Answers

1 *This question tested candidates' income tax computational abilities in a partnership situation, in particular, where there is a change in profit sharing ratios and the introduction and departure of an individual partner. In addition, it tested knowledge of the income tax implications arising from a change of year end.*

(a) (i) Schedule D Case II assessments

2005

Peter

Basis period – year ended 30 April 2005

	€
€240,000 x $\frac{11}{12}$ x $\frac{2}{3}$	146,667
€240,000 x $\frac{1}{12}$ x 50%	10,000
	156,667

Original assessment **Paul**

Basis period – year ended 30 April 2005

	€
€240,000 x $\frac{11}{12}$ x $\frac{1}{3}$	73,333
€240,000 x $\frac{1}{12}$ x 50%	10,000
	83,333

As Paul ceased to be a partner in 2006, this year could be reviewed to actual.
Actual income for the year

	€
€240,000 x $\frac{3}{12}$ x $\frac{1}{3}$	20,000
€240,000 x $\frac{1}{12}$ x 50%	10,000
€300,000 x $\frac{5}{12}$ x 50%	62,500
€300,000 x $\frac{3}{12}$ x 40%	30,000
	122,500

The 2005 year will be reviewed to actual (i.e. the assessable figure becomes €122,500).

Mary

Basis period – 1 October 2005 to 31 December 2005

	€
€300,000 x $\frac{3}{12}$ x 20%	15,000

2006

Peter

Basis period – year ended 30 April 2006

	€
€300,000 x $\frac{5}{12}$ x 50%	62,500
€300,000 x $\frac{7}{12}$ x 40%	70,000
	132,500

Paul

Basis period – 1 January 2006 to 31 May 2006

	€
€300,000 x $\frac{4}{12}$ x 40%	40,000
€360,000 x $\frac{1}{12}$ x 40%	12,000
	52,000

Mary

Basis period – 1 January 2006 to 31 December 2006

	€
€300,000 x $\frac{4}{12}$ x 20%	20,000
€360,000 x $\frac{1}{12}$ x 20%	6,000
€360,000 x $\frac{7}{12}$ x 30%	70,000
	68,000

2007

Peter

Basis period – year ended 30 April 2007.

	€
€360,000 x $\frac{1}{12}$ x 40%	12,000
€360,000 x $\frac{11}{12}$ x 70%	231,000
	243,000

Mary

Basis period – year ended 30 April 2007.

	€
€360,000 x $\frac{1}{12}$ x 20%	6,000
€360,000 x $\frac{11}{12}$ x 30%	99,000
	105,000

Summary:

	2005	2006	2007
	€	€	€
Peter	156,667	132,500	243,000
Paul	122,500	52,000	–
Mary	15,000	68,000	105,000

(ii) Peter

Income tax/PRSI/levies computation for the income tax year 2007

	Notes	€	€
Schedule D Case II		243,000	
Less: Capital allowances	(a)	(3,850)	
			239,150
Irish rental income	(b)		–
UK rental income	(b)		15,687
			254,837
Less: Maintenance payments	(c)		(48,000)
Health expenses	(d)		(10,000)
Taxable income			196,837
Income tax payable:			
€			
38,000 at 20%			7,600
158,837 at 41%			65,123
196,837			72,723
Less: Single person's credit			(1,760)
Age credit			(275)
Single parent credit			(1,760)
UK income tax on rental income			(2,500)
Net income tax payable			66,428
PRSI	(e)		–
Levies	(f)		4,670
Net income tax/PRSI/levies payable			71,098

(iii) The preliminary income tax for the income tax year 2007 was payable on or before 31 October 2007. The filing date for the income tax return is 31 October 2008 (if not filed online).

