Strategic Professional – Options

Advanced Taxation – Irish (ATX – IRL)

Tuesday 3 December 2019

ATX IRL ACCA EN

Time allowed: 3 hours 15 minutes

This question paper is divided into two sections:

Section A – BOTH questions are compulsory and MUST be attempted

Section B – BOTH questions are compulsory and MUST be attempted

Tax rates and allowances are on pages 2–8

Do NOT open this question paper until instructed by the supervisor.

This question paper must not be removed from the examination hall.

ATX – IRL

Think Ahead ACCA

The Association of Chartered Certified Accountants

SUPPLEMENTARY INSTRUCTIONS

1. You should assume that the tax rates and credits shown below, for the Finance Act 2017, will continue to apply for the foreseeable future.
2. Calculations and workings need only be made to the nearest Euro.
3. All time apportionments should be made to the nearest month.
4. All workings should be shown.

TAX REFERENCE MATERIAL

The following rates, credits, formulae and allowances are based on the Finance Act 2017 and are to be used for all questions in this paper.

Income tax rates

	Tax €
Single/widow(er)/surviving civil partner without qualifying children	
€34,550 at 20%	6,910
Balance at 40%	
Married or in a civil partnership (one income)	
€43,550 at 20%	8,710
Balance at 40%	
Married or in a civil partnership (dual income)	
€43,550 at 20%	8,710
€25,550 at 20%	5,110
Balance at 40%	
Single/widow(er)/surviving civil partner qualifying for single person child carer credit	
€38,550 at 20%	7,710
Balance at 40%	

Tax credits

	€
Single person's credit	1,650
Married person's/civil partner's credit	3,300
Widowed person or surviving civil partner's credit (without dependent children)	2,190
Home carer credit (maximum)	1,200
Single person child carer credit	1,650
Incapacitated child credit	3,300
Dependent relative credit	70
Age credit – single/widowed/surviving civil partner	245
– married or in a civil partnership	490
Employee/PAYE credit	1,650
Earned income tax credit	1,150
Third level tuition fees	Upper limit €7,000
Full-time qualifying courses	First €3,000 is ignored
Part-time qualifying courses	First €1,500 is ignored

Rates of PRSI
Self-employed – Class S

Rate 4%

Where income is above €5,000 the rate is 4% of reckonable earnings or €500, whichever is greater.

No PRSI where income is below €5,000 per annum.

Rates of PRSI

Employee – Class A

Rate	4%

No PRSI on earnings of €352 or less per week

Employee – Class K

Rate	4%

Rates of PRSI

Employer (for employees – Class A1)

Rate	10·85%

Universal social charge (USC) for all taxpayers

On the first €12,012	0·5%
On the next €7,360	2%
On the next €50,672	4·75%
On the balance	8%

For individuals, a surcharge of 3% applies in respect of relevant (non-PAYE) income that exceeds €100,000 per annum regardless of age.

For individuals aged 70 and over, and individuals who hold a medical card regardless of age, if aggregate income for the year is €60,000 or less, the maximum rate is 2%

Exemptions:
– Individuals whose income does not exceed €13,000 per annum
– All social welfare payments and income subject to DIRT

Retirement annuities

Age	**Percentage of net relevant earnings**
Up to 30 years	15%
30 years but less than 40 years	20%
40 years but less than 50 years	25%
50 years but less than 55 years	30%
55 years but less than 60 years	35%
60 years and over	40%

Cap on net relevant earnings of €115,000

Corporation tax

Standard rate	12·5%
Higher rate	25%

Value added tax (VAT)

Registration limits	
Turnover from the supply of goods	€75,000
Turnover from the supply of services	€37,500
Rates	
Standard rate	23%
Reduced rate	13·5%
Second reduced rate	9%

Capital gains tax (CGT)

Rate	
From 6 December 2012 to date	33%
From 7 December 2011 to 5 December 2012	30%
From 8 April 2009 to 6 December 2011	25%
From 15 October 2008 to 7 April 2009	22%
From 1 December 1999 to 14 October 2008	20%
Annual exemption	€1,270
Entrepreneur relief	
Rate for disposals on or after 1 January 2017	10%
Lifetime limit on gains	€1,000,000

Motor cars – limits on capital costs

Carbon emissions table:

Category A	Category B/C	Category D/E	Category F/G
0–120g/km	121–155g/km	156–190g/km	191g/km +

Category A/B/C vehicles – capital allowances/leasing charges are based on the specified amount of €24,000 regardless of the cost of the car.

