

Chartered Tax Consultant

Stage 2 Applied Tax: Sample Paper 1 & 2



© The Institute of Chartered Accountants in Ireland 2010

Copyright in this sample paper is owned by the Institute of Chartered Accountants in Ireland. All rights reserved. No part of this text may be reproduced or transmitted or communicated to the public in any form or by any means, including photocopying, Internet or e-mail dissemination, without the written permission of the Institute of Chartered Accountants in Ireland. Such written permission must also be obtained before any part of this document is stored in a retrieval system of any nature.

This sample paper is designed to provide accurate and authoritative information in regard to the assessment of Stage 2 of Chartered Tax Consultant. It is provided on the understanding that the Institute of Chartered Accountants in Ireland is not engaged in rendering professional services. The Institute of Chartered Accountants in Ireland disclaims all liability for any reliance placed on the information contained within this publication and recommends that if professional advice or other expert assistance is required, the services of a competent professional should be sought.

Introduction to Stage 2 Applied Tax: Sample Paper 1 & 2

These papers have been written as a sample examination for **Chartered Tax Consultant, Stage 2 Applied Tax**.

Time Allowed

Four hours is the time permitted for each of the two papers examined under Stage 2, Applied Tax. The first thirty minutes of each paper is designated as “reading time” during which the examination paper will be distributed to all candidates. Notes may be made on the examination paper. Once the reading time has elapsed, the Invigilator will distribute the answer books and will announce the start of the examination proper.

Layout

The layout of these sample papers is indicative of the layout for the Chartered Tax Consultant, Stage 2 Applied Tax Examination

- Paper 1 consists of two independent case studies, plus a computational question section consisting of four questions to be answered from a choice of eight questions. A minimum of 40% of available marks must be attained in the computational question section.
- Paper 2 consists of two independent case studies plus a legislation question section consisting of four questions to be answered from a choice of eight questions. A minimum of 40% of available marks must be attained in the legislation question section.
- It is expected that candidates will dedicate a reasonable amount of time to reading and assimilating the information contained in each of the case studies, computational and legislation questions. Candidates wishing to do well will need to pay close attention to the skills of assimilation and analysis of material presented.

Stage 2 Applied Tax

- “Requirements” are given explicitly for each case study, computational question and legislation question in Stage 2. Some requirements are quite directive, but candidates should also be alert for less directive “requirements”. The responses to the Case Studies must be written in a professional manner, and marks will be awarded for providing the report, email, letter etc. as set out in the requirements.

Open Book

This paper is an open book exam. Candidates are permitted to bring any reference material into the examination hall. Candidates are reminded that it is important to be very selective with regard to the material taken into the exam hall, as attempting to look up a lot of material in the examination is likely to be time consuming and unproductive. The value of material is as a referencing tool. The emphasis in the examination will be on application of knowledge and skills, and interpreting the tax legislation and marks will **not** be awarded for direct transcription or close paraphrase of reference material. The marking schemes will reflect this.

Assessment Architecture

The assessment structure, including marks for assignments is as follows:

Form of assessment	Marks	Topic Tested
Assignment 1	15%	Legislation, research skills, professional skills and accounting for tax
Assignment 2	15%	Income Tax and CGT computational Skills & compliance Skills
Exam-Paper 1		
Section 1 Case Study A	11.60%	Income Tax and CGT
Section 2 Case Study B	11.60%	Corporation Tax and VAT
Section 3 Computational Questions (4)	11.60%	IT, CGT, CT, SD, CAT, VAT and Accounting for Tax
Exam-Paper 2		
Section 1 Case Study A	11.60%	CAT/SD and Corporation Tax
Section 2 Case Study B	11.60%	CAT/SD and VAT
Section 3 Legislation Questions (4)	11.60%	TCA 1997, CATCA 2003, VATA 1972, SDCA 1999
Total	100%	

All assessments will examine tax law up to and including FA 2010.

Paper One:

- Complete Case Study A and B questions as detailed and
- Complete only 4 out of 8 computational questions. Only the first 4 questions answered will be marked.

Time Allocation is 4 hours inclusive of 30 minutes reading time.

Section 1

Case Study A: Gilbert Grape

35 marks

It is 20 November 2010. You are a tax senior working for Kelly & Co Accountants. The senior partner, Tim Kelly asks you to drop up to his office as he has a tax assignment he wants your assistance with and he fills you in on the following information.

Tim has long standing clients Gilbert Grape, his brother Henry, and the family company Sideways Ltd. Gilbert and Henry are both Irish born and reared. They set up Sideways Ltd as a wine retailer in 1990 with each owning 50% of the shares in the company.

Over the years the business expanded, particularly as Celtic Tiger palates got more adventurous, to the point where Sideways Ltd opened a chain of shops in Ireland. All of the shop premises are leased by the company and it did not hold any real property.

Gilbert did most of the overseas travel sourcing the wines and spent more and more time abroad on forming a relationship with a French national and citizen called Yvette. From available records in Kelly & Co, Gilbert spent only 25 days in Ireland in 2006, 62 days in 2007 and 41 days in 2008.

On 3 January 2009, Gilbert moved to France on a full time basis on marrying Yvette. He signed a contract to sell his 50% shareholding in Sideways Ltd to Henry for the market value of €1.2 million in June 2009. Based on advice from Kelly & Co, Gilbert did not pay CGT on the transaction and his 2009 personal tax return was filed in November 2009 accordingly.

Since the sale of his shareholding in Sideways Ltd and the filing of his 2009 tax return, Gilbert has not had any dealings with Kelly & Co as he confirmed in writing to the firm that he would look after his own tax affairs.

On a recent trip home to Ireland, Gilbert met with Tim and indicated that he intends moving back to Ireland on a full time basis on 2 December 2010 with Yvette and that he wants Kelly & Co. to look after his tax affairs again.

Stage 2 Applied Tax

Tim is bothered about the tax consequences of a number of transactions Gilbert discussed during the meeting.

Gilbert purchased a warehouse in a retail park off the M50 in January 2009 for €600,000 which he immediately rented to Sideways for €5,000 per month. This is the first Tim has heard of this purchase and while he was aware that Sideways was leasing a warehouse and paying gross rents of €5,000 per month, he had no idea that Gilbert was the landlord.

Tim is equally concerned when he learns that Gilbert sold the warehouse to Henry in June 2010 for a market value of €700,000. Gilbert continued to receive rental income on leasing the warehouse to Sideways Ltd up to May 2010. Gilbert admitted to Tim that neither he nor Henry have considered or dealt with tax obligations associated with the sale of the warehouse but they both want to sort out any issues arising now.

Gilbert purchased shares for €100,000 in an Irish resident company called High Risk Ltd and earned a dividend of €5,100 in March 2010. He also invested €200,000 in Anglo Irish Bank Ltd shares which was subsequently nationalised.

Gilbert has not filed an Irish income tax return or paid any Irish tax since the 2009 tax return prepared on his behalf by Kelly & Co as he assumed that he did not have any Irish tax obligations.

Yvette has substantial personal wealth and would like to tax efficiently bring funds of €500,000 into Ireland when she and Gilbert move back to Ireland for the purposes of purchasing an Irish residence and she would like to use her savings to cover living expenses on making the move to Ireland.

Requirements

Tim asks you to consider the facts presented above and revert to him with a memo detailing the following tax technical issues as specified in 1 to 6 below. He does not require any computations at this stage but requires full legislative references and case law references where relevant to support your findings:

1. Tim can't locate Gilbert's 2009 tax file. Can you provide an explanation as to why Kelly & Co advised him that no CGT was payable on the sale of Sideways Ltd? Does Gilbert's proposal to return to Ireland in December 2010 present any CGT difficulties in respect of the sale of Sideways Ltd share stating reasons for your conclusion?

8 marks

Sample Paper 1

2. What are the Irish CGT consequences for Gilbert and Henry on the sale of the warehouse if they have not complied with any tax obligations associated with the sale?
6 marks
 3. What are the Irish CGT consequences for Gilbert arising out of the nationalisation of Anglo Irish Bank shares and can Gilbert use this loss for tax purposes?
3 marks
 4. What are the Irish income tax issues relevant to Gilbert and Sideways Ltd in relation to the Irish rental property if both parties have not complied with tax obligations? Does Gilbert have an Irish tax obligation on the dividend he received from High Risk Ltd, stating reasons for your answer?
5 marks
 5. What interest and penalty exposures may Gilbert incur for income tax purposes on rents paid by Sideways and dividend from High Risk Ltd, if any?
3 marks
 6. What will be Yvette's tax status on moving to Ireland in the tax year 2011, stating legislation and case law to support your answer?
4 marks
 7. How can Yvette tax efficiently bring her savings into Ireland?
4 marks
- Professional presentation **2 marks**
Total **35 marks**

Section 2

Case Study B: Pharma Ireland Ltd

35 marks

You are the recently appointed in-house tax executive of Pharma Ireland Limited (Pharma Ire). Pharma Ire is an Irish-incorporated fully owned subsidiary of Pharma Global Inc (Pharma Inc). The Irish operation manufactures and distributes pharmaceutical products from its plants in Leitrim and Sligo. You report to the head of Global Tax Operations, Chad Marsh, who is based in California.

It is 20 October 2010. Chad skypes you with a number of tax issues he wants you to look into based on the following information.

A recent detailed analysis of Pharma Ire's R&D activities carried out by experts uncovered additional qualifying but unclaimed expenditure of €300,000 in respect of the year ended

Stage 2 Applied Tax

30 November 2009. The original R&D expenditure in 2009 was calculated as €250,000 and this was the sum reflected in the company's tax return for 2009. Pharma Ire was formed on 1 November 2007 and its R&D activities in Ireland for its first year of trading culminated in an initial qualifying R&D spend of €500,000.

Qualifying expenditure on R&D activities incurred by Pharma Ire in 2010 is €250,000, plus qualifying expenditure of €500,000 on R&D carried out in a Northern Ireland branch of Pharma Ire located in Fermanagh.

Pharma Ire is considering investing €5,000,000 in 2012 in a state-of-the-art new research facility in Leitrim to be used exclusively for R&D activities. Enterprise Ireland will provide a grant of €1 million towards the total cost of €5,000,000. Pharma intend spending €100,000 on the acquisition of registered designs and €75,000 on authorisations to sell certain medicines to complement the products to be developed in the new R&D centre. Pharma Ire's amortisation policy for intangible assets is set on a straight-line basis over 10 years.

Chad has the trading results and tax liabilities of Pharma Ire to hand and gives you the following information during the Skype link:

- Year ended 30 November 2009 – trading profits of €1,500,000; corporation tax paid of €137,500.
- Year ended 30 November 2010 – projected trading losses of €50,000. PAYE projected to cost €550,000.
- Year ending 30 November 2011 – projected trading profit of €800,000; corporation tax projected €75,000.

In January 2010, a staff canteen was introduced at the Sligo facility. All meals are free and the monthly cost of the facility is €10,000. VAT of €13,500 has been reclaimed up to the September/October VAT3 in 2010 on these canteen running costs. Chad says that the VAT entitlement has not been properly considered and he is now having second thoughts on if VAT should indeed be reclaimed.

An important part of a key machine broke down and was shipped to the UK to be repaired. The UK repair company charged VAT of STG&50,250, and Chad was told all he needed to do was convert that back into euro and reclaim it through the VAT3. Chad isn't sure if that is correct and hasn't done anything about it yet but wants to know how he gets the VAT back.

Sample Paper 1

Chad tells you that Pharma Ire has made an offer to acquire the trade and assets of an Irish business for €10 million. The target business has lucrative drug development prospects and valuable intangible assets such as goodwill, brands and licence agreements.

The vendors have included VAT of €2,100,000 on the draft sales contract and justified this on the basis that they want to claim back VAT on the legal fees arising on the sale of the business. Pharma Ire's legal advisors have recommended that the VAT treatment of the purchase be fully considered before advancing the acquisition.

Chad is considering the merits of centralising the license agreements of the target business into a new company once the purchase is complete. The licence agreements are well established and will require minimal input from the management team and Chad envisages that only one or two administrative personnel are required to work for the company to ensure that the terms of the licence agreements are all fulfilled i.e. payments are made on time and that the correct paper work is in order.

Requirements

Chad wants an email response to the Irish tax issues as outlined in 1 to 7 below. He would like to discuss your conclusions with Pharma Ire's tax advisors and on that basis he wants all of your analysis supported with full legislative references, and case law where relevant.