Notes:

(a) Capital allowances

Year of acquisition	2004		2005		Total
	€		€		€
Cost	20,000		24,000		44,000
Tax written down value 1 January 2007	12,500		18,000		30,500
Less: Wear and tear 2007	(2,500)	(i)	(3,000)	(ii)	(5,500)
Tax written down value 31 December 2007	10,000		15,000		25,000

Notes:
(i) €20,000 x 12·5%
(ii) €24,000 x 12·5%

Allocated to Peter as follows:

	€
€5,500 x 70%	3,850

(b) Section 23 property

	€
Rental income	6,000
Section 23 relief*	(187,500)
Deficit	(181,500)
Rental income from the partnership	40,000
Rental deficit carried forward	(141,500)

$$*€250{,}000 \times \frac{150{,}000}{150{,}000 + 50{,}000}$$

The UK rental income is not aggregated with the Irish rental income and, therefore, the s.23 property cannot be used to shelter this rental income from Irish income tax. This is on the basis that UK rental income is classified as Schedule D Case III income (i.e. income from foreign possessions) unlike Irish rental income which is assessable under Schedule D Case V. However, it is possible that domestic Irish tax law on this point may be contrary to EU law as such a provision could be a hindrance or a potential hindrance to the free movement of investment within the EU.

(c) He is allowed a deduction for the maintenance payments to his ex-wife. However, he is not entitled to a deduction for the payments made to his ex-wife for the maintenance of the children.

(d) €10,000 – s.9 FA 2008.

(e) As he has reached 66 years of age, he does not have PRSI liability.

(f) 2% of €100,100 plus 2·5% of €106,737 = €2,002 + €2,668 = €4,670.

(b) Change of accounting year end

The Schedule D Case II profits for 2008 will be calculated by reference to the year ending 30 June 2008 (i.e. $\frac{12}{14}$ of the tax adjusted profits, before capital allowances for the 14 months ending 30 June 2008).

In addition, the income tax year 2007 will be reviewed by reference to the 12 months ending 30 June 2007 (i.e. $\frac{10}{12}$ of the tax adjusted profits for year ended 30 April 2007 and $\frac{2}{12}$ of the tax adjusted profits for the 14 month period ending 30 June 2008).

As the profits for the 14 month period ending 30 June 2008 are exceptionally large, it is likely that the Schedule D Case II figure for 2007 will be increased.

2 *This question tested candidates' corporation tax computational abilities, in particular, capital allowances, add-backs for motor expenses and other items, as well as knowledge of the favourable holding company regime and the implications arising from a change of accounting year end.*

(a) (i)

M Ltd
Corporation tax computation
for the year ended 30 September 2007

	Notes	€
Net trading loss		(100,000)
Add-backs for:		
Depreciation		40,000
Provision for contributions to directors' pension scheme	(a)	50,000
Motor expenses	(b)	192
Legal and professional fees	(c)	8,000
Repairs and renewals	(d)	50,000
Adjusted trading profit before capital allowances		48,192
Less: Capital allowances	(e)	(54,785)
Adjusted trading loss for corporation tax purposes		(6,593)
Other income	(f)	15,000
Chargeable gains	(g)	89,808
Profits subject to corporation tax		104,808

Corporation tax payable	
€	
15,000 at 25%	3,750
89,808 at 12·5%	11,226
104,808	14,976
Less: Credit for trading losses – €6,593 x 12·5%	(824)
Net corporation tax payable	14,152

(ii) The due dates for the payment of corporation tax are 21 August 2007 and 21 June 2008.
The latest filing date for the corporation tax return is 21 June 2008.

Notes:

(a) Pension contributions are allowed on a paid not on an accruals basis.

(b) Motor expenses:

	€
Motor car – 05 XX 2850	
No add-back of leasing charges as, while acquired by way of a financial lease in 2005, the increased limit of €24,000 applies for 2007.	–
There is no add-back in the case of motor cars for general running costs.	–
Motor car 05 XX 2840	
The add-back for leasing charges is computed as follows:	
$€4,800 \times \frac{25,000 - 24,000}{25,000}$	192
As above, no add-back for general running costs	–
Other motor cars	
As above, no add-backs for general running costs	–
Vans	
No add-backs for leasing charges or general running costs	–
Total add-backs	192

(c) The legal fees incurred in defending a title to a distribution premises is allowable (see tax case *Southern* v *Borax Consolidated Ltd 23 TC 597*).