Category D/E vehicles – capital allowances/leasing charges are based on 50% of either €24,000 or the cost of the car, whichever is lower.

Category F/G vehicles – do not qualify for capital allowances/leasing charges.

Benefits in kind
Motor cars

Business travel lower limit Kilometres	Business travel upper limit Kilometres	Percentage of original market value of car
0	24,000	30%
24,001	32,000	24%
32,001	40,000	18%
40,001	48,000	12%
48,001	Upwards	6%

Preferential loan rates

Loans used to fund the cost/repair of the employee's principal private residence	4%
All other loans	13·5%

Local property tax
Tax bands for valuation purposes

€	€
0–100,000	550,001–600,000
100,001–150,000	600,001–650,000
150,001–200,000	650,001–700,000
200,001–250,000	700,001–750,000
250,001–300,000	750,001–800,000
300,001–350,000	800,001–850,000
350,001–400,000	850,001–900,000
400,001–450,000	900,001–950,000
450,001–500,000	950,001–1,000,000
500,001–550,000	

Properties worth up to and including a value of €1 million will be assessed at a rate of 0·18%.

Properties worth more than €1 million will be assessed on their actual value at 0·18% on the first €1 million and at 0·25% of their actual value on the portion above €1 million.

Indexation factors for capital gains tax

Year expenditure incurred	Multipliers for disposals in the year ending 31 December 2004 *et seq*	Year expenditure incurred	Multipliers for disposals in the year ending 31 December 2004 *et seq*
1974-75	7.528	*1989-90*	1.503
1975-76	6.080	*1990-91*	1.442
1976-77	5.238	*1991-92*	1.406
1977-78	4.490	*1992-93*	1.356
1978-79	4.148	*1993-94*	1.331
1979-80	3.742	*1994-95*	1.309
1980-81	3.240	*1995-96*	1.277
1981-82	2.678	*1996-97*	1.251
1982-83	2.253	*1997-98*	1.232
1983-84	2.003	*1998-99*	1.212
1984-85	1.819	*1999-2000*	1.193
1985-86	1.713	*2000-2001*	1.144
1986-87	1.637	*2001*	1.087
1987-88	1.583	*2002*	1.049
1988-89	1.553	*2003 et seq*	1.000

Capital acquisitions tax

Class thresholds (with effect from 12 October 2016)

		€
Class 1:	Child or minor child of deceased child (or inheritance taken by parent):	310,000
Class 2:	Lineal ancestor (other than inheritance taken by parent) Lineal descendant (other than a child or a minor child of a deceased child) Brother, sister, child of brother or sister	32,500
Class 3:	Any other person	16,250
Rate		33%

