

# Examiner's report

## P6 Advanced Taxation (IRL)

### June 2013



#### General Comments

Most candidates performed well on this paper.

In general candidates completed all questions and appeared to have sufficient time to do so. Some candidates performed very well and scored high marks. Overall the format and presentation of answers was quite good, with appropriate schedules used where necessary.

#### Specific Comments

Some points for attention arising from this sitting are:

- (i) Not all tax planning must be complicated. The timing of transactions can have a big impact on the tax outcome, particularly in relation to capital taxes and losses (see Question 1 (b) (i)).
- (ii) A thorough knowledge of the terms and conditions of the main reliefs continues to be important. This point was made in the last examiner's report (December 2012) and it appears that candidates worked on this area in the meantime. For example, a specific condition of retirement relief was examined as part of question 5 (and answered well – see below). The detailed conditions of favourite niece/nephew relief were examined in question 1. (and again generally answered correctly). Well done!
- (iii) Four professional marks are available in Question 1. In future candidates should ensure that answers are presented in such a way as to maximise these marks.
- (iv) Many candidates still do not have a sufficient understanding of VAT generally and international aspects (for all taxes).
- (v) Always read the question and its requirements carefully.

#### Question One

The scenario outlined a situation whereby an individual is in financial difficulty, following the collapse of her company and she is unable to fund the repayments on an investment property (which is in negative equity). She must now deal with capital gains tax arising on an overseas disposal and reduce her bank borrowings. Fortunately her uncle has a proposal to assist her, but the right tax advice is required. This is a topical situation and a range of issues are examined.

##### (a)

The issues in relation to the accountancy practice receiving a holiday voucher in lieu of a fee were examined. Many candidates did not answer this well and overlooked the possibility of a VAT/Income tax underpayment in the practice and digressed into discussing BIK and/or CAT issues which were not relevant.

##### (b)

###### (i)

The CGT arising on the USA property was generally correctly calculated. However many candidates did not adequately consider how this liability could be reduced. The timing of a transaction can have a very big impact on the taxes payable. In this situation, Mary needed to sell the apartment in 2012 in order to have a loss available for offset against the gain. Most candidates also overlooked the possibility of making a negligible value claim in 2012 in relation to the worthless shares in SPFS Ltd.

###### (ii)

This part was generally well answered and candidates scored well here.

###### (iii)

Many candidates either did not answer this part or did not correctly calculate the effect on borrowings after the various proposals were put in place. Very few candidates recognised the interest exposures.

###### (iv)

Most candidates recognised the applicability of sole trader commencement rules and the need for registration. A significant minority of candidates did not correctly address two basic issues in this question:



- Sole traders are assessed to tax on profits and not on drawings, and/or
- Company losses cannot be offset against sole trade profits.

This lack of understanding of basics causes me some concern as in practice clients will often ask basic questions such as these or variations of them. (Example: “ I am only taking €400 per week out of the business. Why then do I have such a large income tax bill?”)

Some candidates did not read the question properly and referred to Mary setting up a company and startup exemptions etc.

### **Professional Marks**

In general, candidates performed well here. As always, tidiness in presentation of calculations is rewarded with good marks.

However some candidates did not present the letter in the required format and wrote a memorandum instead. A few candidates started the letter with (presumably the email salutation)“ Hi Mary” which is obviously not appropriate in this situation. A minority of candidates produced very untidy workings and need to improve.

### **Question Two**

Expansion abroad is a key part of the life cycle of many businesses.

This question examined VAT, Corporation Tax and Income tax issues associated with the expansion of an Irish company into the UK market. The international aspects of these taxes are important elements of the P6 syllabus.

#### **(a)**

Most candidates performed either extremely well or extremely poorly in determining how the sales to the UK should be dealt with. A large number of candidates incorrectly mentioned “reverse charges” and claiming inputs.

#### **(b)(i)**

Most candidates were familiar with the ‘Permanent Establishment’(PE) issue and obtained the marks for identifying this. However many candidates had an incomplete understanding of what does and does not constitute a PE.

#### **(b)(ii)**

Most candidates determined the UK exposure to tax correctly in each of the relevant years but the basis of same was not always explained

#### **(b)(iii)**

Many candidates correctly suggested that the sales agent’s powers should be restricted but some simply suggested that a subsidiary should not be set up.