Architects' and surveyors' fees connected with an intended site acquisition are capital in nature and, therefore, added back.

The provision for future lease payments is in recognition of an obligating event as at 30 September 2007. Therefore it was correct to make such a provision in accordance with generally accepted accounting principles. The general rule is that trading profits, for corporation tax purposes, are computed in accordance with generally accepted accounting principles so long as they do not conflict with statute. There is nothing in the Taxes Consolidation Act 1997 which seeks to disallow such a provision (see tax case *Honour* v *Herbert Smith 72 TC 130*).

(d) Repairs and renewals:

The element of improvement arising from the refurbishment of the distribution outlet is treated as capital expenditure and is, therefore, added back.

(e) Capital allowances:

	Plant and equipment		**Motor vehicles**		**Factory buildings**	
	€		€		€	
Cost	200,000		92,000 *		500,000	
Tax written down values at 1 October 2006	125,000		69,000		280,000	
Sales at tax written down values	(12,500)		(16,500)	(ii)	–	
	112,500		52,500		280,000	
Additions in the year ended 30 September 2007			24,000	(iii)		
Wear and tear for the year ended 30 September 2007	(22,500)	(i)	(11,750)	(iv)	–	
IBAA for the year ended 30 September 2007	–		–		(20,000)	(v)
Tax written down values at 30 September 2007	90,000		64,750		260,000	

* Tax adjusted cost (i.e. vans €70,000 + motor car €22,000)

Notes:

		€
(i)	€(200,000 – 20,0000 x 12·5%	22,500
(ii)	Deemed sale price:	
	$€18,142 \times \frac{22,000}{25,000}$	15,965
	Tax written down value	(16,500)
	Balancing allowance	(535)
(iii)	Substituted price for capital allowances is €24,000.	
(iv)	€(70,000 + 24,000) x 12·5%	
(v)	Original qualifying expenditure	440,000
	Unexpired relevant period at the date of purchase: 22 years	
	$IBAA = \frac{440,000}{22}$	20,000

Summary – capital allowances

	Plant and equipment	Motor vehicles	Factory building	Total
	€	€	€	€
Wear and tear	22,500	11,750	–	34,250
Balancing allowance	535	–	–	535
IBAA	–	–	20,000	20,000
Totals	23,035	11,750	20,000	54,785

(f) Other income and gains

The dividend from P Ltd, an Irish company, is classified as franked investment income and is not taken into account for corporation tax purposes.

Note: The dividend is taken into account for the corporation tax surcharge that can apply to closely held Irish companies. However, this topic is not included in the syllabus for this level.

The dividend from the UK company (B Ltd) is classified as income from foreign possessions and is taken into account for corporation tax purposes.

Note: It is possible that M Ltd is entitled to a credit for any UK corporation tax suffered by B Ltd on the underlying income from which the dividend was paid. However, as this was not referred to in the question, candidates were not expected to address this point.

The chargeable gain arising on the sale of the shares in P Ltd is computed as follows:

	€	€
Sale consideration		80,000
Less: Incidental costs of sale		(3,000)
		77,000
Cost of shares	10,000	
Indexation – 2001	1·087	(10,870)
Enhancement expenditure (Rights issue)		(10,000)
Chargeable gain		56,130

Adjusted for corporation tax: €

$$\frac{56{,}130 \times 20}{12{\cdot}5} = 89{,}808$$

The chargeable gain arising from the sale of shares in A Ltd comes within the ambit of the favourable holding company legislation, as this 20% holding satisfies the following conditions for the relief:

- the holding is in excess of 5% of the shareholding in A Ltd;
- the period of ownership exceeds the minimum 12 months; and
- the market value of A Ltd's shares was not derived or mainly derived from land in this country.

Therefore, this gain is exempt from corporation tax.