1. What are the tax implications for Pharma Ire in making an additional claim for R&D expenditure for 2009?

3 Marks

2. Calculate Pharma Ire's 2010 R&D tax credit and state how this credit can be tax efficiently used?

5 Marks

3. What tax relief entitlement will Pharma Ire have in respect of the proposed expenditure on the new R&D centre in Leitrim in 2012 and explain the basis for your conclusion?

6 Marks

4. Is the VAT claim for the canteen expenditure correct? Explain your position to Chad

4 Marks

5. Advise Chad on how the UK VAT on the equipment repair work should correctly be dealt with?

4 Marks

Stage 2 Applied Tax

6. What are the VAT implications for Pharma Ire on the proposed acquisition of the business and assets as set out in the draft sales contract?
7 Marks
7. How will profits in the new licence holding company be treated for corporation tax purposes? Support your conclusion with case law.
4 Marks
- Professional presentation and skills **2 Marks**
- Total 35 Marks**

Section 3

Computational Questions

35 Marks

Answer 4 out of a choice of 8 questions. Candidates must achieve a minimum of 40% of the available marks for the four questions answered. Only the first 4 questions answered will be marked.

Question 1:

- (a) On 30 September 2010, Sean Murphy sold his house and garden (0.5 acres) in Blackrock, Co Dublin for €650,000 (current use value). He inherited the house from his aunt on 1 May 1982 when its market value was €200,000.

He lived in the house with his wife until 30 June 1991 when they left to tour Australia and New Zealand not returning until 31 December 1992. On their return, they lived in the house until his wife's death on 28 February 2005 when Sean moved into his sister's house and has lived with her since then.

Required:

Calculate Sean's CGT liability on the disposal of his property in Blackrock.

- (b) John and Mary O'Shea are a married couple, jointly assessed and both Irish tax resident. During 2010, they had the following capital transactions:
- (1) On 15th January, Mary sold an antique painting for €30,000. She inherited this painting from her aunt in December 1998, at which time it was valued by a professional valuer at €1,950.
- (2) Mary has unused capital losses of €10,000 carried forward from 2006.

Required:

Calculate John & Mary O'Shea's CGT liability for the 2010 tax year.

8.75 Marks

Question 2

It is January 2011. You have been asked to look at the recent VAT returns for Disaster Insurance Ltd to see if VAT has been calculated correctly. The following is relevant:

- As it is partly exempt, it has had an average recovery rate of 20% for VAT purposes since it started trading 3 years ago. This recovery rate was agreed with Revenue in 2008 based on the percentage of VATable turnover to exempt turnover. In 2009, the VATable element of the business has grown to 25%. Total VAT incurred in 2009 was €100,000 and in 2010 it was €80,000. You can assume there is little or no "directly attributable" VAT i.e. VAT on goods or services specific to the VATable or exempt portion of the business.
- In early 2010, invoices were received from a solicitor's firm in London for professional advice. The invoices when converted to Euro amounted to €60,000 but had no VAT on them. Nothing has been done about this.
- They have reclaimed the appropriate portion of VAT on all petrol and diesel costs since the company started trading. On average, the recoverable element of VAT was €2,000 per annum based on 20% recovery. Approximately 50% of the cars are run on diesel and 50% are run on petrol.

Required:

Calculate any VAT adjustments needed for the three year period to December 2010.

8.75 Marks

Question 3

Pins & Needles Limited is an Irish resident company engaged in the retail sale of sewing materials.

Stage 2 Applied Tax

The company's key results for the years ended 31 December 2009 and 2010 were as follows:

	2009	2010
	€	€
Sch D Case I profit/(loss)	(150,000)	35,000
Sch D Case III	15,000	10,000
Sch D Case IV	5,000	2,000
Sch D Case V	22,000	20,000
Sch D Case V capital allowances	(7,000)	(7,000)

Other details:

On 7 July 2010, it disposed of a site for €550,000 (current use value €350,000). It purchased the site in May 2000 for €180,000 (current use value €120,000) with the intention of constructing a new store. However, this proposal was never finalised and a decision was made to dispose of the site. Incidental costs of acquisition and disposal were €20,000 and €50,000 respectively.

Required:

- Calculate the company's corporation tax liabilities for the years ended 31 December 2009 and 2010.
- Calculate the company's CGT liability for the year ended 31 December 2010.

8.75 Marks

Question 4

Mary Murphy, a solicitor friend, contacts you on 23 December 2010 in relation to the following transactions that recently took place in relation to her client, Nora Norris:

- On 1 July 2010, Nora received a gift of a house in Kilkenny from her aunt valued at €180,000 in return for her paying her aunt €50,000. This is the first house that she has owned and she occupies it as her principal place of residence on taking the gift of the house. Her aunt did not have a CGT liability on this disposal due to capital losses carried forward from previous years.
- Nora bought six acres of farmland with development potential in Co. Meath for €60,000 from her two brothers who owned the land in equal shares on 1 October. The market value of the land is €66,000.

Mary has also advised you of the following:

- Nora is single and is resident and domiciled in Ireland.
- Details of previous gifts and inheritances received by Nora:

Date	Detail	Taxable Value €
4 June 2006	Inheritance of shares from uncle	30,000
10 April 2007	Gift of cash from cousin	20,000
18 July 2009	Inheritance of unit from father	250,000

She has not paid CAT in respect of previous gifts or inheritances.

Required:

- (a) Calculate Nora’s CAT and SD liabilities in relation to transactions (i) and (ii).
- (b) What are Nora’s exposures for late payment of taxes.

8.75 Marks

Question 5

Sean, aged 54 and a widower, ceased practising as a self-employed solicitor on 30 June 2010.

His tax adjusted profits (before capital allowances) were as follows:

Year ended	€
30 April 2008	95,000
30 April 2009	90,000
30 April 2010	80,000
2 months ended 30 June 2010	5,000

Details of his fixed assets (owned outright) are as follows:

Asset	Date of Purchase	Cost €	Tax WDV @ 1 Jan’ 10 €	Market value @ 30 June’ 10 €
Fixtures & Fittings	Aug 2006	10,000	6,250	7,000
Computer Equip.	Oct 2007	3,000	2,250	2,000
Motor Car	Jan 2008	28,000	18,000	24,000

All assets were used entirely for business purposes but ceased to be used by him for the purposes of his business a few weeks prior to the cessation of his legal practice.

Stage 2 Applied Tax

Details of his other income and expenditure for the 2010 tax year are as follows:

Note	€
Irish deposit interest (net)	1,500
UK rental income	4,000
Qualifying medical expenses	1,000

Required:

Calculate Sean's income tax, PRSI and levies liability for 2010 and any adjustments required for 2009.

8.75 Marks

Question 6

Tim Turner has asked you to consider the following property transactions:

Unit 1

Tim acquired Unit 1 in January 2010 from Beta Ltd. Unit 1 is a factory which was built in January 1993 by Beta Ltd. The cost of the basic building construction was approximately €3.2m. The unit is 40,000 square foot which includes 3,500 square foot of office space. No VAT was charged when Tim acquired the building from Beta Ltd which is now leased to a tenant engaged in manufacturing activities.

Unit 2

Unit 2 is a warehouse purchased by a company Tim owns, Turner Enterprises Ltd. The warehouse was purchased from a builder for €2 million inclusive of VAT of €250,000, shortly after it was built in January 2009. The land element was €400,000 and the developer's construction cost was €1.2 million. Turner Enterprises is engaged in manufacturing activities and has 80% VAT recovery.

Unit 3

This premises was built in January 2010 at a cost of €8 million excluding VAT. The purchase price reflected a site valuation of €1 million. The premises have never been occupied and Tim, having owned it since February 2010, sold it for €10 million in December 2010.

Required:

- (a) Calculate the Industrial Building Annual Allowance available for the year ended 31 December 2010 for all of the above units.

(b) Tim asks you to calculate any other taxes arising on the sale of Unit 3

8.75 Marks

Question 7

During the year ended 31 December 2010, John Jones was engaged in the following share transactions:

- (i) Under the terms of his employer's (Delta Ltd) unapproved share option scheme, he exercised options on 28 February 2010 and acquired shares in Delta Ltd with a market value of €20,000 for €11,000.
- (ii) In May 2010, he sold his Delta Ltd shares for €24,000.
- (iii) On 1 November, he sold 2,000 shares in High Return Ltd for €30,000. He purchased 1,500 High Return shares in May 1997 for €1,500 and received the remaining 500 shares as a bonus issue in October 2001.
- (iv) On 15 December, he received a gift of 100 shares in Steady Return Ltd from his father in law valued at €15,000. He still holds these shares.

He has also advised you of the following:

He is single and is resident and domiciled in Ireland. He is a higher rate income tax payer.

Details of previous gifts and inheritances received by him:

Date	Detail	Market Value €
10 April 2007	Gift of cash from cousin	20,000
18 July 2009	Inheritance from father	250,000

He has not paid CAT in respect of previous gifts or inheritances.

He has unused capital losses carried forward of €15,000 arising from disposals of assets in prior years.

Required:

Calculate the taxes due under transactions (i) to (iv).

8.75 Marks

Question 8

Sean Smith, a landlord, engaged in the following transaction in 2010.

Stage 2 Applied Tax

On 1 May 2010, he granted a lease of an office premises to a third party tenant with full VAT recovery. The office, which is newly completed, has never been let before and was acquired by Sean on 1 January for €500,000 including VAT of €60,000. He has borrowings for the purchase of the property of €400,000 on which interest of €1,000 per month was paid. Sean granted the 21 year lease for an annual rent of €30,000 payable every quarter. Sean opted to tax the lease for VAT purposes.

Required:

Calculate all taxes payable by Sean in 2010 on the acquisition of the property and the creation of the lease.

8.75 Marks

Paper Two:

- Complete Case Study A and B questions as detailed and
- Complete only 4 out of 8 legislative questions.

Time allocation is 4 hours inclusive of 30 minutes reading time

Section 1

Case Study A: Seamus and Lucia Delaney

35 Marks

You are a tax senior in a firm of chartered accountants called Mulcahy & Co in Tralee. You recently met with one of the firm's clients Seamus Delaney on 3 November 2010.

Seamus is married to Lucia who is originally from Portugal but has lived in Ireland on a full time basis since marrying Seamus in June 2007. Lucia has maintained her Portuguese citizenship and continues to own a residential property in Portugal which she and Seamus regularly visit on vacation for two weeks every year.

Seamus is a 100% shareholder and director of Delaney Developments Ltd (DDL) which in turn holds 100% of the shares in Delaney Buildings Ltd (DBL). DDL has a trade of dealing in land which is not fully developed in the South West region. DBL trades as a property construction company which generally buys the semi-developed land from DDL and carries out construction of residential property which it in turn sells to the general public.

To cut professional costs Seamus took over the company's corporation tax compliance function and uses Mulcahy & Co to trouble shoot issues as they arise.

Seamus has the following information to hand at the meeting:

	DDL	DBL
Year ended 30 September 2009	€'000	€'000
Case I adjusted Profit / (Loss)	(200)	350
Interest paid in year ended 30 September 2009	50	
Year ended 30 September 2010	€'000	€'000
Case I adjusted Profit / (Loss)	100	(300)
Interest paid in year ended 30 September 2010	20	

The interest detailed above refers to bank borrowing undertaken by DDL to lend working capital of €650,000 to DBL. DDL has not received any repayments from DBL since making the initial loan funds available. However from 1 December 2010, DBL will start making interest payments to DDL to help it service the bank borrowing and it will also make a capital repayment of €150,000.

During your meeting Seamus tells you that he has not filed a form CT1 or paid any tax for DDL or DBL for 2009 or 2010. Seamus is aware that the companies may incur interest and penalties and is anxious to structure the use of tax losses between the companies to minimise the interest and penalty exposure.

Lucia runs a company called Bakery Delights Ltd which was formed on 7 January 2010. The company trades as a bakery and pastry shop with a 31 December year end. The company is projected to make tax adjusted profits of €250,000 for the year ending 31 December 2010. Seamus also looks after the corporation tax compliance for Bakery Delights Ltd but to date he has not considered the tax position for the company.

DDL and DBL are in financial difficulty and Seamus and Lucia are also in personal financial difficulty. Their position is so dire that they have resorted to seeking financial assistance from their friends and family over the last year to stay solvent as follows:

1. On 1 April 2010, Seamus' father gifted him an apartment in Belfast. On the date of the gift the apartment was worth €150,000. The value of the apartment fell from the date of purchase so Seamus' father did not have to pay any CGT on the gift. The deed

Stage 2 Applied Tax

of transfer was executed by Seamus' legal advisors in Tralee. No tax has been paid by Seamus on this transfer.

