Examiner’s report
F6 (IRL) Taxation
June 2016

General Comments
There were two sections to the examination paper and all of the 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 five questions, three of which were worth 10 marks each and two longer questions worth 15 marks, the questions examined the main syllabus areas of Corporation tax, Income tax, Capital Gains Tax and Value Added Tax. The following paragraphs report on each section and focus on some of the key learning points.

Specific Comments

<u>Section A</u>

It was very pleasing to see that almost all candidates attempted all of the questions. Candidates preparing for the next examination of F6 are advised to work through the MCQ’s from the recent past papers and sample 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 two questions from the June 2016 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 are to be reminded 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 from Section A

Example 1

Max commenced to trade on 1 July 2015. He prepared his first set of accounts for the period to 31 December 2015 and plans to prepare accounts annually to 31 December. On 1 July 2015, Max bought a category B car for €26,000. The business use of the car is 60% of its total usage.

What is the maximum amount of capital allowances that Max can claim on the car for the tax year 2015?

A €1,500
B €900
C €1,800
D €975

The purpose of the question was to test a candidate’s knowledge on computing capital allowances for a sole trader, on a motor car used for private and business purposes. There was also the additional problem that the length of the accounting period in which the allowance was being claimed was of six months duration.

The correct answer was B

Step 1
A candidate should note that the car is category B. A candidate should know that regardless of the cost of the motor car, a motor car that is in category A, B or C will attract capital allowances based on a value of €24,000. This information is contained in the tax reference material. The wear and tear rate that applies to the motor car is 12.5%. and so at the end of step 1 we will have €24,000 x 12.5% = €3,000.

Step 2
Next a candidate should note the business use of the motor car as the capital allowance computed under step 1 will be restricted to the business use percentage. In this case that will be €3,000 x 60% = €1,800.

Step 3
The full capital allowance as computed under step 2 above will only be available if (i) the asset is in use on the last day of the accounting period and (ii) the accounting period is of 12 months duration. Candidates will note that the car is in use by the business at 31 December 2015. However the accounting period is of six months duration as the commencement rules are applying so the capital allowance from step 2 of €1,800 is restricted by 6/12 to €900.

The business commenced the trade on 1 July 2015 and bought the car on that first day of trading, if however the car had not been purchased and used until 1 October this would not have further restricted the capital allowances available as capital allowances are restricted only for the length of the accounting period and not the length of ownership of an asset within a period.

This question could have been answered better in the exam. Candidates should practice this type of question with different type of car category and business usage percentages.

Example 2

A developer is selling a show house for €200,000 inclusive of value added tax (VAT). The sales price includes furniture worth €30,000, inclusive of VAT.

What is the amount of VAT payable by the developer on the sale of the show house?

Note: The lower rate of VAT applies to the sale of immovable property while the standard rate of VAT applies to the sale of furniture.

- **A** €23,789
- **B** €37,398
- **C** €29,850
- **D** €25,830

The correct answer was D

This question was testing a candidates knowledge that where a VAT registered trader supplies a “package”, in this case the house and the furniture, and the two items are clearly separately identifiable, with none being the “principal element”, then VAT will be charged on each item separately at the relevant VAT rate. The question also tested a candidates knowledge of how to calculate the VAT element of a price that is VAT inclusive.

The question required a candidate to apply the lower and standard rates of VAT, both of which are given in the tax reference material.

Step 1
Calculate the VAT inclusive price of the house. That is the €200,000 less €30,000 = €170,000. To remove the VAT on the house we need to divide €170,000 by 113.5%, and then multiply by 13.5% to give the VAT, €170,000/113.5% x 13.5% = €20,220 VAT.

Step 2
Calculate the VAT included in the price of the furniture. VAT inclusive cost is €30,000, to remove the VAT we need to divide that sum by 123%, and then multiply by 23%, €30,000/123% x 23% = €5,610.

Step 3
Add both amounts of VAT together €23,789 + €5,610 = €29,399.

It is important that future candidates are comfortable in being able to calculate VAT from a VAT inclusive price.

<u>Section B</u>

Question One

Part (a) of this 10-mark question covered the use of trade and non-trade charges to reduce or eliminate a company's corporation tax liability.

The question tested how relief could be claimed for trade and non-trade charges. Candidates should know that relevant trade charges are deductible against trade income of the accounting period in which the charge is incurred. Any excess of a trade charge over relevant income may be relieved on a value basis against investment income of the current period or used to create or augment a trade loss forward. Unrelieved trade charges of an accounting period cannot be carried back to a previous period.

For non-trade charges, the legislation does not specify the order of use, however best practice requires that they are offset in the first instance against income taxable at 25% in the current period and any excess can then be offset on a euro for euro basis against income taxable at 12.5%. If at the end of an accounting period a non-trade charge is partly unused, the balance unused is lost. Non-trade charges may not be carried back to a previous accounting period or forward to a future period.

In past examination papers trade and non-trade charges were examined in the main corporation tax question. This may have caused some candidates to omit learning about charges and as a result may have found it difficult to answer this question. It is important that candidates aim to cover the full syllabus as it is essential to have a good knowledge base, particularly of more difficult areas of the syllabus, as you progress to the more advanced tax paper.

Part b, required candidates to explain how loss restriction applies where a company files their accounts more than two months late. This is an important restriction and candidates should know the implications of late filing for companies with losses. Candidates should aim to ensure that they have specific knowledge of this restriction rather than a general idea.