(b) Change of accounting year end

The maximum duration for an accounting period for corporation tax purposes is 12 months.

This will mean that the 15-month period ending 31 December 2008 will be divided into two accounting periods for corporation tax purposes, namely:

- the year ending 30 September 2008; and
- the three-month period ending 31 December 2008.

Therefore, M Ltd will have payment of corporation tax and filing of corporation tax return obligations by reference to both these two deemed accounting periods. The profits for corporation tax purposes will be computed on a time apportionment basis i.e.

- $\frac{12}{15}$ of the total profits for the period ending 31 December 2008; and
- $\frac{3}{15}$ of the total profits for the period ending 31 December 2008.

3 *This question tested candidates' capital gains tax (CGT) computational abilities as well as knowledge of CGT retirement and principal private residence (PPR) reliefs; non-taxability of compensation for personal injuries and restriction of losses arising from the disposal of development land.*

(a) **Sale of site – 1 June 2007**

	€	€
Sale consideration		100,000
Less: Incidental costs of sale		(5,000)
		95,000
Base cost*	4,000	
Indexation	7·528	(30,112)
Capital gain		64,888

$$* \text{€}60{,}000 \times \frac{100{,}000}{100{,}000 + 1{,}400{,}000}$$

Transfer of the out-farm to son

This qualifies for capital gains tax retirement relief. Whilst it has been let since 1998, it is still a qualifying asset for this purpose. This is on the basis that it was let to the child to whom the farm was transferred on 1 September 2007. In addition, it was owned and farmed by Rupert throughout the ten years prior to this letting in January 1998. There is no monetary limit in the case of transfers made to children.

Compensation for the acquisition of part of the garden of his principal private residence (PPR)

This compensation constitutes the disposal of an interest in the gardens attaching to his PPR. As this compensation merely reflected current use value, full PPR relief applies (i.e. no capital gains tax exposure) in respect of this compensation.

Compensation for personal injury

Whilst this is a capital sum derived from an asset (i.e. the right to sue) it is specifically exempt from capital gains tax.

Sale of site on 10 November 2007

	€
Sale consideration	80,000
Less: Incidental costs of disposal	(2,000)
	78,000
Cost	(155,000)
Loss	(77,000)

Sale of tractor

While this is a wasting chattel, it was used for the purposes of Rupert's farming trade. Therefore he was entitled to (and presumably claimed) capital allowances on the tractor. Therefore any gain arising from its sale comes within the ambit of capital gains tax.

	€	€
Sale consideration		12,000
Cost – 1990/91	6,000	
Indexation	1·442	(8,652)
Capital gain		3,348*

* Strictly speaking an apportionment should be carried out for the non-business use of six months but students were not expected to do this calculation.

Summary

	€
Gain on sale of one-acre site	64,888
Loss on sale of quarter acre site offset (Note)	(68,236)
Gain on sale of tractor	3,348
Compensation for part of garden of PPR	–
Personal injury compensation	–
Gains subject to capital gains tax	–
Capital gains tax liability:	–

Note

The losses arising from the sale of development land can be set off against all gains. The balance of the loss of €8,764 is carried forward.

(b) The capital gains tax on the site sold on 1 June 2007 was payable on 31 October 2007. However, in the light of the relief for the loss incurred on the site sold on 10 November 2007, Rupert is entitled to a refund.

If there was no relief for capital loss the capital gains tax payable on the tractor would have been payable on or before 31 January 2008.

4 *This question tested candidates' knowledge of a number of VAT issues including: particulars which must be contained in a VAT invoice; entitlement to a credit for VAT suffered; when a provider of a vatable service must issue an invoice; transfer of undertaking relief and the role of the European Court of Justice in VAT matters.*

(a) The particulars which must be shown on a VAT invoice are as follows:

- Name, address and VAT number of the supplier.
- Name and address of the purchaser.
- Date of issue of the invoice and invoice number.
- Date of supply of the goods and/or services.
- Description of the goods or, if applicable, services supplied.
- Quantity or value of the goods.
- The VAT exclusive price of the goods and/or services.
- The VAT rates chargeable for the different goods and/or services supplied.

