme on retirement.

There is a €200,000 cap on the amount of lump sum termination payment.

Where Herbie is considering funding a pension scheme, the basic exemption may be the highest amount. He will therefore be entitled to a termination payment of €30,050.

(3 marks)

Occupational pension scheme planning
CPSL should set up a company pension scheme. Some of the tax benefits of such a scheme include:

1. The contributions paid by CPSL to the pension scheme are fully tax deductible however they may need to be spread where they are special contributions.

2. CPSL will receive a corporation tax deduction by reference to the pension payments made.

3. Importantly, the contributions paid by CPSL to a Revenue approved company pension scheme are not subject to the same restrictions as those for personal contributions (i.e. limited based on age and net relevant earning amount which is capped at €115,000).

Where a CPSL establish a company pension scheme, it would be advisable for Herbie to fund for his retirement via the pension scheme.

If CPSL set up a corporate occupational pension scheme, it will be possible for CPSL to make special lump sum payments to top-up a pension fund so that it can meet Herbie's future pension requirements. Revenue limits on company contributions make it possible to provide for a maximum fund of two-thirds of the employee/director's final pensionable salary. The pension fund may not be sufficiently funded to provide for such a pension (i.e. two-thirds of the individual's final salary), and the company may make lump sum top-up payments on a periodic basis to meet the fund's future requirements/obligations.

On Herbie's retirement, he will be able to take a portion of the pension fund as a tax-free lump sum. Broadly, there are two options:

1. As Herbie has 20 years of pensionable service with CPSL, this entitles him to a maximum tax-free lump sum payment from the pension fund of 1.5 times their "final pensionable remuneration". Where there is a fund remaining, this can be used by Herbie to purchase an annuity.

2. Alternatively, 25% of the accumulated fund can be taken as a cash lump sum with the balance, either: in an approved retirement fund (ARF); used to purchase an annuity or take the cash and pay income tax on it.

In addition, consideration should be given to planning for a share buyback. Herbie intends to hold on to his remaining shares until his death however, he may wish to extract some cash on retirement via a share buyback.

(3 marks)

(10 marks)

Section D Tax implication of the gift of farmland to Ian

CGT for Barbara

Consideration needs to be given as to whether retirement relief can be claimed by Barbara. The main conditions for retirement relief are:

- The individual making the disposal must have attained 55 years of age – YES
- The land must have been held for ten years by the individual ending with the disposal and was used for the purposes of a trade for 10 years – YES AS HUSBAND'S OWNERSHIP CAN BE ADDED TO BARBARA'S PERIOD

As all of the above conditions are satisfied, Barbara will be eligible for retirement relief. She will have no CGT liability.

(3 marks)

CAT for Ian

Ian will not be eligible for favourite nephew relief as he is not a blood nephew of Barbara's. (2 marks)

AR can only apply where the beneficiary qualifies as a 'farmer'. Therefore, Ian must be a farmer as defined for AR to apply. Ian 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 the calculation below, Barbara can only gift Ian €91,250 before he would fail the 'farmer' test and therefore not qualify for agricultural relief.

Farmer Test for Agricultural Relief

	Total value	Agricultural assets	Non-agricultural assets
Farm land	350,000	350,000	
Tractor	15,000	15,000	
Cash	91,250		91,250
	456,250	365,000	91,250

Farmer test = 365,000/456,250 = 80% (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, Ian would need to spend a minimum of 20 hours working per week, averaged over a year, on the farm. It is likely that Ian will be able to do this as he intends for the farm to be his main source of income.

Business relief may also be available. However, where the conditions for both agricultural relief and business relief are met, agricultural relief should be claimed first.

(2 marks)

Where agricultural relief is claimed, Ian's CAT liability will be as follows:

CAT liability where AR claimed	€
Market value of assets qualifying	350,000
Less stamp duty	(7,000)
	343,000
Less AR	(308,700)
Agricultural value	34,300
Cash	91,250
Less SGE	(3,000)
Less group C threshold remaining	(15,075)
Amount subject of CAT	107,475
CAT at 33%	35,467

(2 marks)

Stamp duty for Ian

Stamp duty of 2% in respect of the farmland will arise for Ian. There is no stamp duty on cash. (1 mark)

(13 marks)

SOLUTION 2

Case 1: Brian Myer Bottling

Brian should not have claimed the €40,000 building expense as a repair as it was not incurred wholly and exclusively for the purposes of the trade. He has therefore underpaid his taxes by 40,000 x 52% = €20,800.