Life interest tables for capital acquisitions tax

Years of age	Joint factor	Value of an interest in a capital of €1 for a male life aged as in column 1	Value of an interest in a capital of €1 for a female life aged as in column 1	Years of age	Joint factor	Value of an interest in a capital of €1 for a male life aged as in column 1	Value of an interest in a capital of €1 for a female life aged as in column 1
0	·99	·9519	·9624	50	·92	·7287	·7791
1	·99	·9767	·9817	51	·91	·7156	·7683
2	·99	·9767	·9819	52	·90	·7024	·7572
3	·99	·9762	·9817	53	·89	·6887	·7456
4	·99	·9753	·9811	54	·89	·6745	·7335
5	·99	·9742	·9805	55	·88	·6598	·7206
6	·99	·9730	·9797	56	·88	·6445	·7069
7	·99	·9717	·9787	57	·88	·6288	·6926
8	·99	·9703	·9777	58	·87	·6129	·6778
9	·99	·9688	·9765	59	·86	·5969	·6628
10	·99	·9671	·9753	60	·86	·5809	·6475
11	·98	·9653	·9740	61	·86	·5650	·6320
12	·98	·9634	·9726	62	·86	·5492	·6162
13	·98	·9614	·9710	63	·85	·5332	·6000
14	·98	·9592	·9693	64	·85	·5171	·5830
15	·98	·9569	·9676	65	·85	·5007	·5650
16	·98	·9546	·9657	66	·85	·4841	·5462
17	·98	·9522	·9638	67	·84	·4673	·5266
18	·98	·9497	·9617	68	·84	·4506	·5070
19	·98	·9471	·9596	69	·84	·4339	·4873
20	·97	·9444	·9572	70	·83	·4173	·4679
21	·97	·9416	·9547	71	·83	·4009	·4488
22	·97	·9387	·9521	72	·82	·3846	·4301
23	·97	·9356	·9493	73	·82	·3683	·4114
24	·97	·9323	·9464	74	·81	·3519	·3928
25	·97	·9288	·9432	75	·80	·3352	·3743
26	·97	·9250	·9399	76	·79	·3181	·3559
27	·97	·9209	·9364	77	·78	·3009	·3377
28	·97	·9165	·9328	78	·76	·2838	·3198
29	·97	·9119	·9289	79	·74	·2671	·3023
30	·96	·9068	·9248	80	·72	·2509	·2855
31	·96	·9015	·9205	81	·71	·2353	·2693

Years of age	Joint factor	Value of an interest in a capital of €1 for a male life aged as in column 1	Value of an interest in a capital of €1 for a female life aged as in column 1
32	·96	·8958	·9159
33	·96	·8899	·9111
34	·96	·8836	·9059
35	·96	·8770	·9005
36	·96	·8699	·8947
37	·96	·8626	·8886
38	·95	·8549	·8821
39	·95	·8469	·8753
40	·95	·8384	·8683
41	·95	·8296	·8610
42	·95	·8204	·8534
43	·95	·8107	·8454
44	·94	·8005	·8370
45	·94	·7897	·8283
46	·94	·7783	·8192
47	·94	·7663	·8096
48	·93	·7541	·7997
49	·93	·7415	·7896

Years of age	Joint factor	Value of an interest in a capital of €1 for a male life aged as in column 1	Value of an interest in a capital of €1 for a female life aged as in column 1
82	·70	·2203	·2538
83	·69	·2057	·2387
84	·68	·1916	·2242
85	·67	·1783	·2104
86	·66	·1657	·1973
87	·65	·1537	·1849
88	·64	·1423	·1730
89	·62	·1315	·1616
90	·60	·1212	·1509
91	·58	·1116	·1407
92	·56	·1025	·1310
93	·54	·0939	·1218
94	·52	·0858	·1132
95	·50	·0781	·1050
96	·49	·0710	·0972
97	·48	·0642	·0898
98	·47	·0578	·0828
99	·45	·0517	·0762
100 or over	·43	·0458	·0698

Interest for a period certain

This table is used to determine a figure on the value of an interest in property for a period certain.

Number of years	Value	Number of years	Value
1	·0654	26	·8263
2	·1265	27	·8375
3	·1836	28	·8480
4	·2370	29	·8578
5	·2869	30	·8669
6	·3335	31	·8754
7	·3770	32	·8834
8	·4177	33	·8908
9	·4557	34	·8978
10	·4913	35	·9043
11	·5245	36	·9100
12	·5555	37	·9165
13	·5845	38	·9230
14	·6116	39	·9295
15	·6369	40	·9360
16	·6605	41	·9425
17	·6826	42	·9490
18	·7032	43	·9555
19	·7225	44	·9620
20	·7405	45	·9685
21	·7574	46	·9750
22	·7731	47	·9815
23	·7878	48	·9880
24	·8015	49	·9945
25	·8144	50 and over	1·0000

Stamp duty

Non-residential property (regardless of value)	6%
Residential property: Owner occupiers and investors	
First €1,000,000	1%
Excess over €1,000,000	2%

NB: Where applicable value added tax (VAT) should be excluded from the chargeable consideration.