2. On 1 August 2010, his sister transferred a commercial unit into their joint ownership in exchange for €50,000. On the date of the transfer, the value of the share in the property transferred to Seamus was €200,000 but the deed transferring the 50% share in the property refers to a value of €100,000. No tax has been paid by Seamus on this transfer but he wants the necessary tax calculations to be based on the value reflected on the deed.
3. Lucia inherited a cottage from her elderly neighbour in Tralee who she had formed a close friendship with on moving to the area. The property was valued at €330,000 on the date of the neighbour's death on 3 February 2010 and recent correspondence from the executor says grant of probate issued on 5 October 2010 with a valuation placed on the property on that date of €300,000.

Seamus has confirmed that neither he nor Lucia have received any gifts or inheritances in the past.

DBL completed a small residential development on the outskirts of Tralee and Seamus wants to include the stamp duty costs for potential purchasers as part of the marketing brochure he is in the process of putting together. He provides you with the following information:

- Development consists of 10 units between 38 and 125 sq metres priced at €185,000 and 10 units larger than 125 sq metres priced at €250,000 each.
- One contract will be used to convey each property?
- The target market for this development is first time buyers and owner occupiers so the marketing campaign will be focused on attracting these purchasers.

As a result of receiving financial assistance from friends and family, and DBL finally completing the development in Tralee, Seamus has reached an agreement with the bank to re-structure his personal borrowings and the corporate borrowings. The bank wants a report on the Delaney's personal tax position and that of the companies as additional borrowings will be made available to clear the tax liabilities.

Requirement

With the above information in mind, Seamus asks you to prepare a report on his behalf addressing issues 1 to 5 outlined below. He says the bank wants full legislative references

Sample Paper 2

and case law where relevant. Seamus also wants advice on the stamp duty implications of the development for the marketing brochure as outlined in 6 below.

1. Based on the information provided, explain how DDL and DBL can tax efficiently bring their corporation tax affairs in order. Highlight tax payment obligations and support your explanation with calculations.
10 marks
 2. What are the tax implications for DDL and DBL on entering into the new interest payments and capital repayment arrangement from 1 December 2010?
4 marks
 3. What is Bakery Delights Ltd's corporation tax position for the year ending 31 December 2010, commenting on any available Reliefs?
3 marks
 4. Calculate the CAT and Stamp Duty liabilities, if any, arising on each of the gifts received by Seamus and provide an explanation for your calculations.
6 marks
 5. What is Lucia's tax status for Irish CAT purposes in relation to the inheritance and calculate CAT, if any, arising on the benefit?
5 marks
 6. Explain the Stamp Duty implications for first time buyers and owner occupiers of the residential development in Tralee?
5 marks
- Marks for professional presentation **2 marks**
- 35 marks**

Section 2

Case Study B: The Trotters

35 Marks

You are a chartered tax consultant working in practice. It is 14 October 2010. Your colleague Jill Mathews asks for your help on some issues arising on an assignment in relation to clients of the firm, Derry and Roger Trotter. She has told you that she is comfortable with the CGT and Income Tax issues relevant to the assignment but would like you to take a look at the VAT, CAT and Stamp Duty issues. She fills you in on the key facts, as follows:

Derry Trotter is 60 years old. He is married and has lived and worked in Dublin all of his life. Derry's brother Roger relocated to the south of Spain in January 2009 where he

Stage 2 Applied Tax

bought a villa on the Costa Blanca for €2,000,000 in early 2009, but its value has fallen significantly and it was valued at €1,250,000 in July 2010.

Roger and his family are home sick and want to move back to Dublin. Roger retained his home in Rathfarnham, but was on the look out for a business venture in Dublin he could run on moving back to Ireland.

By coincidence, Derry and his wife wanted to relocate to Spain but they could not find a property as perfect as Roger's villa.

The two brothers came to an agreement, which appeared to satisfy both of their objectives as follows:

Derry owned a commercial property which he acquired in a dilapidated condition for €500,000 in 2004. He carried out a refurbishment on the property in October 2008, at a cost of €450,000 net of VAT having reclaimed VAT of €70,000 on the refurbishment. The property was vacated in May 2010 having been rented under a 12 month lease subject to VAT up to then. The property was valued at €1,500,000 in June 2010, but it was mortgaged for €1,000,000.

Roger liked the property and its prospects. Therefore, Derry transferred it to Roger along with the mortgage of €1,000,000. The document of transfer was signed in Dublin on 2 June 2010.

Derry also owned 100% of Trotters Ltd, an Irish company which trades in the salvage business. Again Roger felt that the company had good prospects. Therefore he gave Derry a life interest in his Spanish villa for a consideration of 60% of the shares in Trotters Ltd which were valued at €500,000 on the date of the transfer. The document of transfer for the Spanish villa to Derry was signed in Spain on 15 July 2010.

Derry incurred legal fees of €10,000 on the acquisition of the villa, while Roger incurred legal fees of €18,000 on the acquisition of the commercial property.

Jill confirms that neither Derry nor Roger have received gifts or inheritances in the past.

Both Derry and Roger have up to now ignored all of the tax issues associated with the transfers and have engaged Jill to work out the Irish tax issues on their behalf.

In addition Jill has been asked to look at some post acquisition issues which she outlines as follows:

Since taking ownership of the commercial property in June, Roger has sourced a tenant who is interested in taking on a ten year lease of the property. The prospective tenant is

an insurance company who wants to take up the lease from 1 December 2010 for a rent of €50,000 per annum. However, the insurance company is reluctant to pay any VAT although it does have an 80% VAT recovery rate.

Roger has asked Jill to advise him on what he should do about VAT, if any, arising on the transfer from Derry and subsequent lease of the commercial property.

Derry is considering gifting the family home in Rathgar to his adult son Darren (his only child) who has lived in the house with his parents all his life. The house is valued at €900,000. Jill is satisfied that there are no CGT issues for Derry as the property is his principal private residence but she wants your input on CAT and Stamp Duty implications and in particular on the availability of any reliefs for Darren on the proposed transfer.

The Spanish lawyer representing Derry in the transfer of the Spanish villa has charged Spanish VAT of €3,400 on the invoice dated August 2010 for services rendered. Derry wants to know if he should have been charged for Spanish VAT.

Requirement

Jill asks you to consider the facts of the case as she has outlined above and to provide her with an email quoting all relevant legislation and computations addressing the following issues:

1. What Stamp Duty implications arise for Derry and Roger in respect of the transfers on 2 June and 15 July 2010? Provide Jill with calculations and outline payment obligations for any Stamp Duty arising
10 Marks
2. What CAT implications arise for Derry and Roger in respect of the transfers on 2 June and 15 July 2010? Provide Jill with calculations and outline payment obligations for any CAT arising
5 Marks
3. What VAT issues arise on the transfer of the commercial property from Derry to Roger?
6 Marks
4. What VAT issues arise for Roger on entering into the new leasehold arrangement with the insurance company, identifying any opportunities to minimise tax?
6 Marks

Stage 2 Applied Tax

5. Discuss Darren's CAT and Stamp Duty obligations on the proposed gift of his parents home focusing on the availability of any reliefs to minimise tax on the transfer?

3 Marks

6. Was the Spanish lawyer correct in charging Derry VAT on the invoice for services rendered in respect of the swap of the Spanish villa? Support your conclusion with reasons and legislative references.

4 Marks

Professional Presentation

1 Mark

Total Marks

35 Marks

Section 3

Legislative questions

35 Marks

Answer 4 out of a choice of 8 questions. Only the first 4 questions answered will be marked. Candidates must achieve a minimum of 40% of the available marks for the four questions answered. Full legislative reference must be given.

Question 1

- 1.1 State the full legislative reference restricting interest relief in the calculation of rental profits on certain properties?
- 1.2 What is the full legislative reference which provides for the treatment of qualifying interest against non-Irish rental properties?
- 1.3 Separate assessment is an option open to a married couple. State the legislative provision which allows for this treatment and state the date that the claim must be made to apply this treatment for a year of assessment?
- 1.4 Which section provides for Benefit In Kind (BIK) in relation to a van? What is the rate of BIK and the related legislative reference?

8.75 Marks

Question 2

What is the Irish VAT rate applicable to each of the following four supplies and what is the appropriate legislative reference?

- 2.1 General accountancy services received by a company in Dublin from a firm in Belfast.

- 2.2 Transfer of a pub licence as part of transfer of a business as a going concern.
- 2.3 GP surgery fees.
- 2.4 Sales of crutches.

8.75 Marks

Question 3

- 3.1 If I make a disposal of an asset to my brother, can we pick whatever value we like for CGT purposes? Support your answer with relevant legislation reference. What is the tax technical term for the relationship between my brother and I, and where is it defined in TCA 1997?
- 3.2 I receive payment under an insurance policy for destruction of a capital asset. Is that sum liable to CGT? Support your answer with the relevant legislation reference?
- 3.3 I hold Anglo Irish Bank shares that are now virtually worthless and I want to offset the loss on the shares against other gains but I can't realise the loss as I can't find a buyer. Can I offset the loss against other gains? Support your answer with the relevant legislative reference.
- 3.4 Is interest an allowable deduction for CGT purposes, noting any exceptions to the general rule and support your answer with legislative references?

8.75 Marks

Question 4

- 4.1 State the provision that determines the events that cause an accounting period of a company to end? How many possible events are listed in that subsection?
- 4.2 Where does it state in TCA 1997 that income tax principles may be used in computing income for corporation tax purposes?
- 4.3 Must you use either GAAP or IFRS for corporation tax purposes? Support your answer with legislative references.
- 4.4 In the period in which it ceases to trade, a company incurred trading losses which can't be used in that period and can't be carried forward. Can anything else be done to utilise those losses? Support your answer with legislative references?

8.75 Marks

Stage 2 Applied Tax

Question 5

- 5.1 A client has financial difficulties and can't pay an upfront CAT liability arising on an inheritance. Is there any provision in the CAT legislation that will enable him to pay the tax in stages? If so, state the provision. What is the disadvantage of not clearing the CAT liability as an upfront payment?
- 5.2 The first €3,000 of a gift from a donor in a tax year is exempt. What is the relevant statutory provision?
- 5.3 "wherever executed, relates to any property situate in the State". Where is this key phrase to be found in SDCA 1999? What is its significance?
- 5.4 If a document is not stamped in time and/or insufficient stamp duty is paid, what are the implications for late payment? Use legislative references to support your answer?

8.75 Marks

Question 6

- 6.1 What is the precise statutory provision that imposes an income tax charge on any gain realised by a director or employee from a right granted to him/her, by reason of his/her office or employment, to acquire shares or other assets in a company?
- 6.2 Is there an obligation to file a personal tax return on the exercise of a share option, use legislation to support your answer?
- 6.3 What exact provision in the legislation states the payment dates for CGT liabilities for an individual?
- 6.4 State the exact provision which stipulates the rate of tax to be withheld by a purchaser if a CG50 clearance certificate is not provided by the vendor?

8.75 Marks

Question 7

- 7.1 You are Irish resident and ordinarily resident but non-Irish domiciled and you want to use loans in place of directly remitting funds from the UK to Ireland. What are the implications of this proposal? Use legislation to support your answer.
- 7.2 You have a big capital gain on a property you disposed of and don't want to pay the CGT. You have no losses to shelter it. A guy in the pub suggested that you sell

shares you bought some time ago to trigger a big loss and then buy them back again a couple of days later and wait for them to recover. All you've done really is incur transaction costs and you've also managed to shelter the gain. What are the implications to this proposal, using legislation to support your answer?

7.3 It is May 2010. You have an undeveloped site and a builder approaches you. He said that it is possible to avoid VAT on the sale of a house for €250,000 if the site is sold for €100,000 separately from the building works. He's happy to split the 13.5% VAT saving with you. You know that sales of undeveloped land are not liable to VAT and this seems a clever way to ensure that no VAT need arise on this site. Will this proposal work? Support your answer with legislation?

7.4 State the relevant section of the legislation which deals with the scope of the charge to Irish CAT on a gifts received by non-domiciled individuals from 1 December 1999.

8.75 Marks

Question 8

8.1 Kevin sells an office block to Mr Smith in consideration of cash plus the transfer of the mortgage on the office block to Mr Smith. How will this arrangement be treated for Stamp Duty purposes? State legislation to support your conclusion

8.2 A property is sold for €500,000 including VAT of €60,000. What figure is stamp duty chargeable on? What is the relevant statutory provision?