(1 mark)

As a Revenue audit letter has been received, it is not possible for Brian to make an unprompted qualifying disclosure. However, he still has the opportunity to make a prompted disclosure.

(1 mark)

A prompted qualifying disclosure must be made in writing, it must be signed by or on behalf of the taxpayer and it must include:

1. A declaration that all matters contained in the disclosure are correct and complete
2. A payment of the tax and interest. The underpaid tax is likely to be €20,800 plus interest
3. A full explanation in relation to the amounts previously undisclosed and a computation for the amount of tax due.

(2 marks)

Given that the invoice clearly shows that it relates to Brian's private residence and given the quantity, it is likely that Revenue will view this as deliberate behaviour. Therefore, the qualifying disclosure must state the amounts of <u>all</u> liabilities to tax and interest, in respect of <u>all</u> tax heads and periods, where liabilities arise, <u>as a result of deliberate behaviour.</u>

(1 mark)

It is assumed that Brian has never made a qualifying disclosure before as this is his first ever audit. The benefits of making a prompted qualifying disclosure include non-publication, non-prosecution and mitigation of penalties. By making a prompted qualifying disclosure and by fully co-operating with Revenue he could reduce the penalty for deliberate behaviour from 100% to 50% of the tax underpaid.

(2 marks)

(7 marks)

Case 2: Maeve McGrory

Maeve recovered €161,000 when she purchased the commercial unit in January 2014. Therefore, the property is in the VAT net. When Maeve rents out the commercial unit, she must charge VAT if she does not wish to incur a capital goods scheme (CGS) adjustment. She therefore has 2 options:

1. Pay the VAT on the rents to Revenue in her quarterly VAT returns
2. Pay a CGS adjustment (1 mark)

1. Letting is an exempt activity for VAT purposes. However, Maeve as landlord could exercise an option to apply VAT to the letting. As the letting is not residential nor is she connected with the tenants, she should be able to exercise the option.

   (1 mark)

   Unfortunately, Maeve has already agreed a rent of €5,000 per quarter with her tenant. Therefore, if €5,000 is the maximum amount that the tenant is will to pay then this will have to be deemed to be the VAT inclusive amount. The VAT that will be due per quarter will therefore be €5,000 - €5,000/1.23 = €935.

   (1 mark)

   Maeve has already filed her January to March 2016 VAT return without including the VAT. She has essentially underpaid her VAT by €935. In fact she has actually received too much of a refund.

   (1 mark)

   As this underpayment has been picked up very quickly (i.e. before the filing of the subsequent VAT return for the April to June 2016 quarter) and as the net underpayment of VAT for the period being corrected is less than €6,000, the amount of the tax can be included (without interest or notification to Revenue) as an adjustment on the April to June 2016 VAT return.

   (2 marks)

2. Maeve may decide that instead of only receiving net rent of €4,065 per quarter that she would prefer to pay back a CGS. The CGS will be €94,500/20 = €4,725 per annum. This would be more costly for Maeve (when compared with €935 x 4 = €3,740)

(3 marks)

(9 marks)

Case 3: Murphy Hotels Ltd (MHL)

An increase in a pension accrual of €50,000 should have been added back in the corporation tax computation. This addback would have the impact of increasing the taxable trading profits to €150,000. No additional corporation tax will be due as a result of the fact that there are enough trading losses forward to cover the additional taxable trading profits arising from the correct treatment of the increased pension accrual.

(1 mark)

No Revenue audit notification has been received and so MHL should consider self-correction. The self-correction time limit for corporation tax is that the self-correction must take place within 12 months of the due date for filing the return.

(1 marks)

MHL are within the self-correction window as MHL's corporation tax return for the year ended 31 March 2015 would have been due for submission by 21/23 December 2015. The self-correction window for the corporation tax return for the year ended 31 March 2015 will not expire until December 2016.