Stocks and marketable securities	
Where the aggregate consideration is no more than €1,000	0%
Where the aggregate consideration exceeds €1,000	1%

Revenue audits

Schedule of tax geared penalties

		Net penalty after reduction where there is:		
Category of tax default	**Penalty as a % of tax underpaid**	**Cooperation only**	**Cooperation AND a prompted qualifying disclosure**	**Cooperation AND an unprompted qualifying disclosure**
Deliberate behaviour	100%	75%	50%	10%
Careless behaviour with significant consequences	40%	30%	20%	5%
Other careless behaviour	20%	15%	10%	3%

Note: The mitigation (reduction) of penalties in the above table is available to taxpayers on their first default. In the case of a second or third default, if a taxpayer deliberately or carelessly makes incorrect returns within a five-year period of the first default they may not avail of full mitigation.

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Question 1 begins on page 10.

Section A – BOTH questions are compulsory and MUST be attempted

1 You should assume that today's date is 5 November 2019.

You are a tax senior and recently attended a client meeting with Mark Smyth, along with your tax manager, and you took the following notes:

– Mark Smyth is the managing director and sole shareholder in Red Ltd.

– Red Ltd has a retail shop in Cork, Ireland which sells electronic equipment.

– The company prepares its annual accounts to 31 December and has recently diversified into insurance broking services.

– The value added tax (VAT) rate applicable to the electronic equipment is 23%, but the insurance broking is an exempt activity.

– The projected annual turnover (excluding VAT) over the next two years of trading is expected to be approximately €1,000,000, of which €850,000 will relate to sales of electronic equipment and €150,000 will relate to insurance broking.

Mark wants our advice in relation to the following matters:

(i) Red Ltd bought a new building in Cork for €600,000 (plus 13·5% VAT) on 30 November 2018. Initially, the company recovered all of the VAT on acquisition as it had intended to use the entire building for its retail trade.

As the building now includes an insurance broking department, Mark understands that the new recovery rate is likely to be 85%. Mark needs to know the VAT implications of this change on the assumption that the 85% recovery rate is correct.

(ii) In August 2019, Red Ltd bought ten tablet computers for use by its electronic equipment sales staff at a total cost of €4,920 (VAT inclusive). The company reclaimed the VAT in full.

In October 2019, two of the tablet computers were transferred to the insurance broking department for use there, and a third tablet computer was given to Louise Smyth (Mark's wife) for her private use. Louise does not work in the business.

Mark wants us to confirm the appropriate tax treatment of these transfers.

(iii) The company is currently experiencing delays of up to three months in receiving payment from certain large customers. Consequently, VAT on these sales is payable before Red Ltd receives the money from the customers.

Apart from sending out more reminders to customers, Mark is curious to know if the company can take any other action(s) to improve this situation.

(iv) Red Ltd plans to expand its business into France (EU). To achieve this, Mark believes it will be necessary to rent and equip shop premises in France and to employ five new local staff. Financial projections indicate that the French business will incur losses for the first two years, and is then expected to make substantial profits from the third year onwards.

Mark is unsure as to whether the French business should be operated as a branch, or a subsidiary, of Red Ltd.

(v) Red Ltd has decided to terminate the employment of its Irish office manager, Bill Williams, on 30 November 2019. Mark requires advice on the amount of tax which should be deducted from the severance payments to Bill.

Bill is single and commenced employment with Red Ltd on 1 April 1993. Bill's severance package will comprise:

– an *ex-gratia* payment of €60,000;
– pay in lieu of notice of €4,000;
– a company car with a market value of €20,000; and
– statutory redundancy of €41,000.

In addition, Bill will be entitled to a tax-free pension lump sum which has a present value of €10,500.

Mark has confirmed that the pay in lieu of notice was not provided for in Bill's contract of employment.