8.3 Property is leased for €50,000 per annum plus VAT at 21%. The lease is for a term of 40 years. What figure is liable to stamp duty and at what rate?

8.4 A residential property is supplied by the property developer. Is the supply subject to VAT? What is the relevant statutory provision?

8.75 Marks

Sample Paper 1 Solutions

Please note, solutions have been written to achieve the highest possible standard

Section 1

Case Study A: Solution

Memo

To: Tim Kelly

From: Laura Noonan

Date: 24 November 2010

Subject: Gilbert Grape's tax issues

Tim

As requested, I set out below my analysis of the tax issues you presented to me at our recent meeting, as follows:

1. Why did we advise Gilbert that no CGT was payable on the sale of his Sideways Ltd shareholding and does Gilbert's proposed return present any CGT difficulties?

Gilbert was non Irish tax resident and non-ordinarily tax resident in Ireland in 2009 in accordance with the information available on our records as he was non resident in 2006, 2007 and 2008. He became non-ordinarily resident in 2009 having spent three consecutive tax years non-resident in accordance with the provisions of **section 820(2) TCA 1997**.

Under **section 29 (3) TCA 1997**, an individual who is non-resident and non-ordinarily resident is not liable to Irish CGT on the disposal of assets unless such assets are Irish specified assets. The shares in Sideways Ltd are not Irish specified assets as they do not appear to derive the greater part of their value from Irish property as provided for under **section 29(1) TCA 1997**. I have reached this conclusion based on the information that Sideways Ltd does not own any freehold interest in property having leased all its premises and rented the warehouse from Gilbert.

Therefore Kelly & Co correctly advised Gilbert that he was not within the charge to Irish CGT on the disposal of his shareholding in Sideways Ltd.

I note that Gilbert intends returning to live in Ireland on a full time basis on 2 December 2010. I have reviewed the implications for Gilbert on returning to Ireland on this date under

Sample Paper 1 Solutions

the provisions of **section 29A TCA 1997** referred to as Temporary Non-Residents anti-avoidance legislation. This section applies where an Irish domiciled individual disposes of certain assets, while outside the charge to Irish CGT. The assets, known as relevant assets, are a holding in a company, the value of which is either 5% or more of the value of that company or €500,000. The shares in Sideways Ltd are relevant assets as defined. Under **section 29A TCA 1997**, the individual is deemed to have disposed of, and reacquired, the shares at their market value at the end of the year in which he “temporarily” leaves the State, with that gain falling due and taxable in the year in which he returns and resumes his residence. It applies to an individual who:

- is/was Irish resident and domiciled; and
- cease Irish residence in 2003 or thereafter; and
- is non-resident in Ireland for a period of not more than five years; and
- return and resume their Irish resident status.

Applying those rules to these facts, Gilbert will have spent an intervening period of more than 5 years tax resident outside of Ireland as his last year of tax residence was 2005 and he will not become Irish resident again until 2011. Therefore, his proposed return in December 2010 will not trigger the temporary non-resident rules.

2. What are the Irish CGT consequences for Gilbert and Henry on the sale of the warehouse?

The disposal of the warehouse in June 2010 is within the charge of Irish CGT under **section 29(3)(a) TCA 1997** even though Gilbert is neither resident nor ordinarily resident in Ireland in 2010 as the warehouse is a specified asset under this section and therefore the gain arising on the disposal is subject to Irish CGT.

The disposal also comes within the provisions of **section 980 TCA 1997** which imposes an obligation on a purchaser to withhold 15% of the total sale proceeds on the sale of certain assets and pay it over to the Revenue within 30 days of payment of the consideration for the asset. Interest will run and be charged on the purchaser if the tax is not paid by the due date.

The requirement to deduct tax from the sales proceeds applies only to particular assets as outlined under **section 980(2) TCA 1997** where the consideration for the disposal exceeds €500,000. The assets to which the withholding tax applies includes Irish property such as the warehouse disposal by Gilbert.

Stage 2 Applied Tax

Therefore Henry should have withheld 15% of the sales proceeds, in this case €105,000 and he should have paid this to Revenue within 30 days of the transaction closing. By not doing so, Henry is now exposed to interest from the date he acquired the warehouse from Gilbert.

Tax does not have to be withheld by the purchaser of an asset to which **section 980 TCA 1997** applies where the vendor is able to produce a tax clearance certificate known as CG50 clearance from Revenue authorising the payments to be made in full. A non-resident person will receive such a certificate only where:

- he has satisfied Revenue that he has no liability, or
- he has actually calculated, agreed and discharged the CGT liability arising to Revenue or
- if an Irish resident solicitor undertakes to pay any tax due out of the sales proceeds.

We therefore must confirm with Gilbert and Henry if CG50 clearance issued and if not, then Henry must be made aware of the exposure to interest on failure to operate the 15% withholding tax.

I note that Gilbert confirmed during his recent meeting with you that he has not paid any tax in Ireland since moving to France. However, he is obliged to pay the CGT arising on the disposal of the warehouse by 15 December 2010. I provisionally calculate the gain to be €100,000 subject to CGT at 25% which gives rise to a tax liability of €25,000. We will require full details of the stamp duty incurred on acquisition along with other incidental costs of acquisition and disposal incurred by Gilbert, in order to prepare a complete CGT computation on this disposal. Gilbert should pay the CGT liability as soon as possible to limit his exposure to interest on late payment.

3. What are the implications of the nationalisation of Anglo Irish Bank Ltd for Gilbert and can he use this loss for tax purposes?

Revenue declared in eBrief 76/09 that a negligible value claim under **section 538 TCA 1997** was available on the nationalisation of Anglo Irish Bank in 2009. This means that shareholders could realise the loss arising on the difference between what they originally paid for the shares and what the shares were worth on nationalisation.

However as a non-resident and non-ordinarily resident individual in 2009, under the provisions of **section 546(4) TCA 1997**, Gilbert is only allowed to claim a loss on the disposal of an asset if it were the case that, had a gain arisen, the gain would have been a

chargeable gain. As Anglo Irish Bank Ltd shares are not specified assets, then a gain on the disposal of these assets by Gilbert in 2009 would not have been chargeable to Irish CGT. As a result, the loss is not allowable in 2010 against the gain on the warehouse disposal. Gilbert should delay making a negligible value claim until he is within the charge to Irish CGT (i.e. when he becomes Irish resident), which I estimate to be 2011, and then realise the loss for offset against other gains in the year the claim is made or for carry forward for offset in subsequent years.

4. Outline of Irish income tax issues in relation to rents received by Gilbert from Sideways Ltd, and Gilbert's obligations in respect of the dividend from High Risk Ltd?

Gilbert is non-resident and non-ordinarily resident in Ireland in 2009 and 2010. However, he is still within the charge to Irish income tax under **section 18(1)(a)(iii) TCA 1997** in respect of Case V income arising on Irish rental property. Therefore, Gilbert is chargeable to Irish income tax in 2009 and 2010 in respect of rents on the lease of the warehouse to Sideways Ltd.

I note that you were not aware that Sideways Ltd was paying rents to a non-resident landlord and that gross rents of €5,000 were paid each month by the company.

Under **section 1041 TCA 1997**, rents paid to a non-resident landlord are subject to special rules which may also have implications for Sideways Ltd as the tenant. Under the provisions of **section 1041 TCA 1997** a tenant is obliged to apply withholding tax at the rate of 20% on rents payable to non-resident landlords and pay the sums withheld directly to Revenue. If the tenant fails to apply withholding tax then the tenant maybe liable to the 20% tax and will be exposed to interest for failure to operate withholding tax. As an alternative to the tenant operating withholding tax, the landlord may appoint a tax resident agent to collect the rents from the tenant and to be assessable on the Case V income on behalf of the landlord.

The dividend Gilbert received from High Risk Ltd in 2010 is not chargeable to Irish income tax under **section 153 TCA 1997** as he is a non resident and non-ordinarily resident individual who resides in a EU member state. High Risk Ltd should not apply withholding tax on the dividend to Gilbert as set out in **section 172D(3) TCA 1997** provided he has made a declaration in the prescribed form under **schedule 2A TCA 1997**.

Stage 2 Applied Tax

5. Interest and penalties on late payment of income tax

We must establish if Gilbert has appointed an agent to collect and return the Case V income on his behalf for 2010. If he has not appointed an agent, then Gilbert is obliged to file a tax return and pay income tax arising on the Case V income, which is due for submission on 31 October 2011.

Gilbert's 2009 tax return must also be amended to include the rental income arising on the warehouse. If additional tax is due, then Gilbert is exposed to interest of 0.0219% per day of late payment running from 31 October 2009 under **section 1080 TCA 1997**.

If Sideways Ltd has not operated withholding tax on the rents paid to Gilbert and Gilbert did not appoint an agent, then Sideways will be exposed to interest on the withholding tax it failed to collect.

6. What will Yvette's tax status be on moving to Ireland in 2011?

If Yvette is in Ireland for 183 days in 2011 then she will be Irish tax resident under **section 819 TCA 1997** in 2011. However, the extent to which an individual is liable to Irish tax is determined not only by tax residence status, but also by a concept known as "domicile", which is relevant here for Yvette.

Domicile is a concept of general law which applies to individuals only. The concept is usually linked with the notion of a person's "permanent home". It is used to determine the system of personal law to be applied where a person has connections with more than one jurisdiction. It is not defined in TCA 1997. As such, most of the rules determining an individual's domicile have come from decided case law in Ireland and the UK.

Generally, a person has a domicile in the country of which he/she is a national which is referred to as a domicile of origin. Case law has determined that an existing domicile will continue until it is proven that a new domicile, known as a domicile of choice has been acquired.

Therefore, that fact that Yvette will become Irish tax resident in 2011 will not mean that she has abandoned her French domicile unless she intends to fix her chief place of residency in Ireland with the intension of residing here permanently as outlined in cases such as *Bell vs Kennedy LR 1 SC & DIV 307*.

Sample Paper 1 Solutions

The establishment of a permanent matrimonial home in a particular jurisdiction does not override an intention to return to one's country of origin on the death of a spouse (*IRC v Bullock, 1976 STC 409*).

In addition, marriage to a native of the country in which it is alleged the individual has acquired a domicile of choice is not conclusive evidence of an intention to reside there permanently (*IRC v Bullock, 1976 STC 409*).

Therefore, we must establish Yvette's long term intentions in order to ascertain if she will remain French domiciled or if she will actively acquire an Irish domicile of choice.

7. How can Yvette tax efficiently bring her savings into Ireland?

Assuming that Yvette retains her French domicile of origin, then in 2011, as a non domiciled but Irish tax resident individual, Yvette will be chargeable to Irish income tax under **section 71(2) and 71(3) TCA 1997** on Irish source income, income arising from a foreign office or employment the duties of which are carried on in Ireland and on other foreign income to the extent that it is remitted to Ireland.

Therefore she will be taxed on her Irish source income in full, but the taxation of foreign income is restricted to remittances. This is known as the remittance basis of taxation.

For income tax purposes, in arriving at the total remittances taxable for any year, only remittances of income, as distinct from remittances of capital, are within the charge to Irish income tax. Remittances of capital are not liable to income tax, but may be liable to CGT if arising from a gain made on the disposal of a foreign asset.

The remittance basis of taxation applies to the full amount of actual income received in Ireland. "Income" for this purpose is income that is earned and remitted from 1 January of the year an individual takes up residence in Ireland. Income that has been earned by Yvette prior to 1 January 2011 is deemed to be capital and may be remitted into Ireland tax-free provided that it is not mixed with income arising after 1 January 2011. This could occur if 2011 income is earned on or paid into a bank account that also contains her pre-2011 savings. This is referred to as a "mixed fund".

Remittances from a mixed fund are deemed to come first out of income rather than capital, as outlined in Statement of Practice IT.3.07. If the €500,000 is likely to be funds remitted out of a foreign bank account to which a mixture of savings, capital and income are lodged

Stage 2 Applied Tax

following Yvette's arrival in Ireland, Yvette may trigger a charge to Irish income tax on her foreign income.

It is, therefore, important that income earned prior to Yvette becoming Irish tax resident can be clearly identified as such and separated from income earned after becoming resident for the purposes of tax efficiently remitting foreign savings to Ireland.

