



# Examiner's report

## P6 Advanced Taxation (IRL)

### June 2012

#### General Comments

The examination consisted of two sections. Section A is compulsory and contained question one for 29 marks and question two for 31 marks. Section B comprised three further questions of 20 marks each of which candidates were required to attempt two.

All candidates attempted all four questions, and there was no evidence of time pressure. Where sections of questions were left unanswered by candidates, this appeared to be due to a lack of knowledge or poor exam technique, as opposed to time pressure.

The performance of candidates was consistent with previous sittings. In the optional section, questions three and four proved most popular with question three attracting the highest marks. VAT sections both of question one and question four were poorly attempted by candidates showing a lack of knowledge of the fundamental rules.

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 in question two. There was no evidence that candidates were rushed or had difficulty in completing the paper within the timeframe available.

A number of common errors arose in candidate's answers which should be noted for future sittings:

- Applying the annual CGT exemption to a company.
- Incorrect application of territorial rules.
- Poor knowledge of the operation of VAT.
- Mixing up CAT and CGT reliefs, for example allowing CGT costs in preparing a CAT computation, including allowing original costs of acquisition as a deduction.

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. Please note that the professional marks are now allowed in either question one or question two in section A only.
- Ensure that your knowledge of the Irish tax system is up to date. Candidates sitting the exam in December 2012 must familiarise themselves with the changes introduced in the Finance Act 2012.
- 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

This question dealt with a group of companies and the requirements included: the computation of group loss relief; capital gains tax group relief on the transfer of assets and subsequent use of loss, VAT 13A provisions and the disposal of a subsidiary company. Overall the question was well attempted with good marks being achieved by many candidates.

### **1(a)(i)**

This section accounted for six marks and required a corporation tax computation for each group company utilising available losses. The computations for each of the companies and claims for loss relief were largely very well dealt with and high marks were achieved in this section. Some common errors included:

- Not claiming trade loss relief against non-trade income on a value basis,
- Including the loss forward in Young Ltd for the purposes of group relief,
- Claiming group relief for the capital losses in Young Ltd against Jasper Ltd.

Most candidates laid out their answer in columns which made it easier to view their relief claims. The loss schedule was largely well done.

### **1(a)(ii)**

Most candidates recognised that in order to utilise the capital loss in Young Ltd, the asset in Jasper Ltd must be transferred across to Young Ltd. However, a number of candidates did not recognise that the loss in Young Ltd was a 'pre-entry' loss and therefore had to be split between pre and post entry losses. Where this was recognised, candidates scored well. Few recognised that once the asset was transferred to Young Ltd, that higher Case I loss relief became available for offset against other income in Jasper and Betty Pink.

### **1(b)**

The VAT issue was very poorly dealt with. Few students seemed to be aware of 'VAT 13A' relief. Many candidates offered incorrect suggestions as options to alleviate the cash flow problem. These included charging VAT at 21% on all exports so that you could claim an input credit, suggesting that the exports were exempt, which meant you could not claim input credit, and suggestions that more sales should be targeted to Irish customers.

As noted above, the poor knowledge of basic VAT provisions suggests a lack of core taxation knowledge that should be evident at this level.

### **1(c)**

This section was largely well attempted and most candidates structured their answers in a clear and logical manner. Most candidates determined the net cash position of disposing of Betty Pink under the two options suggested.

Many candidates did not recognise the application of participation exemption relief and as a result spent time calculating the capital gains tax exposure. In calculating the capital gains tax exposure on the sale of the assets, most candidates correctly calculated the capital gain on the disposal of buildings and goodwill while some incorrectly included a capital loss on the furniture and fittings. In arriving at the net of liquidation values, many candidates failed to deal with the liquidation implications of Betty Pink after disposing of its assets. In the main, VAT was not considered by candidates.

## **Question Two**

Overall this question was well attempted and good marks were achieved.

### **2(i)**

The main issues in this section were well recognised but computational errors resulted in a loss of marks for many. Part (i) dealt with the capital taxes issues arising on the disposal of shares in a family company from

father to son. Candidates generally scored well in this section, the majority recognised the retirement relief for CGT purposes and business relief for CAT purposes. Many correctly identified the impact of the investments on the reliefs and good attempts were made at computing the resultant taxes.

Common errors included:

- Incorrectly calculating the market value of the company, including using the Balance Sheet Net Asset Value, not including goodwill or the investments, or failing to deduct the long term liabilities.
- Allowing consanguinity relief on the transfer of shares.
- Calculating Retirement Relief by determining the gain on the disposal of the investments as an asset in themselves.
- Failing to recognise the CGT/CAT offset
- Not applying the correct business asset formula to determine CAT Business Relief but instead using the chargeable business asset/chargeable asset formula for CGT retirement relief purposes.