Details of Bill's historic salary and benefits in kind (BIK) are as follows:

Year ended	Salary	BIK
	€	€
Year ended 31 December 2016	34,000	5,000
Year ended 31 December 2017	35,000	5,000
Year ended 31 December 2018	37,000	6,000
11 months ended 30 November 2019 (expected)	40,000	5,000

(vi) Mark bought 50 acres of agricultural land in January 2012 for €350,000. In March 2015, he spent €130,000 on agricultural works on the 50 acres, which included fencing, a drainage system, an access roadway and pipes under the land to provide drinking water to cattle.

Mark, who has never been registered for VAT, has continued to farm the land thereafter but plans to sell 20 acres of the land in December 2019 for €200,000. The value of the remaining 30 acres of land on the day of sale is expected to be €230,000.

Mark requires our help in calculating any chargeable gain arising on the sale, and in understanding the VAT implications of the sale.

Required:

Write a memorandum to your tax manager in which you:

(i) Explain the consequences to Red Ltd of the expected change in the value added tax (VAT) recovery rate to 85% in respect of the building in Cork, Ireland. (4 marks)

(ii) Explain the VARIOUS tax consequences of the transfer of the three tablet computers for both Red Ltd and Louise Smyth. (6 marks)

(iii) Suggest what action(s) could be taken to improve Red Ltd's cash flow position in relation to VAT payable by some large customers. (2 marks)

(iv) Compare the taxation implications of the TWO suggested alternative trading structures (branch and subsidiary) in respect of the French office, and recommend the most appropriate structure for Red Ltd to use.

Note: You should assume that the OECD model tax treaty provisions apply to France and that the rate of corporation tax in France is 28%. (10 marks)

(v) Advise on and calculate which taxes should be deducted by Red Ltd from Bill's severance package in November 2019. (5 marks)

(vi) Explain whether VAT will apply to the proposed sale of agricultural land by Mark Smyth, and calculate the capital gains tax (CGT) payable (if any) on the sale. (4 marks)

Professional marks will be awarded for the presentation of the memorandum, the extent to which the calculations are approached in a logical manner and the effectiveness with which the information is communicated. (4 marks)

(35 marks)

2 You should assume that today's date is 5 September 2019.

Your client, Anne Lynch (single, aged 45), is a sole trader, whose business 'Ocean Salt' operates as a wholesale supplier to the catering trade in Dublin, Ireland. The business was set up on 1 November 2017 by Anne, who works full time in the business. The business has been profitable to date.

Anne has sought advice in relation to the following two issues:

(i) Proposal to incorporate the business

Anne is so concerned about her unlimited liability status that she plans to incorporate the business as soon as possible by forming a company called 'Ocean Salt Ltd' and transferring the relevant assets and liabilities into that company. Her chosen date for the transfer is at start of business on 1 November 2019 (the day after her next accounting year end). She has informed you that under no circumstances will she postpone the incorporation of the business.

The business' projected net assets as at 31 October 2019 are as follows:

	€	€
Non-current assets		
Property	300,000	
Equipment	80,000	380,000
Current assets		
Inventory	46,000	
Trade receivables	50,000	
Cash at bank	49,000	
	145,000	
Current liabilities		
Trade payables	(74,000)	71,000
		451,000

Notes:

1. The business property was bought new in October 2017 and cost €300,000 (net of VAT). It has a current market value of €420,000.
2. The equipment originally cost €190,000 and has a current market value of €85,000. Its tax written down value was €70,000 at 31 October 2018.
3. The value of goodwill has been agreed at €200,000.
4. The market value of inventory and receivables is the same as the book value.

It is proposed that Anne will transfer all the assets (excluding cash) to the company for the following consideration:

– the company will owe Anne €60,000 in the form of a director's loan,
– the company will take over the liabilities of the business, and
– the balance of the consideration will be satisfied by the issue of shares.

However, Anne is having second thoughts about transferring the property to the company and wants advice on this issue.

(ii) Inheritance

Anne's father, David, a widower, died in January 2010 and left his house to Anne subject to a right of residence granted to her sister, Marion, who was aged 55 at the time.