(1 mark)

MHL should undertake the following steps to self-correct the corporation tax return for the year ended 31 March 2015: Revenue must be notified of the adjustment in writing or electronically by amending the Form CT1 through the Revenue On-Line (ROS) service. Where Revenue are informed in writing of the amendment, it should be highlighted in the letter that no extra tax needs to be paid but the trading losses forward amount as at 31 March 2015 is reduced by €50,000 to €150,000.

(1 mark)

(4 marks)

SOLUTION 3
REPORT
To: Eddie Devlin
From: CPA
Date: August 2016
Re: Reorganisation of group and company purchase

(a) The tax implications for him of setting up a holding company for Devlin Shop Furniture Limited. You should clearly state the taxes to be considered as well as any reliefs that can be claimed.

It has been agreed that Eddie will transfer his current shares in DSFL (100 ordinary shares with a base cost of €100) for shares in Devlin Holdings Ltd (DHL), the new holding company which will be incorporated.

DSFL is currently valued at €1,200,000 and Eddie has a base cost of €100 (small amount of indexation is ignored). Therefore, if Eddie transfers his shares in GFL for no consideration, a potential CGT liability of €395,967 (€1,200,000 - €100 = €1,199,900, €1,199,900 x 33% = €395,967) could arise.

(2 marks)

In addition, where shares with a value of €1,200,000 are transferred a potential stamp duty liability of €12,000 could arise.

(1 mark)

However, CGT and stamp duty reliefs are available where there is a company reorganisation without a change in ownership.

For CGT s584-587 TCA 1997 are relevant. Eddie is effectively swapping his shares in DSFL for new shares, in the same proportion, in DHL. DHL, as the acquiring company, will take a 100% holding/full control of DSFL. The reorganisation is for bona fide commercial purposes and does not form part of an arrangement whose main purpose is the avoidance of tax. As all the conditions above are fulfilled, no CGT should arise. For tax purposes, Eddie is treated as having made no disposal of the old shares (i.e. DSFL) and the new shares (DHL) are treated as if they are being acquired at the same base cost/date of acquisition as the original holding in DSFL.

(2 marks)

For stamp duty s80 SDCA 1999 is relevant. No stamp duty will arise on the reorganisation where the following conditions are satisfied:

- the acquiring company (DHL) is a limited company - satisfied;
- the acquiring company(DHL) will issue new shares in exchange for 90% or more of the shares in the target company (DSFL) - satisfied;
- the shares being issued in the acquiring company (DHL) will represent at least 90% of the value of the target company DSFL) - satisfied;
- the transaction is being undertaken for bona fide commercial reasons - satisfied.

(2 marks)

Stamp duty will not arise on the shares acquired by DHL. If the relationship between DHL and DSFL is broken within two years of the transfer, the stamp duty relief will be clawed back.

(1 mark)

(8 marks)

(b) Further details of the tax implications of him lending €500,000 to the new holding company and the tax implications of getting this money back.

There are no tax implications on the lending of €500,000 to the holding company. This amount will be credited to the director's loan account. The €500,000 will show as a liability on the statement of financial position of the holding company. When the holding company has the money to pay back the loan, this can be done so tax free. The loan can be paid back in a piecemeal basis or in one lump sum if cash flow permits.

(2 marks)

(c) The tax implications for the new holding company buying shares in Garden Furniture Ltd.

The new holding company will have to pay stamp duty of 1% on the acquisition (€500,000 x 1% = €5,000). In addition, the anti-avoidance loss buying provisions should be considered.

(2 marks)

(d) The projected corporation tax liability of Devlin Shop Furniture Ltd for the year ended 30 September 2017 if all tax relief claims are made.

DSFL and GFL will be in a corporation tax group from the date that the holding company structure is put in place i.e. 1 October 2016.

Losses carried forward in DFL before the date the group was formed cannot be group relieved. (1 mark)

The anticipated corporation tax trading losses in GFL for the year ending 30 September 2017 is €140,000. GFL is also projected to have gross interest income of €2,500 for the year ending 30 September 2017. Therefore €5,000 of the current year trading loss will be used to offset any tax on this under s395B TCA 1997. The balance of losses available for group relief are €135,000. A s396B claim does not have to be made before s420A.