It is recommended that she sets up two separate bank accounts: one to hold accumulated income and capital arising before she takes up residency; the other to receive post-residency income. If Yvette can ensure she can display that the funds remitted are clearly from income or savings or capital sources accumulated prior to becoming Irish resident, then no Irish income or capital gains tax issues should arise on such remittances.

I trust that the forgoing is helpful to establishing Gilbert's various tax issues. If I can assist with the clarification of any point or calculation of Gilbert's CGT or income tax liabilities in further detail, please do not hesitate to ask me. I also recommend that we ensure that Gilbert and Yvette have taken appropriate French tax advice on the tax consequences of the proposed move to Ireland and on Gilbert's French tax obligations on the Irish income and gains arising in 2010.

Regards

Laura

END OF MEMO

Section 2

Case Study B: Solution

E-mail

To: Chad M

From: Mary D

Date: 25 October 2010

Subject: Irish Tax queries

Chad

As agreed at our meeting on 20 October, I have considered the Irish tax consequences of the issues raised in the following.

1. What are the implications for Pharma Ire in making an additional claim for R&D expenditure in 2009?

Under **section 766(5) TCA 1997** claims for an R&D credit must be made within 12 months of the end of the accounting period the claim relates to. Therefore claims relating to expenditure incurred in the year ended 30 November 2009 must be lodged to Revenue by 30 November 2010. Any R&D tax credit not claimed by a company within this period will be lost.

We can claim a 20% credit for the additional incremental R&D expenditure identified for the year ended 30 November 2009. As Pharma Ire formed on 31 October 2007, any qualifying expenditure in a later accounting period is treated as incremental and will qualify for the tax credit. Therefore, the additional R&D credit for the year ended 30 November 2009 is €60,000 (€300,000 at 20%). On making the claim before the deadline of 30 November 2010, a refund of corporation tax of €60,000 should issue. The revised total corporation tax liability for 30 November 2009 will be €77,500 on foot of making the additional R&D credit claim.

2. Calculate Pharma Ire's 2010 R&D tax credit and state how this credit can be tax efficiently used.

Pharma Ire is entitled to claim an R&D credit on qualifying expenditure of €750,000. The credit was increased from 20% to 25% in 2010, giving rise to an R&D credit of €187,500 on the 2010 spend. Under **section 766(1)(a)(II) TCA 1997** the expenditure can qualify for the credit if the R&D was carried out in another EU Member State, provided it does not qualify for a tax deduction under the law of another territory, in

Stage 2 Applied Tax

this case the UK. Therefore, will we need to ensure that the expenditure of €500,000 is not claimed as a tax deduction in the calculation of the NI branch's UK corporation tax liability to secure the tax deduction in the calculation of the Irish corporation tax liability of Pharma Ire.

As a loss is projected for 2010, a nil corporation tax liability will arise generating an excess R&D credit of €187,500. This excess credit can be set back against the corporation tax liability of the preceding accounting period under **section 766(4A) TCA 1997** as follows:

30 November 2009 tax liability	€77,500
Less excess R&D credit 2010	<u>(€77,500)</u>
Refund of tax in 2009	€77,500

The remaining excess of €110,000 can be claimed as a tax refund of up to 33% of the excess under **section 766(4B) TCA 1997** and may be payable by the filing date for the accounting period in which the expenditure is incurred. The refund is payable provided the terms of **section 766B TCA 1997** are fulfilled – i.e. the refund is limited to the greater of the corporation tax liability of the company in the previous 10 years or the company's payroll taxes in the year of claim. In this case, the credit is less than the payroll tax liabilities for the year ended 30 November 2010 and a refund of €36,300 will therefore be payable by 21 August 2011.

The remaining excess of €73,700 must be used to reduce the corporation tax liability of the accounting year ending 30 November 2011, which is projected to be €75,000.

3. What tax relief entitlement will Pharma Ire have in respect of the proposed expenditure on the new R&D centre in Leitrim in 2012 and explain the basis for your conclusion?

A R&D credit is available for qualifying expenditure incurred on a building used for R&D purposes under **section 766A TCA 1997**. The building must qualify as an industrial building as specified under **section 268 TCA 1997**.

Qualifying expenditure amounts to 100% of the cost of the building projected to be €5 million less Enterprise Ireland's grant of €1 million as provided for under **section 766A (1)(b) TCA 1997**. Therefore, a 25% R&D credit of €1,000,000 is available in 2012.

Sample Paper 1 Solutions

Under **section 766(4B) TCA 1997**, the credit can be used to generate 3 installments of refunds payable over a 33 month period if sufficient corporation tax is not available in 2012 to fully utilize the substantial R&D credit. However, the refunds are restricted under **section 766B TCA 1997** to the greater of the corporation tax payable in the 10 years prior to the year of the claim or the payroll liabilities for the year ending 30 November 2012. Any unclaimed excess can be carried forward indefinitely for offset against future years corporation tax liabilities of the company.

Section 291A TCA 1997 provides relief in the form of capital allowances against trading income in respect of the intangible assets listed in **section 291A(1) TCA 1997** where used for the purposes of a trade. From the information provided, it would appear that proposed expenditure of €100,000 on the acquisition of registered designs and €75,000 on authorisations to sell certain medicines to complement the products to be developed in the new R&D centre will qualify. If the company borrows to fund the acquisition, the interest cost can also be included in the claim.

Pharma Ire can opt for a deduction in respect of the intangible assets based on one of the following options:

- take an accounts based allowance matching the capital allowances with the depreciation/amortisation charge per the accounts which is computed as €17,500 from 2012 to 2021, **or**
- take a fixed rate allowance over 15 years (7% in the first 14 years and 2% in the last year) which is computed as €12,250 for years 2012 to 2025 and €3,500 in 2026,

The deduction that a company can claim in any year is restricted to 80% of the relevant profits of the company. However, given the amounts of tax deductions involved i.e. €17,500 under the accounts based method or €12,250 under the fixed rate allowance; it is unlikely that this restriction will impact on the calculation of Pharma Ire's entitlements to capital allowances.

4. Is the VAT claim in respect of canteen expenditure correct?

Section 5(3) VATA 1972 deals with self-supplies of services and provides that a deemed supply occurs if services are provided by the accountable person free of charge for the person or the person's staff or for any purpose other than the business.

Where an employer makes canteen services available to staff free of charge, a self-supply is therefore deemed to occur. The VAT charge arising is based on the cost to the employer

Stage 2 Applied Tax

of providing the service, which in this case is €13,500. On that basis we should correct the VAT3s submitted to date in 2010 and repay the VAT incorrectly claimed.

Alternatively, this provision only applies if employees make no payment for the service. Following a recent ECJ case (*Hotel Scandic*), it has now been confirmed that, if an employee pays any amount for the service, the employer is liable to VAT on the receipts and no self-supply arises. I would therefore recommend that we change our procedures in relation to the canteen such that employees make a nominal payment in relation to the services received. That payment should be regarded as VAT-inclusive and VAT paid over to Revenue accordingly, without triggering a clawback of the VAT incurred on the cost of supplying the canteen.

5. How the UK VAT on the equipment repair work should be correctly dealt with.

The place of supply rules in relation to the repair of moveable goods depends on whether the customer is a consumer (B2C) or in business (B2B). If this were a B2C supply, the UK repair company has treated this correctly. However, as this is clearly a B2B supply, the UK repair company is incorrect and should issue a credit note, together with a repayment of the UK VAT of STG £50,250 incorrectly charged. The correct treatment is for the UK repair company to zero-rate the supply and for us, under **section 5(5) VATA 1972**, to apply the reverse charge rules, with the two entries on the VAT3 essentially cancelling each other out.

6. What are the VAT implications for Pharma Ire on the proposed acquisition of the business and assets as set out in the draft sales contract?

Usually, when a VAT registered business disposes of assets on which it has claimed a VAT input credit, then it must charge VAT to the purchaser. However, VAT is not chargeable under **section 3(5)(b)(iii)** and **5(8) VATA 1972** if the following conditions are satisfied:

- the purchaser is a VAT registered person, and
- the transfer constitutes an undertaking or part of an undertaking capable of being operated on an independent basis.

This is commonly referred to as “transfer of business relief” and based on the facts provided it should apply to the acquisition of the business and assets as proposed by Pharma Ire. This relief is not optional in that, once the conditions are satisfied, it must be applied and the vendor is not entitled to charge VAT. If, however, he incorrectly does charge VAT as it

Sample Paper 1 Solutions

suggested under the terms of the draft sales contract and VAT is paid, Revenue are entitled to refuse to give an input credit for the VAT incorrectly charged.

While the vendor will make a supply which is outside the scope of VAT, under **section 12(1)(a)(iii)(a) VATA 1972** they can to recover VAT on costs associated with the sale. As we are carrying on a taxable trade, we are entitled to recover VAT on professional costs in the usual manner.

Therefore, the reasons provided for charging VAT are not valid and the sales contract must be amended to exclude VAT.

7. How will profits in the new licence holding company be treated for corporation tax purposes? Support your conclusion with case law.

Based on the information currently available, the activities of the proposed new company set up to hold the licence agreement will generate income which will be treated as passive income. Passive income profits are subject to corporation tax at a rate of 25% under **section 21A TCA 1997**. The reason I suggest that the income is subject to the 25% rate is because the activities do not appear to be in the nature of trade as provided by the Badges of Trade. For example there should be supplementary work in connection with the article as a trading activity is likely to exist if work is required to bring the article to a more marketable condition. Case law such as *Noddy Subsidiary Rights vs IRC (1996) 43 TC 458* has established that activities are in the nature of trade if value is added to the product by demonstrating that new customers are sought out and that skill is exercised in negotiation of contracts.

In order to demonstrate that the activity is a trading activity liable to the 12.5% rate then it will be necessary to show that there is value added to the licences and that the employees of the company have sufficient levels of skills to indicate that a trade is actively being carried out by the company such as seeking new customers, adding value to the licences, exploiting agreements to optimise profits etc.

I trust that you find the enclosed helpful. If you would like a further discussion on any of these issues, please don't hesitate to contact me.

Regards

Mary

Stage 2 Applied Tax

Section 3

Solutions to Computation Questions

Question 1

(a) Disposal of property in Blackrock

	€
Sales proceeds	650,000
Less: Base cost	
Market value (1982/83) €200,000 × 2.253	<u>(450,600)</u>
Capital gain	199,400
Less: Principal private residence relief (see below)	
€199,400 × 268/341	<u>(156,713)</u>
	42,687
Less: Annual exemption	<u>(1,270)</u>
Taxable gain	41,417
CGT @ 25%	<u>10,354</u>

Calculation of period of occupation

	Months Occupied	Months Absent
1 May 1982–30 June 1991	110	
1 July 1991–31 December 1992		18
1 Jan 1993–28 February 2005	146	
1 March 2005–30 September 2009		55
1 October 2009–30 September 2010	<u>12</u>	<u>—</u>
	<u>268</u>	<u>73</u>
Total number of months		<u>341</u>

(b) John and Mary O'Shea

1. Sale of antique painting (January)

	€	€
Sales proceeds		30,000
Less: Market value at date of inheritance (December 1998)	1,950	
Indexation 1998/99	1,212	

Sample Paper 1 Solutions

Indexed base cost	2,363
Taxable gain	27,637
Summary and calculation of CGT liability	

	Total
	€
(1) Antique painting	27,637
Less: Losses forward	(10,000)
	17,637
Less: Annual Exemption	(1,270)
Taxable gain	16,367
CGT @ 25%	4,092

Question 2

Disaster Insurance Limited – VAT

	2008	2009	2010
Underclaim of inputs based on recovery rate*		5,000	4,000
Underdeclared VAT on reverse charge service**		0	-9,450
Fuel error***	-1,000	-750	-750
Annual total	-1,000	4,250	-6,200
Overall total			-2,950

* Recovery rate for 2009 and 2010 should be 25% not 20% - i.e. €100,000 * 5% for 2009 and €80,000 * 5% for 2010.

** €60,000 * 21% * 75% irrecoverable

*** Claim was €2,000; it should have been 50% of €2,500 in 2009 and 2010; 50% of €2,000 in prior years. Therefore, the net over claim is €1,000 for 2008 and €750 for 2009 and 2010.