In May 2019, Marion died at the age of 64. Valuations of the house were performed by an independent auctioneer and are as follows:

	January 2010	May 2019
	€	€
Value of the house	1,000,000	1,500,000
Gross annual value of the house	40,000	60,000
Gross annual value of the right of residence	18,000	25,000

Required:

(a) Advise Anne Lynch on the various tax consequences for both herself and the new company of incorporating the business 'Ocean Salt' on 1 November 2019, and the tax effect if Anne were not to transfer the property to the company.

You should prepare a summary of the taxes payable under both options (transferring the property or not transferring the property) and recommend (stating your reasons) which course of action Anne should choose.

Notes:

1. Your advice should refer to capital gains and to all other relevant taxes.
2. You should support the advice for this part with relevant calculations but may ignore the annual exemption for capital gains tax. (20 marks)

(b) Calculate the taxable value in January 2010 and May 2019 of the inheritance(s) of their father's house for both Marion and Anne.

Note: You are NOT required to calculate the capital acquisitions tax (CAT) payable. (5 marks)

(25 marks)

Section B – BOTH questions are compulsory and MUST be attempted

3 Tablet Ltd is a pharmaceutical company based in Limerick, Ireland. The finance director requires advice in respect of the following issues:

(1) Specified intangible assets

Tablet Ltd acquired patents relating to certain pharmaceutical products in January 2018 at a cost of €4,000,000. The acquisition was partly financed by a bank loan, on which interest of €130,000 was paid in the year ended 31 December 2018. In the statement of profit or loss, the company's accountant has amortised these patents over a ten-year period on a straight-line basis, with a full year's amortisation in the year of acquisition.

Tablet Ltd's Case I income for the year ended 31 December 2018 is €610,000, comprising:

– €450,000 from the trade of managing patents (after adding back the amortisation but before deduction of any capital allowances or related interest relief), and

– €160,000 from other trading activities.

(2) Employee shares

The company's senior management has identified nine key members of staff whom they wish to retain and reward. They do not want to reward all the company's employees.

The nine key members of staff all earn over €75,000 per annum and the senior management proposal is to award shares valued at €15,000 to each of them.

Required:

(a) (i) Explain the tax reliefs available to Tablet Ltd in relation to the patents. Include a description of the expenditure which may be relieved, the restrictions on the relief, and any clawback provisions.
(7 marks)

(ii) Calculate the taxable income of Tablet Ltd for the year ended 31 December 2018 on the basis that the company wishes to write off the cost of the patents for tax purposes as quickly as possible. Clearly identify the intangible asset reliefs available and any unutilised amounts. (4 marks)

(b) (i) Explain the tax implications of the proposed share awards for both Tablet Ltd (as employer) and the nine key employees, including the tax implications of the subsequent disposal of the shares at a gain by the employees. (5 marks)

(ii) Explain how the tax arising on the proposed share awards may be reduced and the conditions which must be adhered to by both Tablet Ltd (as employer) and the employees in order to achieve this reduction.
(4 marks)

(20 marks)

4 (a) Aladdin Ltd is an Irish resident company, whose shares are held as follows:

Major Ltd	40%
Change Ltd	20%
Space Ltd	16%
Diamond Ltd	24%

Change Ltd is resident in Canada (non-EU) but all the remaining shareholder companies are resident in Ireland.

In the year to 31 December 2018, the five companies had the following results:

	Case I profit/(loss) €	Case V profit €
Aladdin Ltd	(500,000)	40,000
Major Ltd	100,000	
Change Ltd	150,000	
Space Ltd	(32,000)	
Diamond Ltd	2,000,000	

Required:

(i) Identify and explain the loss relief available to Aladdin Ltd and its shareholders for the year ended 31 December 2018. (4 marks)

(ii) Calculate the corporation tax payable for 2018 by Aladdin Ltd, Major Ltd, Space Ltd and Diamond Ltd, making maximum use of any available reliefs. Give explanations of the basis for your calculations and the treatment of any unused losses. (7 marks)

(b) James Delaney died intestate (without making a will) on 5 August 2019, and was survived by his wife, Sharon (aged 67), and their daughter, Julie. The family home, valued at €500,000, was in joint names and Sharon inherited her husband's share directly as the joint tenant of the property.