(1 mark)

The projected corporation tax position for DSFL for the year ending 30 September 2017 is:

Case I trading profit	€100,000
Case III interest income	€5,500

A s420 TCA 1997 group relief claim can then be made to reduce the taxable trading profits in DSFL to €0. The balance of losses available for group relief is €135,000 - €100,000 = €35,000.

A s420B TCA 1997 value base group relief claim can then be made. The amount of group losses required to eliminate the corporation tax on €5,500 of interest is

€5,500 x 25% = €1,375
€1,375/0.125 = €11,000

Therefore, DSFL's corporation tax liability will be nil for the year ended 30 September 2017.

Losses forward in GFL are €24,000 (€140,000 - €5,000 - €100,000 - €11,000 = €24,000) (2 marks)

(4 marks)

(e) The tax implications for Devlin Holdings Ltd (DHL) of the potential sale of Garden Furniture Ltd (GFL) in 4 - 5 years. You should include details of any reliefs available.

Section 626B TCA 1997 provides for a tax exemption which is commonly referred to as the Participation Exemption. This exemption can apply to the gain on the disposal of shares by a holding company such as DHL. A number of conditions must be met before a gain can be exempt:

1. The investor company (i.e. DHL) must be a 'parent' company and hold at least 5% in GFL at the time of disposal. DHL satisfies this condition as:
   - DHL held not less than 5% of GFL's ordinary share capital – it was 100% parent;
   - DHL was beneficially entitled to not less than 5% of the profits available for distribution to equity holders of GFL; and
   - on a winding up, DHL was beneficially entitled to not less than 5% of the assets available for distribution to equity holders.
2. The investor (i.e. DHL) is required to have the minimum holding in the investee company (GFL) for a continuous period of at least 12 months – this will be satisfied if the shares are held for 4/5 years
3. The investee company (i.e. GFL) must carry on a trade – GFL is a trading company.
4. At the time of the disposal the investee company (i.e. GFL) must be resident in a Member State of the EU or a country with which Ireland has a tax treaty – GFL is an Irish resident company and so this condition is satisfied.

(2 marks)

The level of Irish land and buildings owned by GFL should be monitored as the participation exemption will not apply where the shares in GFL derive the greater part of their value from land in Ireland.

(1 mark)

In summary, DHL could therefore sell GFL in 4 - 5 years' time and pay no corporation tax on the chargeable gain. The full proceeds could therefore be held by DHL for further investment in another company.

(1 mark)

(4 marks)

SOLUTION 4

Dear Harold and Rose

Further to your recent email to our practice, please find below an initial analysis of your Irish tax position:

Income tax position in 2016 and 2017

Rose appears to be Irish domiciled. She was originally from Ireland, her father is Irish and she appears to have always intended on returning to Ireland.

Harold is non-Irish domiciled. He appears to be UK domiciled as his father and previous generations were all from the UK. He also may return to the UK to live in the future.

(1 mark)

A summary of Harold and Rose's days count in Ireland are as follows:

2015 – 28 days
2016 – 21 days holidays + 27 days from 5 December 2016 = 48 days
2017 – over 183 days (1 mark)

In 2016 Harold and Rose will not be considered Irish tax resident as they have not been in Ireland for 183 days. Also, based on the information given, as they only stayed in Ireland for 28 days in 2015, they will not be classed as Irish resident in 2016 on the 280 lookback rule.

(1 mark)

Therefore in 2016:
Harold will be non-resident, non-ordinary resident and non-domiciled.
Rose will be non-resident, non-ordinary resident and Irish domiciled. (2 marks)

Harold and Rose will only be subject to Irish tax on their Irish source income in 2016. That is, on the Irish rental income of €4,000 each they generated from the holiday home in Donegal.

