



Examiner's report

P6 Advanced Taxation (IRL)

December 2011

General Comments

The examination paper was consistent with previous sittings and comprised of two sections. Section A was made up of two compulsory questions; question one for 35 marks and question two for 25 marks. Section B consisted of three optional questions of 20 marks each, of which candidates had to attempt two.

The performance of candidates overall showed a notable improvement over previous sittings. All but one candidate attempted both compulsory questions. In a small number of cases, candidates did not attempt a section of a question thereby having no opportunity to access these marks. In section B, questions four and five proved most popular with question five attracting the highest marks. Question three was poorly answered with candidates displaying a limited knowledge of both partnership losses and capital losses on share disposal.

The layout of answers was generally good with schedules being clearly linked with the reports, and in the main, logically structured. In the majority of cases, high professional marks were achieved. There was no evidence that candidates were rushed or had difficulty in completing the paper within the timeframe available.

As always, candidates are reminded to use the following guidelines in approaching the paper:

- Make use of the pre-exam 15 minutes reading and planning time to read all of the questions,
- Give careful consideration to the requirements in each question and the marks offered for each part of the requirements,
- Pay particular attention to the required layout of the answer e.g. memorandum, letter, etc. so as to best achieve the available professional marks in question one and two,
- Ensure that your knowledge of the Irish tax system is up to date. Candidates sitting the exam in 2012 must familiarise themselves with the changes introduced in the Finance Act(s) 2011,
- Revise the core areas covered at F6 level to enhance your proficiency in tax computation and understanding of the fundamental rules in preparation for the exam.

Specific Comments

Question One

The key issues in this question were well dealt with, including the recognition of gift and distribution implications of the free use/transfer of the townhouse to James, stamp duty implications on the various transactions, and the various issues that arose on liquidation. The supporting computations were reasonably well dealt with but failure to recognise some of the issues, set out below, meant that certain marks were lost:

Part (a)(i) Free use of townhouse:

Candidates generally did not recognise the look through provisions of a gift from a company and also that James received a gift from both himself and Martin. As a result the value of the gift had to be apportioned.

Part (a)(ii) Gift of townhouse:

Common errors included not recognising:

- that the withholding tax on the distribution could be collected by the company from James.
- that the transfer of an asset at undervalue reduces the base cost of shares which has capital gains tax implications.
- the look through provisions of a gift from a company and that James received the gift from both himself and Martin.

Many candidates incorrectly allowed a credit against CAT for the tax paid by the company on the adjusted chargeable gain and few reduced the value of the gift for the stamp duty arising.

Part (a)(iii) Sale of remaining properties and subsequent liquidation

This section was generally well attempted however candidates often excluded indexation when calculating the tax due by the company on the disposal of the properties. Other common errors included:

- Failing to deduct the capital gains tax due by the company from the value of the company's assets and liabilities in arriving at the net distributable cash.
- Not using separate base values of the shares, i.e. for Martin at date of incorporation and for James at date of receipt of shares, or apportioning these values based on the percentage shareholdings held, and finally not reducing the values for the undervalue arising on the transfer of the townhouse.

Part (a)(iv) Impact on liquidation on reliefs previously claimed

This part was well dealt with, with the exception of consideration of the €750,000 limit in considering the claw back for James. Some suggested the setting up of trusts or delaying the transfer of the townhouse until dwelling house relief could apply. Some marks were awarded for these suggestions.

Part (b) Alternative structures

Many students did not attempt this part. Those who suggested distributing assets in specie as part of the liquidation dealt with the matter well. Marks were awarded where students suggested the use of pension planning and termination payments.

Part (c) VAT on properties

This section was poorly answered with many candidates not recognising the two year rule in relation to the transfer of the retail property and that it was not redeveloped. As a result many treated the building as new premises and charged VAT on the sale. Few recognised that the letting of the property to a connected person gave rise to a cancellation adjustment and therefore VAT on the transfer of the townhouse to James would not arise. While many students recognised that the free use of the townhouse to James gave rise to a 'claw back' of VAT claimed, the adjustment was poorly dealt with.