Stage 2 Applied Tax

Question 3

(a) Corporation tax computation – year ended 31 December 2009

	€	€
Sch D Case I income		Nil
Sch D Case III income		15,000
Sch D Case IV income		5,000
Sch D Case V income	22,000	
Less: Case V capital allowances	<u>(7,000)</u>	<u>15,000</u>
Total profits		<u>35,000</u>
Corporation tax		
€35,000 @ 25%		8,750
Less: Loss relief S.396B TCA 1997		<u>(8,750)</u>
Corporation tax liability		<u>Nil</u>

Loss Memo

	€
Sch D Case I Loss – current year	150,000
Less: S.396B TCA 1997 relief	
€8,750 / 12.5%	<u>(70,000)</u>
Loss carried forward to 2011	<u>80,000</u>

Corporation tax computation – year ended 31 December 2010

	€	€
Sch D Case I income	35,000	
Less: Loss carried forward	<u>(35,000)</u>	Nil
Sch D Case III income		10,000
Sch D Case IV income		2,000
Sch D Case V income	20,000	
Less: Case V capital allowances	<u>(7,000)</u>	<u>13,000</u>
Total profits		<u>25,000</u>
Corporation tax		
€25,000 @ 25%		<u>6,250</u>

Sample Paper 1 Solutions

Loss Memo

	€
Sch D Case I Loss c/f from 2009	80,000
Less: Utilised in 2010	<u>(35,000)</u>
Loss carried forward to 2011	<u>45,000</u>

CGT computation – year ended 31 December 2010

	€	€
Sales proceeds		550,000
Less: Costs of disposal		<u>(50,000)</u>
Net proceeds		500,000
Less: Acquisition costs		
Purchase price (2000/01)		
Current use value - €120,000 × 1.144	137,280	
Development value	<u>60,000</u>	(197,280)
Costs of Acquisition		
Current use value €20,000 × (120,000/180,000) × 1.144	15,253	
Development value €20,000 × (60,000/180,000)	<u>6,667</u>	(21,920)
Capital Gain		<u>280,800</u>
CGT @ 25%		<u>70,200</u>

Question 4

(a) Transaction (i), Gift received of house in Kilkenny

CAT liability

	€
Market value of house	180,000
Less: Consideration	<u>(50,000)</u>
	130,000
Less: Annual exemption	<u>(3,000)</u>
Taxable gift	127,000

Stage 2 Applied Tax

Add: Previous benefits (Group B)	
Inheritance of shares from uncle	30,000
Total benefits	<u>157,000</u>
Less: Tax free threshold (Group B)	(41,481)
Total taxable benefits	<u>115,519</u>
CAT @ 25%	28,880
Less: CAT on prior benefits	<u>Nil</u>
CAT on current benefit	<u>28,880</u>

Stamp duty liability

As this is Nora's first home, she qualifies for first time buyer relief and the gift is not liable to stamp duty.

(a) Transaction (ii), Purchase of farmland at undervalue from her brothers

CAT liability

Nil CAT is due as the under value is €6,000 and amounts to a gift of €3,000 from each brother which is covered by annual small gift exemption.

SD liability

It is non-residential property with a value of between €40,000 and €70,000. The 4% rate applies but consanguinity relief reduces this to 2%. Stamp Duty = €66,000 × 2% = €1,320.

(b) Late payment of taxes

The CAT was due to be paid by 31 October 2010 so interest and penalties are running.

The transfer of the house from Nora's aunt is a voluntary transfer and therefore the instrument of transfer must be submitted for adjudication within 30 days of the transfer.

The stamp duty return and the stamp duty arising on the transfers from Nora's brother should have been submitted to Revenue via ROS within 44 days of execution of the document so interest and penalties are running. She may also have a surcharge exposure in relation if tax is based on a value less than the open market value of the property.

Sample Paper 1 Solutions

Question 5

Income tax computation – 2010

	Note	€	€
Sch D Case I income	1	31,667	
Less: Capital allowances	2	<u>Nil</u>	
		31,667	
Add: Balancing charge	2	<u>3,071</u>	34,738
Sch D Case III income			4,000
Sch D Case IV income	3		<u>2,000</u>
Taxable Income			<u>40,738</u>
Tax payable			
€36,400 @ 20%		7,280	
€2,000 @ 25%		500	
€2,338 @ 41%		<u>959</u>	8,739
Less: Tax credits			
Widowed person		2,430	
Medical Expenses (€1,000 × 20%)		200	
DIRT (€2,000 × 25%)		<u>500</u>	<u>(3,130)</u>
Income tax payable			5,609
PRSI	4		1,222
Health Levy	5		1,630
Income Levy	6		<u>775</u>
Total income tax, PRSI & Levies liability			<u>9,236</u>

Note 1 – Sch D Case I income

2010 – Basis period: 1 January 2010 to 30 June 2010

$$€5,000 + (4/12 \times €80,000) = €31,667$$

Revenue may review the penultimate year in 2009 if profits for the actual 2009 tax year are greater than those originally assessed:

	€
Original assessment (year ended 30 April 2009)	90,000
Actual assessment (year ended 31 December 2009)	
(4/12 × €90,000) + (8/12 × €80,000)	83,333

Based on the above, an additional assessment is not required.

Sample Paper 1 Solutions

Question 6

(a) Unit 1

- This premises is a qualifying industrial building as tenant is engaged in manufacturing.
- It should qualify in full for capital allowances as the office element is less than 10% (3,500/40,000 is 8.75%).
- The qualifying construction cost is €3.2 million and the tax life is 25 years from January 1993.
- The €3.2 million can therefore be written off over the residue period of eight years giving an annual IBA of €400,000. No IBA can be claimed on the excess over the original qualifying construction cost.

Unit 2

- This premises is a qualifying industrial building – Turner Enterprises Ltd is engaged in manufacturing.
- The qualifying construction cost is €1.8 million as €200,000 of the €250,000 VAT incurred (i.e. 80%) is recoverable
- As Turner Enterprises Ltd has acquired the property from a builder, the “net price paid” formula must be applied, which is as follows:
$$€1.8m * 1.2 m / 1.2m + 0.4m = €1.35m$$
- IBAA can be claimed on the €1.35 million qualifying cost over the tax life of twenty-five years giving an annual IBA of €54,000.

Unit 3

Tim is not entitled to any IBAA for 2010 as he does not hold the relevant interest at 31 December 2010.

- (b) Tim is subject to CGT of $€2m \times 25\% = €500,000$ due to be paid by 31 January 2011.

Question 7

- (i) Under **section 128B TCA 1997**, John is subject to income tax on the exercise of the share options of €3,690 ($€9,000 \times 41\%$), which is payable within 30 days of exercise.

Stage 2 Applied Tax

- (ii) A subsequent disposal of these shares at a gain of €4,000 gives rise to a chargeable gain of €4,000, although this should be sheltered by the €15,000 capital loss forward.
- (iii) CGT is on the disposal of the High Return Ltd shares is calculated as follows:

CGT liability

	€
Sales proceeds	30,000
Less: Base cost (1997/98)	
Purchase price €1,500 × 1.232	(1,848)
Bonus issue	<u>Nil</u>
Gain	28,152
Less: Capital loss c/f (15,000–4,000)	<u>(11,000)</u>
	17,152
Less: Annual Exemption	<u>(1,270)</u>
Taxable gain	<u>15,882</u>
CGT @ 25%	<u>3,971</u>

- (iv) CAT and stamp duty are due in respect of the gift from his father-in-law.

CAT liability

	€	€
Current benefit		15,000
Add: Prior Benefits (Group C)		
Gift from cousin	20,000	
Less: Annual exemption	<u>(3,000)</u>	17,000
Taxable benefits		<u>32,000</u>
Less: Tax free threshold (Group C)		<u>(20,740)</u>
Taxable amount		<u>11,260</u>
CAT@ 25%		2,815
Less: Tax on prior benefit		<u>Nil</u>
CAT on current benefit		<u>2,815</u>

Stamp duty is calculated as 1% of €15,000 - i.e. €150. Consanguinity relief does not apply. This liability can be also deducted in the calculation of John's CAT liability.

Sample Paper 1 Solutions

Question 8

Income tax:

Sean is liable to income tax as follows:

Rental income (note 1)	20,000
Less allowable interest (note 2)	<u>(8,000)</u>
Net Case V income	12,000

Note 1:

Rent is taxable under Case V on an entitlement basis. Therefore, taxable rents for 2010 are €30,000 multiplied by $8/12 = €20,000$.

Note 2:

Pre-letting interest is not allowable – allowable interest is €12,000 by $8/12$.

VAT

The €60,000 VAT incurred on the purchase may be reclaimed in full as Sean has opted to tax the lease. This also means he needs to charge 21% VAT on all rent.

Stamp Duty

Sean was liable to 6% stamp duty on the acquisition of the property. The stamp duty due is €26,400, i.e. 6% of €440,000 (i.e. the VAT-exclusive amount).

Stage 2 Applied Tax

Sample Paper 2 Solutions

Please note, solutions have been written to achieve the highest possible standard

Section 1

Case Study A: Solution

Mulcahy & Co

Report on the tax affairs of Seamus and Lucia Delaney, and their companies

November 2010

The purpose of this report is to address the matters set out below, as follows:

1. DDL and DBL Corporation Tax position for 2009 and 2010.

DDL is trading as a land dealing company and is therefore subject to corporation tax at the 25% rate as an excepted trade under **section 21A(1) TCA 1997**.

DBL is a construction company and is therefore subject to corporation tax at 12.5% rate under **section 21(1)(f) TCA 1997**.

DDL and DBL form a group for the purposes of loss relief under **section 411(1)(a) TCA 1997** as DBL is a 75% or more subsidiary of DDL.

Tax Issues for year ended 30 September 2009

DDL and DBL have an outstanding Corporation Tax Return (Form CT1) for the accounting year ended 30 September 2009. Tax returns for both companies were due for submission on 21 June 2010. The late filing of the tax return is a problem for the following reasons:

- Interest is accruing under **section 1080 TCA 1997** on the non-payment of tax due
- A surcharge for late filing applies under **section 1084 TCA 1997**
- The ability to use certain reliefs, such as loss relief, is restricted under **section 1085 TCA 1997**

Sample Paper 2 Solutions

DDL is in a loss position of €200,000 while DBL is in a profit position of €350,000. Therefore, DBL is potentially exposed to a surcharge based on its tax liability for late submission of the tax return along with interest on late payment of taxes.

My objective will therefore be to minimise the tax liability arising in DBL by claiming all available group losses and group charges from DDL while also contending with the restrictions on the use of loss relief due to the late submission of DDL's tax return and claim for group relief by DBL.

The losses in DDL of €200,000 may be surrendered to DBL on a euro for euro basis under **section 420(1) TCA 1997**. Generally it is not tax efficient to offset a 25% loss against profits liable to tax at 12.5%, however as DBL is exposed to a surcharge and interest, it is appropriate now to use the loss in DDL to minimise DBL's tax liability. Under **section 1085 TCA 1997**, the loss relief surrendered by DDL to DBL is restricted by 50% as the returns are over 12 months late.

The interest paid by DDL in the year ended 30 September 2009 is acquisition interest which qualifies as a non-relevant trade charge under **section 247 TCA 1997**. The non-relevant trade charge can be surrendered to DBL under **section 420(6) TCA 1997** on a euro for euro basis. As excess non-relevant trade charges cannot be carried forward, the surrender of these charges by way of group relief is the only tax efficient option available. Again **section 1085 TCA 1997** will restrict the amount of charges available for group surrender by 50%.

Tax issues for year ended 30 September 2010

For the accounting year ended 30 September 2010, the Form CT1 is due for submission on 21 June 2011. A surcharge, interest exposure and restriction of group loss relief will arise if this deadline is missed.

In 2010, DBL has a trading loss of €300,000 while DDL has taxable profits of €100,000 plus non-relevant trading charges of €20,000. DDL can firstly reduce its taxable profits by claiming relief for the non-relevant trade charges of €20,000 on a euro for euro basis against its profits subject to tax at 25%. DBL can surrender its available losses to DDL on a value basis under **section 420A TCA 1997**.

Stage 2 Applied Tax

DBL's remaining losses can be carried back for offset against profits in the previous period under **section 396A (3) TCA 1997** subject to the 50% restriction under **section 1085 TCA 1997**. Group relief surrendered in accordance with **section 420 TCA 1997** is claimed in priority to losses carried back under **section 396A(3) TCA 1997**.

