

Examiner's report

F6 (IRL) Taxation

December 2017

General Comments

There were two sections to the examination paper and all questions were compulsory. Section A consisted of 15 multiple choice questions (two marks each) which covered a broad range of syllabus topics. Section B had six questions, four of which were worth 10 marks each and two longer questions worth 15 marks. The questions in Section B examined the main syllabus areas of Corporation Tax, Income Tax, Capital Gains Tax and Value Added Tax and Administration of the Irish taxation system. Overall the paper was well answered.

The following paragraphs report on each section and focus on some of the key learning points.

Specific Comments

Section A

It was good to see that almost all candidates attempted all questions.

Section A questions aim to provide a broad coverage of the syllabus, and candidates should aim to revise all areas of the F6 syllabus, rather than attempting to question spot. The following questions from the December 2017 paper are reviewed with the aim of giving future candidates an indication of the types of questions asked, guidance on dealing with exam questions and to provide a technical debrief on the topics covered by the specific questions selected.

Candidates should be aware that it is in their interest to select one of the choices to each question as there is nothing to be gained by omitting an MCQ.

Sample Questions for Discussion

Example 1

Simon commenced to trade as a sole trader on 1 July 2015 and prepared accounts to 31 December 2015. He prepares accounts annually thereafter. Simon bought a new machine on 1 September 2015 for €8,000, which was used 100% for business purposes. He sold this machine on 1 December 2016 for €7,200.

What is the balancing allowance/charge arising on the disposal of the machine in the tax year 2016?

- A** €800 balancing allowance
- B** €300 balancing allowance
- C** €466 balancing allowance
- D** €200 balancing charge

The correct answer was B €300 balancing allowance.

This question was testing the candidates' knowledge of how capital allowances are applied in a commencement situation, and the calculation of balancing allowance/charge on disposal of an asset. Capital allowances are available to a business, where an asset is purchased for use in the business and that asset is in use on the last day of the accounting period. The rate of wear and

tear is 12.5%, the allowance available to a business may be restricted where (i) the asset is not used 100% for business purposes and/or (ii) the accounting period is less than 12 months.

For the tax year 2015 Simon would be able to claim a capital allowance of €500, ie $€8,000 \times 12.5\% \times 6/12$, reflecting the six month accounting period. In 2016 no wear and tear allowance can be claimed, as the asset was not in use on the last day of 2016 accounting period. The tax written down value (TWDV) of the asset on disposal was €7,500 ($€8,000 - €500$), and so the balancing allowance was €300, ie the sales proceeds of €7,200 less the TWDV of €7,500.

The most common error made by candidates was to allow a full year of capital allowances in 2015.

Example 2

Pat, a single man, aged 63, has a full medical card. During the tax year 2016 Pat earned a salary of €58,000 and received Irish deposit interest of €1,100 net.

What is Pat's universal social charge (USC) liability in tax year 2016?

- A €1,500
- B €2,483
- C €2,544
- D €1,533

The correct answer was A €1,500

As this question was testing the candidates' ability to apply the rules for calculating USC, it would be good to remember that most of the information you need will be in the tax tables provided at the front of the exam paper.

All income subject to Deposit Interest Retention Tax (DIRT) is exempt from USC and so the only income assessable is Pat's salary. Pat is a medical card holder and as his aggregate income is less than €60,000 the maximum USC rate that applies for 2016 was 3%.

Pat's USC liability is therefore calculated as $(€12,012 \times 1\% \text{ plus the balance of } €45,988 \text{ at } 3\%) = €1,500$.

Most candidates seemed to be aware that income liable to DIRT is exempted from USC, however they did not seem to be aware of the maximum rate rule.

Section B

Question One

This 10-mark question examined VAT.

The standard of answering in this question was good, the calculation of the VAT on the sales was excellent however candidates could have performed better on calculating the VAT on inputs.

In calculating the VAT deductible on diesel it was necessary to allocate the diesel cost between the exempt tour bus sales and the taxable courier services. It was good to see that this was correctly dealt with by most candidates.

Candidates should be aware that most maintenance and repair activity is charged to VAT at 13.5% and it is best to assume the most common occurrence unless the question indicates otherwise.

As the website development costs related to the whole business it was again necessary to apportion the cost between the exempt activity and all other business activities. This apportionment should be done using the VAT exclusive turnover figures.

While most candidates are doing this, just a reminder to always check before you do any VAT calculations whether the figures you are dealing with are VAT inclusive or VAT exclusive.

Question Two

This 10 mark question examined the Capital Gains Tax area of the syllabus, the focus in this question was on Principal Private Residence (PPR) relief where we had a development gain, a disposal of a chattel and part disposal of land.

The most common approach to the calculation of a PPR gain where there is a development gain also, is to (i) compute the gain on the disposal of the house as though there is no PPR relief available and then (ii) to recompute the gain ignoring any developmental proceeds and costs. The gain from (ii) will then be available in all or in part depending on the qualifying periods of residence in the house. Most candidates used this approach however other alternatives are also possible.

Lauren's absence from the house while working in Ireland was for a period of five and a half years, of which a maximum of four years qualifies as a deemed occupancy. This caused the PPR relief to be restricted to 204/222.

A non-wasting chattel is exempt where the sales proceeds are less than €2,540, the disposal of the antique tables and chairs for €3,800 does not fall into this category. Some candidates get confused on this rule and assume there is an exemption if the gain on disposal is less than €2,540. Indexation relief is not possible as it would increase the loss. It is worth noting that the loss on the disposal of this asset cannot be offset against the other gains arising as it was incurred in a connected party transaction and can only be relieved against a gain arising at some future date with the same connected person.