(b) The significance of a valid VAT invoice for a VAT registered person who receives it is that, in general, it enables this person to claim a credit for the VAT. Such credit is given on the basis that the relevant goods or services purchased/received are in relation to the person's vatable activity. In other words, there is no entitlement to a credit for the VAT suffered if it relates to a VAT exempt activity or if there is a specific prohibition of a credit for the VAT element of the purchase price of the goods or the service provided to this person.

Where the goods or services purchased relate in part only to vatable activities such a person would be entitled to a partial credit for the VAT suffered.

(c) A provider of a vatable service is obliged to issue a VAT invoice within 15 days after the end of the month in which the service is completed.

There is, however, no such obligation if the service is provided to a party who is not a vatable person.

(d) The vendor's agent is not correct. The sale/purchase of a business between two vatable persons constitutes a transfer of an undertaking and, therefore, is not a vatable supply. Consequently, if the client pays the VAT, there is technically no entitlement to a credit for it.

(e) The Revenue official is not correct. The ultimate arbiter on VAT matters is the European Court of Justice.

5 *This question tested candidates' analytical abilities re the issue whether gains arising from the sale(s) of houses were subject to income tax or capital gains tax. In addition, it tested knowledge of the RCT rules.*

(a) As Richard acquired the site with the specific intention of building two houses with a view to their sale to third parties, it would appear that the disposals would be regarded as an adventure in the nature of trade.

Further, the definition of trade has, in essence, been widened by the Taxes Consolidation Act 1997 for situations where land has been developed by the vendor.

Therefore it would appear that the gains arising from the sales of these two houses will be subject to income tax rather than capital gains tax.

(b) If Richard was subject to capital gains tax, tax would be payable at 20%. On the other hand, if he is subject to income tax, then he is deemed to be carrying on two trades, the profits from which are taxable as follows:

- 20% on the deemed gains from the sites
- 46·5% on the deemed profits from the construction operations.

The legislation states that the apportionment of profits between the two deemed trades should be on a just and reasonable basis.

Furthermore, on the assumption that he commenced to carry on the trade when he acquired the site in 2006, he would (unlike if he was subject to capital gains tax) be entitled to a deduction for the appropriate portion of the interest arising on the loan(s) in computing his trading income.

Finally, by virtue of the preliminary tax rules concerning the payment of income tax and capital gains tax he would (unlike for capital gains tax) be able to defer payment of the income tax until the filing date of the relevant income tax return without incurring any statutory interest.

(c) As a person carrying on a business which includes the erection of buildings, Richard would be regarded as a principal for RCT purposes. Therefore he should register as a principal for this purpose. In addition, he should deduct RCT at 35% on any payments made to a sub-contractor who does not have a C2 and forward it to the Collector-General.

This marking scheme is given as a guide to markers in the context of the suggested answer. Scope is given to markers to award marks for alternative approaches to a question, including relevant comment, and where well reasoned conclusions are provided. This is particularly the case for essay based questions where there will often be more than one definitive solution.

				Marks
1	**(a)**	**(i)**	2005	
			Peter	1
			Mary	1
			Paul	3
			2006	
			Peter	1
			Mary	$1^1/_2$
			Paul	$1^1/_2$
			2007	
			Peter	1
			Mary	1
				11
		(ii)	Capital allowances	$1^1/_2$
			Irish rental income	$2^1/_2$
			UK rental income	1
			Maintenance payments	$1^1/_2$
			Health expenses	1
			Tax bands	1
			Single person credit	$^1/_2$
			Age tax credit	$^1/_2$
			Single parent tax credit	$^1/_2$
			UK rental income tax credit	$^1/_2$
			PRSI	1
			Levies	$1^1/_2$
				13
		(iii)	Preliminary tax due date	1
			Filing date	1
				2
	(b)	2008 – Apportion income		$1^1/_2$
		Review 2007		$1^1/_2$
		Increase in assessable income for 2007 likely		1
				4
		Total		**30**