Question Two

Overall this question was well attempted and good marks achieved. The key issues were well recognised but computational errors resulted in a loss of marks for many. Part (i) dealt with the capital gains tax exposure on George and good marks were achieved in the majority of cases. Common errors included suggesting retirement relief applied to George by not recognising his age was under 55, not recognising that principle private residence relief applied and not recognising that the loss arising on the disposal of the premises was a connected person's loss and as a result it could only be applied to the disposal of shares to Greg. Some candidates also failed to apply the correct territorial rules and as a result allowed loss relief on the disposal of the Spanish property.

Part (ii) considered the capital acquisitions tax and other exposures for recipients. In the main, this was well attempted. Errors occurred where candidates did not deduct the cost of the annuity in arriving at the taxable value of Greg's gift. Where the deduction was taken into account, many failed to correctly determine the value of the annuity as a cost for CAT purposes and simply took the annuity cost multiplied by 10 years. In the majority of cases, business relief was correctly identified and the non-qualifying assets noted. However, many failed to apply favourite nephew relief and consanguinity relief on the transfer of the premises. In respect of the other beneficiaries, the most common errors were:

- Not applying the age factor to Maura's right of residence.
- Incorrectly determining the value of Maura's life interest in the annuity.
- Not recognising the correct CAT thresholds for Sarah and Julie.
- Not recognising that Julie was subject to CAT by virtue of George's residence position.

Question Three

This question was poorly attempted with some basic issues not recognised such as the application of specified reliefs for income tax purposes; the treatment of rights issues for capital gains tax purposes, and the treatment of married couples in year of death. The marks awarded for this question were low. In the majority of cases, candidates did not read the requirements properly and spent time preparing a full income tax calculation which was not requested and for which no marks were available. The main areas of difficulty identified in this question were:

- The computation of case II income for the year of cessation with candidates displaying difficulty in determining the original assessable profits, under the ‘continuing basis’ for 2010. This would appear to be largely due to the treatment of partners’ salaries where some candidates treated these as subject to Schedule E. Similar issues arose in determining the penultimate year position on an actual basis.
- Candidates were not sufficiently familiar with the terminal loss rules while many did not allow loss relief at all in the determination of taxable income.
- A number of candidates incorrectly exempted the interest from the government securities.
- In relation to artist’s exemption many candidates failed to recognise that the relief should be restricted in any way. Of those who did recognise the relief, many were unable to correctly state the rules or show how the restriction was determined.
- Many candidates failed to time apportion Agnes’ income and taxed the full year’s pension instead.

Difficulty was also evident in the computation of the capital loss on the share disposal with the majority of candidates not recognising that the rights issue attach to the original shares and the disposal is not on a FIFO basis. In addition, the majority of candidates did not recognise that government securities were exempt. As a result of the above two issues, Part (b) of the question was very poorly dealt with.

Question Four

This question was well attempted with good marks being achieved. Part (a) of the question dealt with the VAT treatment of premises. Most candidates recognised that the property was liable under the Capital Goods Scheme and that various adjustments were required due to the change in usage. However, marks were lost in calculating the adjustments. Common errors included:

- Restricting the first interval adjustment to one twentieth and not the full 30% adjustment.
- Restricting the ‘big swing’ adjustment to one year’s adjustment.
- Failing to recognise that the property was not ‘new’ at the time of the proposed sale and that VAT would not apply. While a number of candidates suggested that an option to tax existed, few suggested that a refund of VAT to Celine would arise as a result.

Part (b) dealt with revenue audit issues and was, in the main, well attempted. Where errors occurred, it was where candidates were not familiar with specific provisions. For example, the ‘reverse charge’ principle for VAT purposes or the requirement to register with the PRTB. Most recognised that that PAYE/PRSI should be operated on the cash wages but few suggested that the wages should be grossed up.

Part (c) dealing with tax default categories was largely very well dealt with full marks being achieved by many candidates.

Question 5

This question was the most popular optional question achieving high marks in many cases. Part (a) dealt with trading structures and most candidates demonstrated a good knowledge of the different treatment of a branch versus a subsidiary. This part was largely well answered.

Part (b) dealt with unapproved share option schemes and was surprisingly poorly dealt with. While most recognised that the options were liable to income tax, many failed to recognise that the treatment of such options depends in the first place on the time available for exercise resulting in a loss of marks. In addition, many did not comment on the capital gains tax treatment of the shares acquired under option.

Part (c) was mainly well dealt with and maximum marks were achieved by many. However, many suggested that a termination payment could be a tax efficient part of a remuneration package.