This income will be subject to 20% tax in Ireland. They will each be entitled to an apportionment of the Irish personal tax credit of €1,650. The proportion available is worked out as follows:

$$€1{,}650 \times \frac{\text{Irish income}}{\text{Irish income + worldwide income}}$$

(2 marks)

In 2017:
Harold will be resident, non-ordinary resident and non-domiciled.
Rose will be resident, non-ordinary resident and Irish domiciled. (2 marks)

An individual like Harold who is resident but not domiciled in Ireland is liable to income tax in full on:

1. any income arising in Ireland; and
2. other income arising outside of Ireland but only to the extent that it is remitted into Ireland; and
3. income from an office or employment, insofar as that income relates to the performance, in Ireland, of the duties of that office or employment (irrespective of where it is paid or whether it is remitted into Ireland or not).

Harold's sources of income in 2017 are:

Irish Employment	€150,000	Subject to Irish PAYE	
UK commercial rental	€12,000	Subject to Irish tax if remitted	
UK residential rental	€18,000	Subject to Irish tax if remitted	
Interest income (German)	€5,000	Subject to Irish tax if remitted	
UK and US dividends	€15,000	Subject to Irish tax if remitted	(3 marks)

A non-Irish domiciled individual such as Harold should ensure that he keeps gains and profits earned before he becomes Irish tax resident (i.e. 1 January 2017) in a separate bank account to income earned after he becomes Irish resident so that he can identify and remit pre residence funds free of Irish tax.

(2 marks)

An Irish domiciled individual like Rose who is resident but not ordinarily resident in Ireland in 2017 is liable to income tax on:

1. any income arising in Ireland; and
2. foreign sourced income (whether remitted to the State or not).

Rose's sources of income in 2017 are:

UK Employment	€25,000	Subject to UK PAYE and claim transborder relief in Ireland
UK commercial rental	€12,000	Subject to Irish tax with double tax relief for any UK tax suffered
Interest income (German)	€5,000	Subject to Irish tax

(2 marks)

(16 marks)

The Irish tax consequences of the sale of the Irish property in 2016 and the UK property in 2017 and the Irish property

Harold and Rose are both non-resident in Ireland in 2016 when the Donegal property is sold. However, non-resident individuals remain subject to Irish capital gains tax (CGT) on the sale of Irish specified assets. Irish specified assets include: land in Ireland, including buildings on the land.

Therefore, Harold and Rose will be subject to Irish tax at 33% on the gain on the sale of the Donegal property in 2016. They may be subject to UK tax also as they are resident in the UK. Credit should be given in the UK for any Irish tax suffered.

(2 marks)

Harold intends to sell the Liverpool property in 2017. At this time he will be resident in Ireland but he is not Irish domiciled. An Irish resident non-domiciled individual is chargeable to Irish CGT on:

1. gains from the disposal of Irish assets and
2. gains remitted to Ireland in the year of assessment on the disposal of foreign assets.

Harold anticipates making a loss of €45,000 on the sale in 2017. As stated above, Ireland only taxes remittances of gains and, therefore, the disposal of the €300,000 proceeds arising from the disposal of loss-making Liverpool asset can be remitted to Ireland tax free.

(2 marks)

(4 marks)

SOLUTION 5

(a) Tax implications of transfers

Transfer of site to Emer

Tax implications for Gerard

Gerard needs to consider his CGT position in respect of the gift. Market value will be imposed. Therefore, his deemed proceeds are €100,000. He acquired the site in 2004 for €15,000. He therefore has a potential capital gain of €85,000 which would expose his to a CGT liability of €28,000 approximately.

The CGT exemption for the transfer of a site to a child cannot be claimed as Emer intends to build a holiday house on the site and not her principle private residence.

(1 mark)

Section 599 TCA 1997 provides for retirement relief (RR) from CGT on the disposal or transfer of qualifying business assets to a child of the disponer, such as Emer, without any limit on the value of assets transferring where the disponer is aged less than 66. Gerard is only 58.

For RR 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 owned for at least 10 years and used for the purposes of the trade continuously throughout the 10 year period. As Gerard has reached 55 years, has held the farm land for in excess of 10 years, RR should be available on the transfer. As a result of RR, no CGT liability should arise for Gerard.

(1 mark)

No VAT needs to be charged as the field is not developed.

Tax implications for Emer

Even though Emer is not Irish resident, she will need to consider CAT and stamp duty in respect of the gift she is receiving.

The gift is within the charge to CAT as Gerard, the disponer, is resident and because the property is situated in Ireland.