#### **(b)(iv)**

The issue of branch versus subsidiary was reasonably well dealt with but not always in the context of Mullins Ltd, forgetting that Mullins Ltd expected to be profit making.

#### **(c)**

Few candidates recognised the dual residency of John O’Brien and simply determined he was either UK or Irish tax resident.

### **Question Three**

The vast majority of Irish companies are close companies.

This optional question was attempted by most candidates and, although many candidates had difficulty in correctly identifying Alexis Ltd as a close company (part (a)), in general they demonstrated a good knowledge of the application of the specific close company rules.

#### **(a)**



This part was poorly answered and candidates are directed back to the definition of a close company.

**(b)**

The implications of a transfer of an asset at undervalue were well dealt with.

**(c)**

The CT computation was largely well dealt with, but of concern is that some candidates taxed the Franked Investment Income, whilst others taxed deposit interest at 30%.

**(d)**

The close company surcharge calculations were generally well dealt with. Where poorly dealt with, it was obvious that candidates had not revised the area and the required two computations for the different source of income and surcharge.

**(e)**

Most candidates suggested a dividend could be paid to avoid/minimise a surcharge but did not maximise their marks by identifying the timing of same.

#### **Question Four**

Candidates are often deterred by the perceived complexity of VAT on property. Most candidates chose not to attempt this question.

This optional question mainly examined VAT on property and other VAT issues including the VAT implications of partial exemption and self supplies. The (minority of) candidates that attempted this question generally performed well.

At this level the majority of marks are allocated for the correct application of tax law, rather than for reciting the rules. In this question there were six marks available for describing the operation of the capital goods scheme but the remaining fourteen marks were based on the application of VAT law to specific scenarios.

**(a)** The summary of the Capital Goods Scheme was largely well dealt with.

**(b)**

**(i)** Transfer of undertaking:

This was generally well answered but a number of candidates tried to tax each asset separately.

**(ii)** Sale of a redeveloped building.

and

**(iii)** Change of Use:

These were applications of the capital goods scheme rules outlined in (a) and were generally answered well.

**(iv)** Self Supplies: These were generally well dealt with, although some candidates did not correctly extract the VAT element from the gross figure of €2,000 by multiplying by 23/123. (The ability to do this is assumed at this level)

**(v)** Audit fee and electricity

This part addressed the area of partial exemption for VAT and its impact on input credits. There was some misunderstanding here. Most candidates did not correctly apportion the VAT element of the audit fee and many did not advise to apportion the light and heat.

### Question Five

There are specific rules governing the purchase of its own shares by a company, and these determine whether or not the transaction will be treated as a capital gains tax disposal or a distribution. As was the case in Question 4 the majority of the marks were available for the application of the rules to the situation outlined. In general candidates performed well on this question.

#### (a)

Most candidates performed well, recognising the conditions which must be met to obtain CGT treatment on a buy back.

#### (b)

Most candidates recognised that CGT treatment applied to Paul Murphy and did not apply to Ronald Keane.

It is important that candidates explain why the CGT treatment does or does not apply to Paul and Ronald, with reference to the rules outlined in (a). Many candidates did not take the time to do this and consequently did not optimise their marks. This is not a repetition of part (a) of the question but it is an essential application of the rules.

A significant minority of candidates did not analyse Paul's residence position correctly and jumped to the assumption that he had become non-resident and was ineligible for the CGT treatment. It is important to remain calm and apply the basic residence rules (current and prior year days) to situations such as this.

Most candidates displayed a thorough understanding of the rules of retirement relief and correctly identified that it did not apply to Paul. Well done.

A number of candidates unfortunately embarked upon a detailed (and irrelevant) discussion of the close company rules regarding loans from participators and (even more irrelevant) loans to participators. Please read the question carefully.

Many candidates did not refer to the stamp duty implications. Many candidates also forgot that the company is buying the shares and therefore it has the liability for stamp duty.

#### (c)

A number of candidates did not recognise the company law requirements of having sufficient distributable reserves (and that board resolutions were required). Many candidates missed the point that the repayment of the loan to Paul Murphy was not relevant in the context of distributable reserves. Some candidates confused cash reserves and distributable reserves.