The tax calculations for DDL and DBL are as follows:

Year ended 30 September 2010

	Statutory reference	DDL €	DBL €
Case I (loss)/profit		100,000	(300,000)
Interest relief	Section 247	<u>(20,000)</u>	
Position before group relief		80,000	(300,000)
CT @ 25%		20,000	
Loss on Value Basis	Section 420A/B	(20,000)	
Loss memo			
Losses surrendered to DDL			160,000
Offset losses to 30/09/09			<u>140,000</u>
			<u>Nil</u>

Year ended 30 September 2009

	Statutory reference	DDL €	DBL €
Case I (loss)/profit		(200,000)	350,000
Interest as a charge	Section 247	<u>(50,000)</u>	
Before relief		(250,000)	350,000
Group relief	Section 420B		
Late filing restriction	Section 1085	(125,000)	
Available relief (euro for euro)	Section 420		(125,000)
Loss relief carried back (restricted)	Section 396A(3)		<u>(70,000)</u>
Taxable profits			155,000
CT @ 12.5%			19,375
10% surcharge	Section 1084		<u>1,937.50</u>
Tax Due			21,312.50
Interest will also arise on late payment of tax			

2. Tax implications for DDL and DBL on interest payments and capital repayments under the arrangements proposed for 1 December 2010.

DBL proposes to commence making interest payments to DDL from 1 December 2010. Under **section 246(2) TCA 1997**, DBL is required to withhold tax at 20% on the payments it makes to DDL. However, as DDL and DBL are in a 51% group for the purposes of **section 410(3) TCA 1997**, the requirement to apply withholding tax is removed. DBL is required to return details of the interest paid gross to DDL under self assessment rules as outlined in **section 891 and 894 TCA 1997**.

The plan for DBL to make a capital repayment to DDL of €150,000 could have implications for DDL's future relevant non-trade charge deductions. **Section 249 TCA 1997** imposes rules known as the recovery of capital provisions which state that the capital repaid must be used to reduce the loan and related interest or in circumstances where the loan is not repaid, then the claim for tax relief on the non-trade charge must be restricted.

3. What is Bakery Delights Ltd's corporation position for 31 December 2010?

Bakery Delights Ltd will qualify as a start up company under **section 486C TCA 1997** and will therefore be entitled to claim an exemption for its profits for the period ended 31 December 2010. This relief applies to the profits of "qualifying trades" for new companies starting to trade in 2009 or 2010. It operates by reducing the corporation tax attributable to such profits to nil but it only applies where the total amount of corporation tax payable by the company for an accounting period is not greater than €40,000. The relief applies for three years from the commencement of the trade, subject to conditions.

A *qualifying trade* is defined as a trade which is set up and commenced by a new company in 2009 and 2010 only. It does not include any trade:

- which was carried on previously by another person and to which the company has succeeded (which would seem to rule out the incorporation of a business by a sole trader/partnership), including trades transferred between connected companies; or
- the activities of which were previously carried on as part of another person's trade or profession;

Stage 2 Applied Tax

Based on the information available, it appears that Bakery Delights Ltd qualifies for the exemption and should therefore have a nil corporation tax liability payable on 21 September 2011.

4. Calculate CAT and Stamp Duty payable by Seamus on the gifts as detailed and provide reasons for the explanation.

Belfast apartment

Seamus is in receipt of a chargeable gift from his father. However, as the value of the gift is below the Group A threshold in 2010 of €414,799, then no current CAT liability will arise on this benefit.

For stamp duty purposes, the conveyance of the Belfast apartment is not subject to Irish stamp duty because section 98(1) SDCA 1999 exempts conveyances of immovable property situated outside the State.

Seamus should clarify whether UK stamp duty is payable.

Cork commercial unit

CAT Liability

Irish CAT arises on this gift as the value of the benefit is in excess of the Group B threshold appropriate to the relationship between Seamus and his sister.

CAT must be calculated using the market value of the property on the valuation date as set out in **section 26 CATCA 2003**, which in this case is the market value of €400,000 as at 1 August 2010. If a value of less than the market value on 1 August 2010 is returned to Revenue then a surcharge under **section 53 CATCA 2003** may be imposed by Revenue. Therefore I will calculate CAT using the actual market value as at 1 August.

The CAT due is calculated as follows:

	€
Market value of 50% interest in property	200,000
Less: Consideration	<u>(50,000)</u>
	150,000
Less: Annual exemption	<u>(3,000)</u>
Taxable gift	147,000
Less: Tax free threshold (Group B)	<u>(41,481)</u>
Total taxable benefits	<u>105,519</u>
CAT @ 25%	26,380

Sample Paper 2 Solutions

The CAT return (Form IT 38) and tax payment arising on this benefit were both due on 31 October 2010. Interest is applied on the late payment under **section 51 CATCA 2003** at a rate of 0.0219% per day of late payment. A surcharge will also arise as a result of the late submission of the tax return which amounts to 10% of the tax liability under **section 53A CATCA 2003**.

Stamp Duty

The stamp duty liability is payable by Seamus. As a voluntary disposition, market value should have been used in the deed of transfer as per **section 30 SDCA 1999**. Revenue will impose a surcharge for undervaluation of the instrument under **section 15 SDCA 1999**. The surcharge is applied by reference to the percentage by which market value is understated which in this case will give rise to a potential surcharge of 50% of the duty payable.

As the subject matter of the disposition is commercial property, the 6% rate of duty applies, subject to consanguinity relief which reduces the rate to 3%. Using the actual market value of the property on the date of the transfer, I calculate a stamp duty liability of €6,000 on claiming consanguinity relief.

The stamp duty return should have been made within 30 days and submitted for adjudication. The tax due should have been paid within a further 14 days of the issuing of a notice of assessment so interest and penalties will arise under **section 14 SDCA 1999**.

A deduction for the stamp duty of €6,000 is available in the calculation of the above CAT liability provided that the stamp duty is paid by the time the CAT return is submitted.

5. What is Lucia's tax status for Irish CAT purposes and calculate CAT if any, arising on the benefit?

Based on the information available, it appears that Lucia is Irish tax resident and but non-Irish domiciled. There is special treatment available to non-domiciles under **section 11(4) CATCA 2003** in respect of inheritances of non-Irish property by a non-resident disponent if Lucia is not resident for five consecutive tax years preceding the year of assessment in which the benefit falls.

However, this treatment does not apply in these circumstances as a charge to Irish CAT arises on all inheritances of Irish situs property under **section 11 CATCA 2003** regardless of the domicile of the beneficiary. Therefore the inheritance by Lucia of the cottage from her neighbour is liable to Irish CAT.

Stage 2 Applied Tax

CAT is calculated using a value of the benefit on the valuation date. Based on the information available, the valuation date is the date of grant of probate as the earliest date the personal representatives can pass the assets of the estate to the beneficiaries.

Therefore the CAT liability arising is calculated as follows:

	€
Market value at valuation date	300,000
Less: Tax free threshold (Group C)	<u>(20,740)</u>
Total taxable benefits	<u>279,260</u>
CAT @ 25%	69,815

This CAT is due to be paid and filed by 31 October 2011.

6. Explain the Stamp Duty implications for first time buyers and owner occupiers of the residential development in Tralee.

Regardless of the floor area of the property, first-time buyers who are also owner occupiers of new or second hand residential property will be exempt from stamp duty under **section 92B SDCA 1999**.

A full exemption under **section 91A SDCA 1999** is available to individuals who are owner-occupiers of new residential property with a qualifying floor area certificate that the property is under 125 square metres. The owner-occupier does not have to be a first-time buyer under this section.

A stamp duty relief is available to owner occupiers of new residential property over 125 square metres under **section 92 SDCA 1999**. The relief reduces the stampable consideration to the greater of the site cost or 25% of the total site and construction cost. Based on the information available, the stampable consideration of the ten units with a floor area greater than 125 square metres can be reduced as follows:

$$\text{Stampable consideration} = \text{€}250,000 \times 25\% = \text{€}62,500.$$

I have assumed that the €250,000 purchase price is VAT exclusive. As €62,500 is less than the stamp duty threshold of €125,000, the units could be marketed on the basis that no stamp duty will arise on the purchase of these properties by qualifying owner-occupiers.

Sample Paper 2 Solutions

However, I would recommend that the marketing materials should carry a disclaimer to the effect that every purchaser is responsible for his own stamp duty obligations and independent advice is recommended.

END OF REPORT

Stage 2 Applied Tax

Section 2

Case Study B: Solution

From: Acharteredtaxconsultant@XYZ&CO.ie Sent: Fri 19/10/2010 09:15
To: Jillmathews@XYZ&CO.ie
Subject: The Trotters Tax Issues

Jill

As requested, I set out the analysis you requested, as follows:

1. Stamp Duty implications for Derry and Roger on various transfers on 2 June and 15 July, complete with calculations and consequences of late payment of tax.

Stamp duty arising on the swap of the commercial property in Dublin

The transfer of the commercial property from Derry to Roger is within the charge of Irish Stamp Duty under **section 2 SDCA 1999** as the property in question is located in the State. The instrument transferring the property is stampable under the Conveyance of Transfer on Sale of Property head of charge as specified in **Schedule 1 SDCA 1999**.

The transfer is treated as a voluntary disposition under **section 30 SDCA 1999** as there is no consideration passing other than the transfer of the mortgage. A voluntary disposition inter vivos is chargeable to stamp duty at ad valorem rates based on the value of the property transferred.

I note that Roger will also take over the mortgage on the property which is €1,000,000. Revenue will generally allow the calculation of stamp duty to be based on the greater of the mortgage or the equity of redemption. The equity of redemption is the difference between the value of the property and the mortgage. In this case, stamp duty will be calculated on €1,000,000 which is the greater value of the mortgage compared to the equity of redemption of €500,000. This is in line with **section 41 SDCA 1999**.

The transaction should also qualify for consanguinity relief as provided for in the **First Schedule SDCA 1999**. The relief operates by reducing the rate of ad valorem duty applicable to the value of the transaction by 50%. Therefore, stamp duty on the instrument transferring the commercial property from Derry to Roger is:

$$€1,000,000 \times (6\% \times 50\%) = €30,000.$$

Sample Paper 2 Solutions

This duty is payable by Roger.

As the transaction is a voluntary disposition, it should have been submitted for adjudication to the Revenue Commissioners within 30 days of the date of execution of the instrument which I calculate to be 2 July 2010. Interest will be applied under **section 14 SDCA 1999** from the date of the execution of the instrument until the settlement of the liability at a rate of 0.0219% per day. In addition, a tax geared penalty of 10% will apply if the stamp duty is settled before December 2010, with higher penalties arising if the instrument remains unpaid later than 6 months from the date of execution as set out in **section 14(2) SDCA 1999**.

Therefore, I recommend that Roger submits the instrument for adjudication along with a payment of stamp duty and interest calculated up to the date of payment as a matter of urgency as he is exposed to substantial interest and penalties for late payment.

Stamp duty arising on the transfer of the Spanish property

The transfer of the Spanish property from Roger to Derry will also be within the charge to Irish Stamp Duty under **section 2(1) SDCA 1999**. This section charges Irish stamp duty on an instrument if:

- a) it is executed in the State
- b) wherever executed, it relates to any property in the State or
- c) it relates to a matter or thing to be done in the State.

Applying the principle established in the UK case of *IRC v Maple & Co. (Paris)* ([1908] AC 22), as the transfer includes shares in an Irish company as consideration, then the instrument is chargeable to Irish stamp duty.

Consanguinity relief will also apply to reduce the rate of stamp duty by 50%.

The consideration on which stamp duty is calculated is €1,250,000 and stamp duty is calculated as follows:

First €125,000 = Nil
Next €875,000 × 3.5% = €30,625
Balance €250,000 × 4.5% = €11,250
Total Stamp Duty = €41,875

Derry is liable to pay the stamp duty.

Stage 2 Applied Tax

The claim for consanguinity relief and the fact that the instrument relates to a voluntary disposition means that adjudication is obligatory. The submission for adjudication was due 30 days after the execution of the document. Interest will be applied at 0.0219% from the date the document was executed until the date the stamp duty liability is settled. In addition, a tax geared penalty of 10% will apply if the stamp duty is settled before January 2011, with higher penalties arising if the instrument remains unpaid later than 6 months from the date of execution as set out in **section 14(2) SDCA 1999**.

Again, I recommend that Derry settles this stamp duty liability as soon as possible to stem his exposure interest and penalties.

Stamp Duty arising on the transfer of the shares

Derry transferred shares in Trotters Ltd to Roger so a charge to stamp duty arises under the Conveyance or transfer on sale of stock Head of Charge.

Therefore, Roger is liable to stamp duty of 1% on the value of the shares of €500,000 which amount to €5,000. No consanguinity relief is available on transfers under the Conveyance or transfer on sale of stock Head of Charge.