				Marks
2	**(a)**	**(i)**	Add-backs:	
			Depreciation	$^1/_2$
			Pension contributions	$^1/_2$
			Motor expenses	2
			Legal and professional fees	$2^1/_2$
			Repairs and renewals	$^1/_2$
			Capital allowances:	
			Wear and tear	3
			Balancing allowance	1
			IBAA	$1^1/_2$
			UK dividends	1
			Irish dividends not chargeable	$^1/_2$
			Chargeable gain re P Ltd	$2^1/_2$
			No chargeable gain on the disposal of shares in A Ltd	$1^1/_2$
			Corporation tax rates	1
			Corporation tax credit for trading losses	1
				19
		(ii)	Corporation tax payment dates	1
			Corporation tax return filing dates	1
				2
	(b)		Two accounting periods	$1^1/_2$
			Implications for corporation tax payment and return filing dates	$1^1/_2$
			Time apportionment	1
				4
			Total	**25**

3	**(a)**	Sale of site on 1 June:	
		Incidental costs	$^1/_2$
		Indexed base cost	2
		Transfer of farm to son:	
		Retirement relief applies	$1^1/_2$
		Letting to son	1
		Farmed it for, at least, 10 years	$1^1/_2$
		Compensation for part of garden:	
		Disposal of interest in PPR	$1^1/_2$
		Current use value: – no dilution in PPR	$1^1/_2$
		Compensation for personal injury:	
		Specifically exempt	$1^1/_2$
		Sale of site on 10 November:	
		Computation of loss	2
		Sale of tractor:	
		Subject to CGT	$1^1/_2$
		Computation of gain	$1^1/_2$
		Summary computation:	
		Set off of losses from disposal of development land and losses carried forward	2
			18
	(b)	Capital gains tax due dates	2
			2
		Total	**20**

			Marks
4	(a)	Name, address and VAT number of the party issuing the invoice	$\frac{1}{2}$
		Name and address of the party to whom issued	$\frac{1}{2}$
		Date of issue of invoice and invoice number	$\frac{1}{2}$
		Date of supply	$\frac{1}{2}$
		Description of goods and/or services supplied	$\frac{1}{2}$
		Quantity and value of goods	$\frac{1}{2}$
		VAT rates chargeable	$\frac{1}{2}$
		VAT exclusive price of goods and services	$\frac{1}{2}$
			4
	(b)	Ability to claim a credit for VAT suffered	1
		Input credit in relation to vatable activity	1
		VAT exempt activity	$\frac{1}{2}$
		Specific prohibition	$\frac{1}{2}$
		Part vatable activities	1
			4
	(c)	15 days after the end of the month in which the service is completed	2
	(d)	Agent is not correct	$\frac{1}{2}$
		Transfer of an undertaking	1
		No supply for VAT purposes	1
		Not entitled to a VAT credit	$\frac{1}{2}$
			3
	(e)	Revenue official not correct	$\frac{1}{2}$
		European Court of Justice ultimate arbiter on VAT matters	$1\frac{1}{2}$
			2
		Total	**15**
5	(a)	Specific intention of selling houses	$\frac{1}{2}$
		Adventure in the nature of a trade	1
		Legislation in Taxes Consolidation Act 1997	1
		Income tax would apply	$\frac{1}{2}$
			3
	(b)	Capital gains tax – all of gains at 20%	$\frac{1}{2}$
		Income tax – two deemed trades taxable at 20% and 46·5%	$1\frac{1}{2}$
		Just and reasonable apportionment	$\frac{1}{2}$
		Income tax – interest deduction	1
		No interest deductible if capital gains tax applies	$\frac{1}{2}$
		Preliminary tax benefit	1
			5
	(c)	Treated as a principal for RCT purposes	1
		Obligation to deduct RCT if sub-contractor has no C2	1
			2
		Total	**10**