Question Two
This 10 mark question examined the capital gains tax (CGT) area of the syllabus.

Part (1) was not well answered. Candidates should be aware that a gain arising on the disposal of wasting assets used for business purposes is a chargeable gain. Where an asset is not used wholly for the purpose of the trade then the proportion that reflects the business use only is taxable.
Where a loss occurs on the disposal of a wasting asset used in business there is no relief for capital gains tax purposes as the loss is covered by wear and tear allowances or balancing allowance.
Candidates should not adjust the sales proceeds when calculating the gain (avoid getting mixed up with the balancing allowance/charge calculation), as in CGT we only compare the actual sales proceeds with the actual cost.

Parts (2) and (3) were generally well answered.

In a question that has one individual/couple disposing of a number of assets during the year, it is important that candidiates calculate the gain/loss on each transaction separately and then make a summary by period of the gains/losses, arriving at a total gain/loss for each period. Only then should the annual exemption be applied and the total gain less annual exemption is then taxed at the relevant CGT rate (33% currently). It is important not to calculate the tax after each separate transaction or to apply the tax rate to the total gain before the annual exemption.

Part (b)
In general well answered, future candidates are advised to be aware of payment dates and be able to get these easy marks. When giving a date it is important to give day, month and year. So for due date of payment for a gain incurred in October 2015 you must state 15 December 2015.

Question Three
This 10-mark question examined the value added tax (VAT) area of the syllabus.

This was a well answered question, however some points worth noting:
Part (a) It is important to read the question noting (i) are the amounts VAT inclusive or exclusive and (ii) the VAT rate to be applied and (iii) the basis of accounting for VAT in use i.e. cash or invoice.
The majority of candidates correctly noted the additional lower rate of VAT on admission fees. VAT rates are given in the reference material.
It is important to read all questions carefully. This question stated that the €700 invoice from the UK supplier was VAT exclusive, yet many candidates treated this as if it were VAT inclusive.
While the business accounted for VAT on a cash receipts basis, this means that you only pay VAT when you receive payment for your sales, however you still continue to claim your VAT inputs when invoiced by suppliers. You don't have to pay the invoice in order to deduct the VAT.

Part (b) was well answered.

Part (c) Candidates were not fully aware of when it is possible to file annual VAT returns. This is important for small businesses as it can substantially reduce administration costs.

Question Four

This 10-mark question on Income tax examined the areas of pre-trading expenses, income averaging for farmers, industrial buildings allowance on a second hand building and excess Case V capital allowances.

Part (a) Candidates are to be reminded that theory areas of the syllabus are important and answers should be specific to the question.

Part (b) Farm Income averaging is now based on a five year averaging period, it is important to be aware of recent legislation changes. When calculating industrial building annual allowance (IBAA) for a second had building it is important to remember that the qualifying cost is the lower of the original qualifying cost or the price paid by the second hand purchaser. The qualifying cost is then spread over the remaining tax life of the industrial building. This has been examined in the long corporation tax question in the past but proved difficult for many candidates.
Another key point to note is that excess case V capital allowances may be offset against other income, however in income tax it is restricted to a maximum of €31,750 per annum. Just for information purposes this restriction does not apply in corporation tax.

A final comment on this question is that it is very important to read the question requirement, part (b) required candidates to calculate the taxable income. Some students calculated the tax payable. It is important for time management purposes to ensure that you only do work for which you can get marks.

Question Five

This was a 15-mark income tax question, overall it was well answered.

Part (a) examined the calculation of the taxable amount of a redundancy payment. This was generally well answered, it is important to point out that the formulae required are in the reference material and that the N in the formula stands for the number of years of <u>complete</u> service, so we should in this question be using 34 years. Candidates should know which payments received by an individual are taxable in the first instance, statutory redundancy and pension lump sum up to €200,000 are completely exempt.

In part (b), candidates should ensure that they are aware of the rules and limits for applying Rent a room relief. The home renovation incentive scheme is being widely used by taxpayers and while new it is important to know how relief under this scheme can be claimed. Irish dividend income received net is grossed up by dividing by the standard rate of income tax, and candidates should know that there is a difference between Case IV and Schedule F. In order to avoid making mistakes on the basic tax credits, candidates should be clear on medical insurance, and medical and dental expenses.

Question Six

This 15-mark question, part (a) was on the calculation of a fairly straight forward corporation tax liability computation, which is normally well answered.

Candidates are reminded of the new format for answering, showing zero's where addbacks are not required. There is no restriction on motor running expenses for a company, a restriction will only apply where there are car lease payments of which there were none in this question, and that restriction will depend on the cost and category classification of the car. The adjustment of the capital gain for inclusion in other income of the company was omitted in most instances.

Where a tenant pays a lease premium on a building, the lease term being for 50 years or less, the tax treatment is that the leassor will pay income/corporation tax on a portion of the lease payment received as determined by the formula P x (51-N)/50. The leassee will get tax relief on this portion spread over the life of the lease. Many candidates did not appear to be aware of this treatment.

Candidates should be aware that interest earned on monies on deposit is not taxable until received.

Part (b) Candidates are reminded that there is a very good article on New companies start-up relief in the technical resources for F6 (IRL). A general idea of startup relief seemed to prevail but the conditions to qualify and the calculation of the actual amount of the relief available to Blue Ltd were not well known by candidates. This is an important relief and candidates should aim to be know the area well. Also many candidates did not seem to know the difference between Company start-up relief and Start your own business relief in Income tax.