Emer will have no CAT to pay but she will be utilising €95,000 of her group A threshold. (€100,000 – SGE €3,000 – SD €2,000)

(1 mark)

In respect of stamp duty, Emer will have to pay stamp duty at a rate of 2%. Therefore, her liability will be €100,000 x 2% = €2,000.

(1 mark)

Transfer of house to Jimmy

Tax implications for Gerard

Gerard should be able to claim principle private residence relief on the disposal so no CGT should be due.

(1 mark)

Tax implications for Jimmy

Jimmy needs to consider his CAT position. He will not be entitled to dwelling house relief as Gerard, the disponer, has been living in the house with him.

As a result of the gift of the house Jimmy will have the following CAT exposure:

Market value	€300,000
Less stamp duty	(€3,000)
	€297,000
Less SGE	(€3,000)
	€294,000
Less Group A threshold	(€225,000)
	€69,000
CAT at 33%	€22,770

(1 mark)

In terms of tax planning, the dwelling house exemption would be available if Gerard does not live in the house with Jimmy for 3 years before the transfer. Therefore, if Gerard moves out and Jimmy continues to occupy the house as his principle residence, the dwelling house exemption should completely alleviate the above CAT liability. The implications for CGT PPR relief need to also be considered.

(1 marks)

In respect of stamp duty, Jimmy will have to pay stamp duty at a rate of 1%. Therefore, his liability will be €300,000 x 1% = €3,000.

(1 mark)

(8 marks)

(b) VAT queries

The VAT registration limit for the sale of gates is €75,000. Therefore, in year 1 Lafferty Gates Ltd (LGL) will not be required to register for VAT. However, when turnover reaches €75,000 in the previous 12 months, LGL will be required to register for VAT. This is likely to happen part way through year 2.

(2 marks)

In terms of purchases, LGL will buy raw materials from VAT registered businesses in Ireland and the UK.

If LGL do not register for VAT in year 1, the VAT position on purchases will be as follows:

- Irish suppliers will charge 23% VAT on their invoices to LGL. LGL will not be able to recover the VAT.
- UK suppliers will charge UK VAT on their invoices to LGL. LGL will not be able to recover the VAT.

(2 marks)

If LGL do register for VAT in year 1, the VAT position on purchases will be as follows:

- Irish suppliers will charge 23% VAT on their invoices to LGL. LGL will be able to recover the VAT in their VAT returns.
- UK suppliers will not charge UK VAT on their invoices to LGL. LGL will provide their UK suppliers with their Irish VAT number. The UK suppliers will then zero rate the invoice as an intercommunity supply. LGL will then account for VAT on the reverse charge basis in their VAT return. As the purchase is of raw materials, the input VAT and output VAT should be the same and there should therefore be no overall cost.

(2 marks)

In terms of sales, in year 1 most of LGL customers will be VAT registered in Ireland and the UK. There will also be some sales to non VAT registered customers in Ireland and the UK. In year 2, he will have sales to the USA.

If LGL do not register for VAT in year 1, no VAT will be charged on their sales to any customers. They will have to register for VAT at some point in year 2. Up to the point in year 2 when they are required to register for VAT, no VAT will be charged on their sales to the USA.

(2 marks)

When they are registered for VAT in Ireland, the VAT position on their sales will be as follows:

- Sales to non-VAT registered customers in Ireland and UK – Irish VAT at 23% will have to be charged. These customers will not have the ability to recover the 23% VAT they are charged and LGL products will become more expensive/less competitive.
- Sales to Irish VAT registered businesses – Irish VAT at 23% should be charged.
- Sales to UK VAT registered businesses – LGL should obtain their customer's UK VAT registration number and then zero rate the invoice as an intracommunity dispatch.
- Sales to USA – as these are exports outside the EU they should be zero rated.

(2 marks)

My advice in respect of whether LGL should register for VAT is that they should register straight away so that they can recover the VAT on their purchases. Most of their customers are VAT registered so LGL's VAT registration will have no financial impact on sales to them. The only customers that will be adversely impacted will be the non-VAT registered customers. However, they are small in number and LGL will be required to register for VAT in the near future anyway.

(2 marks)

(12 marks)