The instrument transferring the shares is subject to adjudication as it is a voluntary disposition. Again interest and penalties will be payable as the submission for adjudication was not submitted within 30 days of execution.

2. What CAT implications arise for Derry and Roger in respect of the transfers on 2 June and 15 July 2010? Support the analysis with calculations?

Roger is within the charge to Irish CAT as he is Irish domiciled and ordinarily tax resident, he has received a benefit of Irish situs assets and the disponent is tax resident under **section 6 CATCA 2003**.

Roger has taken a taxable gift of the commercial property from Derry with a market value of €1,500,000. He is entitled to a deduction for the mortgage he has assumed on the property. He can claim a deduction for the stamp duty he pays on the transfer and for professional fees incurred by him on taking a gift of the commercial property. His CAT liability is as follows:

Sample Paper 2 Solutions

Value of Benefit	€1,500,000
Less LCE	
Stamp Duty	(€30,000)
Legal fees	(€18,000)
Mortgage	<u>(€1,000,000)</u>
Incumbrance-free-value	€452,000
Less Small Gift exemption	<u>(€3,000)</u>
Taxable Value	€449,000
Tax Free Threshold Group B	<u>(€41,481)</u>
Net Taxable Value	€407,519
Taxed @ 25%	€101,880

The date of the benefit is 2 June 2010 therefore the submission of the Form IT38 and payment of CAT is due on or before 31 October 2010. Interest and penalties will arise if CAT is not paid and filed by this date.

Derry has received a life interest in Roger's Villa in consideration of €500,000 worth of shares in Trotters Ltd. The life interest is calculated under the limited interest provisions set out in **Table A Part 2 of the First Schedule to the CATCA 2003** which discounts the value of the benefit by reference to the age and sex of the person taking on the life interest. The relevant factor for a male aged 60 is 0.5809. This factor is applied to the incumbrance-free-value of the benefit and CAT is calculated accordingly:

Value of Benefit	€1,250,000
Less LCE	
Stamp Duty	(€41,875)
Professional fees	<u>(€10,000)</u>
Incumbrance-free-value	€1,198,125
Limited Interest Factor 0.5809	€695,990
Less consideration	<u>(€500,000)</u>
Taxable Value	€195,990
Less small gift exemption	<u>(€3,000)</u>
Taxable Value	€192,990
Tax Free Threshold Group B	<u>(€41,481)</u>
Net taxable value	€151,510
Taxed @ 25%	€37,877

Stage 2 Applied Tax

The date of the gift is 15 July 2010 therefore the submission of the IT38 and payment of CAT is due on or before 31 October 2010. Interest and penalties will arise if CAT is not paid and filed by this date.

The Trotters have only a short timeframe to submit a Form IT38 and pay their respective liabilities by 31 October. Of course a deduction cannot be claimed for the stamp duty liabilities unless the outstanding stamp duty is actually paid to Revenue. Therefore, I recommend that the Trotters settle their stamp duty liabilities and CAT liabilities by 31 October 2010.

3. What VAT issues arise on the transfer of the commercial property from Derry to Roger?

I note in the information you provided that Derry does not appear to have charged VAT on the transfer of the commercial property to Roger.

We need to consider if the property is in the VAT net and if VAT should have been charged by Derry accordingly.

For VAT to arise on the disposal of a property, as provided for under **section 4B VATA 1972**, there are generally three conditions that must be satisfied:

- The property must have been “developed”.
- The property must be supplied for consideration in the course of business.
- The property must be considered “new”, as set out in section 4B (2) (c) and (d) and (e) VATA 1972.

I will consider the conditions above based on the information provided as follows:

Property must have been developed

“Developed” means that the property is adapted for a materially altered use whereby expenditure exceeds 25% of the consideration for the subsequent supply. It is not clear from the information if the property has been adapted for a materially altered use but Derry has spent €450,000 on the property which is more than 25% of the market value arising on the current supply of €1,500,000 indicating that the property is “developed”.

Property supplied in the course of a business

As Derry has reclaimed VAT on all work carried out to the property and charged VAT on the letting to the property to the former tenants, it appears that the current supply is in the course of business.

Property must be “new”

The supply of a property is taxable only while the property is considered new. A property is considered new upon completion and will be considered new for a maximum period of five years from the date on which the property itself, or a development of the property is completed. As this property is within the five-year period since it was developed under the October 2008 refurbishment, it is still new for VAT purposes.

Therefore, Derry is required to charge VAT at a rate of 13.5% on the market value of the property to Roger. The VAT he should have charged is therefore €202,500. The VAT should have been returned on Derry's May/June 2010 VAT3 due for submission on 19 July 2010 assuming that he remits VAT on a bi-monthly basis. Derry is exposed to interest of 0.0274% per day of late payment under **section 21 VATA 1972**. Therefore I recommend that he should submit an amended VAT3 return as soon as possible and pay over the VAT due.

4. VAT issues for Roger on entering into the new leasehold arrangement with the insurance company, identifying any opportunities to minimise tax.

As outlined above, Derry must charge Roger VAT on the supply of the freehold of the property. Roger's ability to reclaim that VAT depends on whether the next use to which he, as a landlord, puts the property is VATable or not.

Lettings of property from 1 July 2008 are exempt from VAT. However, the landlord may, with some exceptions, exercise an option to apply VAT to a letting, as provided for under **section 7A VATA 1972**.

A landlord who makes an exempt letting is not entitled to deduct VAT incurred on the acquisition or development of a property, which is subject to the letting. However, where a landlord opts to tax a letting, that service becomes subject to VAT at the standard rate, currently 21%. Therefore the landlord is entitled to deduct VAT incurred on the acquisition or development of a property that is to be used for the purposes of making taxable lettings provided they charge 21% VAT on the rents.

Stage 2 Applied Tax

The option to tax a letting is a matter for the landlord. It is still important for a landlord to confirm this with the tenant in writing in advance as it may not be possible to collect VAT from a tenant if they have not been informed prior to agreeing the lease that VAT will apply to the rents.

If Roger does not opt to tax the lease, he cannot claim a deduction for €202,500 VAT arising on the transfer from Derry.

I assume that the tenant is reluctant to incur a VAT cost on the proposed lease because they are not aware of the “new” VAT on property rules i.e. VAT on the upfront capitalised value of a long lease no longer applies. Instead, VAT is charged at 21% on the periodic rents and the tenant can reclaim VAT in accordance with their recovery rate under the provisions of the Capital Goods Scheme, as set out in **section 12E VATA 1972**.

Therefore the tenant will incur VAT at 21% on the periodic rental payments and they will be entitled to reclaim 80% of this VAT.

By contrast, Roger is faced with a significant VAT cost if the option to tax is not exercised. I recommend that further discussions take place with the tenant to ensure that they fully understand the VAT implications of opting to tax the rents. Roger should press the option to tax issue otherwise he will incur a substantial VAT cost. He may have to renegotiate the rent so that the tenant is not at a cashflow disadvantage as a result of his decision to opt to tax the lease.

5. Darren’s CAT and Stamp Duty obligations on the proposed gift of his parent’s home and focusing on the availability of any reliefs to minimise tax on the transfer.

As a first time buyer, Darren should not be subject to stamp duty under **section 92B SDCA 1999** provided that he does not own any other dwelling/residential property.

The instrument of transfer is subject to adjudication as the transfer is an inter vivos voluntary disposition and must be submitted to Revenue within 30 days of execution.

Darren is liable to CAT on taking a transfer of the house. Dwelling house relief under **section 86 CATCA 2003** exempts CAT arising on a benefit of a residential property, which the donee has occupied as their principal private residence for the three years immediately preceding the date of the gift or inheritance. Darren is not entitled to claim

Sample Paper 2 Solutions

Dwelling House relief because his period of occupation coincided with a period during which the disponers, Derry and his wife, also occupied the house as their main residence, as provided for under **section 86(3A) CATCA 2003**.

Alternatively, Derry and his wife could delay the transfer by four years in which time they will not have lived in the house in Dublin as their main residence. Darren will have achieved a three year period of residence preceding the date of the transfer of the house in which his parents did not live in the house also. He may at that point be entitled to Dwelling House relief provided the rules remain the same as at the time of writing this email. Of course, Derry and his wife may have CGT to pay on the portioned of any gain related to the period in which they did not occupy the house as their principal private residence exclusive of the last twelve months of ownership.

6. Was the Spanish lawyer correct in charging Derry VAT on the invoice for services rendered in respect of the swap of the Spanish villa?

On the basis that the service supplied related to immovable property i.e. the Villa in Spain, then it appears that the Spanish lawyer was correct in charging Derry Spanish VAT on the service. The Irish equivalent of this rule is provided for under **section 5(5)(c)** and **section 5(5A) VATA 1972**.

I hope that the above analysis meets your requirements. I recommend that the Trotters also ensure that all Spanish tax issues on the transfer of the villa are resolved on foot of Spanish tax advice.

If you would like to discuss any issue in further detail, please do not hesitate to contact me.

Regards

A Chartered Tax Consultant

Stage 2 Applied Tax

Section 3

Solutions to Legislation Questions

Question 1

- 1.1 Section 97(2J) TCA 1997
- 1.2 Section 71(4) TCA 1997
- 1.3 Section 1023 TCA 1997. The claim must be made by either spouse before 1 April in the year of assessment they wish for separate assessment to apply
- 1.4 S.121A TCA 1997; the rate is 5% and is provided for under section 121A(3)

Question 2

- 2.1 21%; section 11(1)(a); reverse charge provisions of section 5(5D) VATA 1972
- 2.2 Outside the scope of VAT; section 3(5)(b)(iii) and section 5(8) VATA 1972
- 2.3 Exempt; Part 1 Para 2(3) First Schedule
- 2.4 0%; Part 2 Para 11 (3)(c) Second Schedule

Question 3

- 3.1 No; Section 547 to 549 TCA 1997 determines that market value must apply; connected persons, defined in S.10 TCA
- 3.2 Yes; capital sum derived from an asset as per section 535(2)(a)(ii) TCA 1997
- 3.3 Yes; negligible value can be made as per section 538 TCA 1997
- 3.4 Generally interest is not deductible as per section 552(3) TCA 1997; however an exception is provided for under section 553 TCA 1997 for companies

Question 4

- 4.1 Section 27(3) TCA 1997; 5
- 4.2 Section 76 TCA 1997
- 4.3 No you can choose as per section 76A and Schedule 17A TCA 1997
- 4.4 Yes; you can claim terminal loss relief under S.397 TCA 1997 against profits arising in previous 3 years

Question 5

- 5.1 Yes; section 54 CATCA 2003 allows for payment in five equal annual instalments. Interest accrues on unpaid tax
- 5.2 Section 69 CATCA 2003

Sample Paper 2 Solutions

5.3 Section 2(1)(b) SDCA 1999. It means that if a document is executed outside Ireland, a charge to SD on Irish situs assets can't be avoided by doing so

5.4 Section 14(1) SDCA 1999 and section 14(2) SDCA 1999 – interest and penalties on late payment and filing

Question 6

6.1 Section 128(2) TCA 1997

6.2 Section 128(2A) TCA 1997

6.3 Section 958(3)(a)(v) TCA 1997

6.4 Section 980(4)(a)(i) TCA 1997

Question 7

7.1 Anti-avoidance legislation under section 72(2) TCA 1997 will treat the repayments on such a loan as deemed remittances to Ireland

7.2 If shares are disposed of and shares of the same class are reacquired within 4 weeks after the disposal, any loss arising on the disposal is only allowable against any gain that may accrue on the disposal of the shares reacquired in the 4 week period under section 581 (3) TCA under “bed and breakfast” anti-avoidance rules

7.3 As the undeveloped property is disposed of in connection with a building or development agreement, the disposal of the property is subject to VAT in accordance with section 4B(3) VATA 1972

7.4 The scope of the charge to Irish CAT on gifts received by a non-domiciled person from 1 December 1999 is provided for under section 6(4) CATCA 2003

Question 8

8.1 The consideration of cash plus the discharge of the mortgage will be subject to stamp duty under section 41 SDCA 1999

8.2 Stamp duty is payable on €440,000 as per section 48 SDCA 1999

8.3 Stamp duty is payable on €50,000 as per section 56 SDCA 1999; the rate of stamp duty is 6% as per Schedule 1 SDCA Lease Head Para 3(c)(ii)

8.4 Yes, the supply is subject to VAT under section 4B(6A)(e) VATA 1972.