The part disposal rule was widely known and correctly applied.

Question Three

This 10-mark question examined in part (a) the computation of taxable rental income for an individual and in part (b) the exemption from income tax available for persons aged 65 and over.

Part (a) of this question was generally well answered.

In respect of property 1, candidates should remember that tax relief is not available for Local Property Tax (LPT) paid by the owner of an investment property against their rental income.

In relation to Property 2, many candidates did not appear to know the formula that allows you to calculate the taxable portion of a lease premium that is received by a lessor. The formula of $P \times (51 - N)/50$ should be learned, P represents the full amount of the premium received and N represents the number of years in the lease.

Where interest is incurred on a loan for a commercial property, and some of that interest arises in a period prior to the letting of the property for the first time, then tax relief will not be available on this portion of the interest.

The rent a room relief that applied to property 3 was widely known.

Part B was not well answered. Many candidates did not seem to be aware of the low income age exemption rule where an individual is exempt from income tax where their income does not exceed €18,000 or where there is a married couple/civil partnership where one spouse / civil partner is aged 65 or over the income limit that applies is €36,000.

Question Four

This 10-mark question covered corporation tax, part (a) looking at the rules that determine when an accounting period ends and the allocation of income arising and part (b) that dealt with the calculation of start-up relief and circumstances that would cause the relief not to be available to a start-up company.

Part (a) An accounting period for corporation tax cannot exceed 12 months, so where a set of accounts exceeds 12 months it must be broken down. In this question the set of accounts covered a period of 27 months. The first accounting period for corporation tax was the first 12 months, the second accounting period was also 12 months and the third was three months.

The second part of this question, which required the candidates to allocate trade income on a monthly basis, interest income to the period it was received and rental income on an accruals basis, was well answered. Marks were allocated when these rules were applied even though the accounting periods for corporation tax were incorrectly set up.

Candidates are reminded that Irish dividend income received by Irish resident companies is exempt from corporation tax.

Part (b)(i) The amount of start-up relief available to a company is restricted to the amount of employer's Pay Related Social Insurance (PRSI) paid by the company during the year. There is a maximum of €5,000 employer's PRSI allowed in respect of each employee. While this question was reasonably well answered some candidates were not aware of the €5,000 restriction.

(ii) The question asked candidates to identify two circumstances in which start-up relief is not available however, most candidates were only aware of one.. It is also worth remembering that marginal relief is available where a company's tax liability exceeds €40,000 but is less than €60,000

Question Five

This 15-mark question was an income tax computation for a separated couple. In the introduction line to the question it was stated that the couple were legally separated and so any maintenance payments should then have been taken as legally enforceable.

Some general comments may be useful. Candidates should remember that they are expected to state the income source/class to which income belongs e.g. Schedule D Case I. Where candidates performed less well than expected it was generally because they did not use the standard income tax pro-forma layout. It is essential that all candidates use this layout as it helps candidates to reduce the number of errors made. Some candidates calculated the PRSI and USC liabilities of the taxpayers however, there was no requirement to do this in the question. Where a candidate performs work they are not required to do they will not be allocated marks for this work and they are also using up their valuable exam time.

Paul had Schedule E income but as a director holding 20% of the share capital of the company he was a proprietary director and so was not entitled to the PAYE credit but instead would receive the earned income tax credit. His dividend income needed to be grossed up as Dividend Withholding Tax (DWT) had been deducted. Candidates should also remember that the special DIRT rate of income tax only applies to deposit interest and not to dividend income.

For tax relief purposes Paul is only allowed to deduct maintenance payments paid in respect of his separated spouse from his gross income. The rules on relief for third level fees was not always correctly applied, candidates should be clear on this relief as it is widely availed of by taxpayers.

Sheena's Schedule D Case I income and capital allowances were well answered. Again the maintenance payments on which she was assessable were not always correctly calculated. Sheena's tax credits were generally correct with candidates knowing the rules for tax relief on medical expenses and knowing that relief is given at source for private medical insurance.

Question Six

This 15-mark question was based on a core area of corporation tax.

Part (a) was well answered, with add back and deductions well laid out using the now established format of stating the item with the relevant amount or zero. Candidates are advised to apply this format.

In many instances candidates set out the lease payment restriction formula incorrectly. It is important to remember that it is the qualifying lease payment x (Cost of the car – Relevant limit)/Cost of the car.

The chargeable gain is adjusted by a factor of 33%/12.5%, and it was good to see that many candidates carried out this adjustment.

The interest of €8,000 incurred on a loan used to purchase ordinary shares in an associated company was correctly added back, however many candidates failed to deduct the interest later as a charge before arriving at profits liable to corporation tax. It is also worth noting that protected interest can be offset against investment income prior to being offset against income taxable at 12.5%.

Part (b) In this part of the question the candidate was being tested on the rules that allow relief for capital allowances relating to rental income and relief for rental losses.

In quite a few instances candidates stated that the interest earned on government securities was exempt, which it is not, perhaps getting mixed up with the exemption of the gain/loss on the disposal of Irish government securities.

Rental capital allowances may in the first instance be offset as a deduction against income from the source from which they arise and then against all profits (including chargeable gains) of the same accounting period or for a preceding period of the same length. The relief is given on a € for € offset basis, there is no calculation necessary..

Rental losses may be offset only against rental income of a previous accounting period of the same length or may be carried forward indefinitely.