The residue of James' estate was valued at €150,000 and, under the rules of intestacy, Sharon is entitled to a two-thirds share and Julie is entitled to the remaining one-third share.

Sharon had received an inheritance of €18,000 from her brother, Jack, in 2013 and received an inheritance of €8,000 from her cousin, Zelda, in 2014. Sharon's income is insufficient for her needs.

Julie has not received any prior gifts or inheritances. Unlike her mother, she has sufficient income for her needs and she understands that the bank interest for cash on deposit is only 1% per annum. Accordingly, Julie has agreed in principle to give her share of the residue of her father's estate to her mother either directly as a gift or in the form of a loan.

Required:

(i) Calculate the capital acquisitions tax (CAT) payable (if any) by Sharon in relation to the following alternatives:

- **A gift of €50,000 from Julie; or**
- **An interest free loan of €50,000 from Julie to Sharon, with no specified repayment date.**

(4 marks)

(ii) Recommend an alternative tax efficient proposal. (2 marks)

(c) Certain nephews/nieces will be treated as 'favoured' nephews/nieces for capital acquisitions tax (CAT) and accordingly will be treated, in certain circumstances, as sons/daughters, qualifying for the Class 1 tax free threshold.

Required:

List the requirements for this CAT relief to apply. (3 marks)

(20 marks)

End of Question Paper

Answers

1 Red Ltd

Memorandum

To: A manager
From: A senior
Re: Mark Smyth and Red Ltd, various taxation issues
Date: 7 November 2019

Further to our meeting with Mark Smyth on 5 November 2019, our advice in relation to the issues raised is as follows:

(i) Effect of the change in the value added tax recovery rate on the building in Cork

At the end of the first 12 months following acquisition (i.e. 30 November 2019), the recovery rate is reviewed and if there is a change of rate, the initial amount recovered is adjusted by way of an additional claim or refund.

In this case, the initial amount recovered was €81,000 (based on a recovery rate of 100%). The value added tax (VAT) refund based on the new recovery rate of 85% would be €68,850. Accordingly, Red Ltd will be required to repay €12,150 of the initial VAT claim to the Revenue in its VAT return for January/February 2020.

The first year recovery rate (85%) will be used as a benchmark for the remaining life of the property (20 intervals) and the benchmark revised deductible amount will be €3,443 (€68,850/20) per annum.

(ii) Tax consequences of the tablet computer transfers

Each tablet computer costs €492 (including VAT) so VAT amounts to €92 per tablet computer.

Transfer of two tablet computers to the insurance broking department:

- VAT: As a transfer from taxable use to exempt use, this is a self-supply. VAT of €184 (€92 x 2) should be included as output VAT in Red Ltd's next VAT return.
- Corporation tax: As the input VAT on the two tablet computers is irrecoverable, capital allowances at 12·5% may be claimed by Red Ltd on the VAT inclusive cost of the two tablet computers of €984 (€492 x 2) rather than the VAT exclusive cost of €800 (€984 – €184).

Gift of tablet computer to Louise Smyth for private usage:

- VAT: This is also a transfer to non-business use, which is a deemed supply. VAT is chargeable on the cost of the goods, and €92 should be included as output VAT in Red Ltd's next VAT return.
- Corporation tax: As Red Ltd is a close company (sole shareholder is Mark), and Louise is the wife (an associate) of a participator, the gift of the tablet computer is treated as a distribution of €492 from Red Ltd to Louise Smyth. Red Ltd will not be entitled to claim capital allowances on this tablet computer.
- Dividend withholding tax (DWT) of €98 (20% x €492) will apply to the distribution. This is payable by the 14th of the month following the distribution. The company is entitled to seek recovery of this DWT from Louise. If Louise does not repay the DWT to Red Ltd, the DWT suffered may be treated as a further distribution.
- Income tax (Louise Smyth): Louise will be taxed under Schedule F on the distribution at her marginal tax rate. She will receive a deduction for the DWT deducted.