## **2(ii)**

This section sought to deal with the capital taxes implications of separating the trade from the investments into two separate companies. This required restructuring and a number of candidates made a reasonable attempt at the restructure, with many recognising the share for undertaking relief. However many were unaware of the conditions attaching to the relief.

For those who were not aware of the relief, some students made reasonable attempts at a restructure by suggesting the shares be sold to Walter, but funded by a termination package, followed with the transfer of the resulting trading company to Alex. Marks were awarded for relevant alternative suggestions.

With regard to the restructure which would consist of an investment company and a trading company, few candidates dealt with the implications of an investment holding company and the option of liquidating same.

Four professional marks were available in this question for format and presentation, effectiveness of written communication, use of schedules and logical flow of the answer. In general, good marks were achieved by candidates with the reports well structured, appendices referenced within the document and presented at the end of the report.

## **Question Three**

This question was well attempted and good marks were achieved by many.

### **3(a)**

This section dealt with discretionary trust tax. For those candidates who were aware of the 6% once off and 1% annual charge, full marks were achieved even though they addressed these points generally in section (b). However some candidates did not deal with this at all and no marks could be attributed.

### **3(b)**

This section sought to address the CAT issues arising on the individual beneficiaries from benefits received from the trust. In general, candidates dealt with the various taxes well. Most recognising that the group one threshold applied, and many achieved full marks on recognising the availability of dwelling house relief for Alannah. Common errors included applying stamp duty to benefits arising on a death and not availing of the CGT credit against the CAT arising on the transfer of the investments. The income tax implications for both the trust and for Joseph on the income arising was also poorly answered.

Few candidates recognised the potential surcharge issues for the trustees while some used the group 2 threshold in respect of the remainder interest in the residential unit acquired by Joseph on Alannah's death.

The taxation implications for the trustees was well attempted with many recognising the income tax exposure for the trustees on income arising, as well as the capital gains tax arising on the increase in value of both the building and the investments. However, some incorrectly calculated CGT on the transfer of the absolute interest in the residential unit to Joseph on Alannah's death.

### **3(c)**

Most candidates scored well in this section. However, some candidates did not recognise the correct group threshold.

### **Question Four**

This question dealt with VAT on distance selling, the territorial rules for income tax and capital gains tax anti avoidance. Section (a) was very poorly answered and many candidates were clearly not aware of the implications of 'distance selling' at all. Suggestions offered were poorly considered and included suggesting that Catherine should only deal with registered persons, or keep her turnover down so she would not have to charge any VAT, Irish or UK.

Section (b) dealt with the territorial rules for a couple for income tax purposes and, in the main, candidates did not perform well on this part. This is somewhat surprising as this is an area that candidates should have achieved high marks.

Common errors included:

- Incorrectly applying the territoriality rules to Catherine. Joe's status was generally correctly identified.
- Not recognising that Joe's salary is fully taxable as he exercises his employment in Ireland.
- Failing to recognise the Limited Remittance Basis Relief for Joe.
- Failing to apportion Catherine's Case I profits on a commencement basis.
- Suggesting that 'Split year' relief would apply to Catherine.

In section (c), a number of candidates were familiar with the anti-avoidance measures and dealt with this issue well, however some were not fully aware about the different dates for determining the charge and the payment of CGT. It was notable from the answers provided that many candidates are not clear on the territorial rules for CGT purposes even without the anti-avoidance provisions. This again suggests that the fundamental rules need to be continuously revised.

### **Question Five**

This was the least popular question and attracted low marks overall.

#### **5(a)**

This section examined the taxation of termination payments and in general as well attempted. Many candidates correctly calculated the tax free element of the termination payment however failed to address the availability of top slicing relief. In the majority of cases, the lifetime tax free limit of €200,000 was ignored.

#### **5(b)**

This section dealt with Seed Capital Relief and many candidates seemed unaware of this relief. For those who were familiar with it, reasonable attempts were made to include the conditions and the nature of the relief. Some candidates suggested BES relief and EIS relief for which marks were also given. For those who were not aware of Seed Capital relief, the 'start-up company relief' was suggested. While this did not deal with the investment of Dan's funds, some marks were awarded.



**5(c)**

The important issue of 'contract for service' versus 'contract of service' was reasonably dealt with by the majority of candidates. However, while the majority of candidates concluded that Michelle was not an employee, they failed to adequately identify their reasons for reaching this conclusion. Few provided indicators of employment versus self-employment. This is a very important issue from a tax viewpoint and candidates need to have a better knowledge of this area.