(iii) Cash flow issues relating to VAT

Red Ltd has a turnover from its taxable activity of less than €2 million, and is therefore entitled to account for VAT on a cash receipts basis. However, the company is required to apply to the Revenue for authorisation to do this.

Tutorial note: *A business is also entitled to register for VAT on a cash receipts basis if more than 90% of its turnover derives from supplies to persons who are not registered for VAT (B2C).*

The liability to pay VAT will then arise by reference to the VAT period in which the cash is received and not by reference to the issuing of an invoice.

After the changeover, VAT is not accounted for in respect of cash received for goods supplied while accounting on the invoice basis.

Tutorial note: *If turnover from the taxable activity is expected to increase above €2 million in any 12-month period, the company would be obliged to switch back to the invoice basis.*

If Red Ltd does not elect for VAT on a cash receipts basis, the following suggestions may improve cash flow:

- Postpone issuing invoices at the end of a two-month period until the start of the following month (subject to the legislative requirement of issuing an invoice no later than the 15th day of the month following the supply of goods or services).

- Apply for annual VAT registration with monthly direct debits, to avoid large variations in VAT payments.

Tutorial note: *In relation to the direct debit scheme, it is important to ensure that the direct debits are sufficient. If the balancing payment (at the end of the year) is more than 20% of the tax payable for the year, then an interest charge of approximately 5·88% is applied to the balancing payment.*

(iv) Trading structure for French office

(1) Branch

The taxation implications of operating the French shop as a branch are:

- The French branch losses anticipated in the first two years will be automatically utilised against the Irish profits of Red Ltd, as the worldwide business is considered to be a 'single entity' for tax purposes.
- The branch profits will be liable to Irish corporation tax at 12·5%, assuming the trade is managed and controlled from Ireland.
- Any French branch profits are also likely to be liable to French tax at 28%, as the branch will be considered to be a permanent establishment. However, a credit will be available in Ireland for any foreign tax paid, but limited to the Irish tax charged on the same income, i.e. at the lower of the French or the Irish corporation tax rate. Therefore, it is likely that there will be no additional Irish corporation tax to pay on the profits of the French branch.
- Where French tax is unrelieved in any year, it can be carried forward indefinitely and credited against the Irish corporation tax payable on the French branch profits in future years.

(2) Subsidiary

The taxation implications of incorporating a French subsidiary of Red Ltd are:

- As the losses arise in a company resident in the EU, the losses arising in the French subsidiary can be set against profits in Red Ltd but only:
  - where the subsidiary is 75% owned by Red Ltd (which is likely to be the case), and
  - the losses cannot be relieved under any other provisions elsewhere first (i.e. losses are not available for offset in France either by a current year claim, other group relief claim, a preceding years claim or the carry forward of the losses).

    This is a very restricted entitlement and in practice loss relief against Red Ltd's profits is unlikely to be available.
- The profits of the subsidiary will be liable to corporation tax in France at 28% and there will be no exposure for the French profits to Irish corporation tax.
- Any dividends paid to Red Ltd will be liable to corporation tax under Schedule D Case III.
- Credit relief will be available for any foreign withholding tax and underlying foreign tax paid on the profits out of which the dividend was paid.
- As with a branch, where any French tax is unrelieved in any year, it can be carried forward indefinitely and credited against the Irish corporation tax payable in future years.
- Dividends received from the French subsidiary will not count as investment income in Red Ltd for close company surcharge purposes.

Recommendation

As the French business is likely to be loss making for the next two accounting periods, a branch structure should be implemented, in order to facilitate the use of these French losses against Red Ltd's Irish profits.

Even once the French business becomes profitable, there is unlikely to be any additional Irish taxation on the profits from the French business due to availability of a double tax relief credit for the French tax suffered (at a higher rate) on the same profits.

However, the application of a subsidiary structure may facilitate the use of the holding company exemption on a future disposal which may make structuring the operations through a subsidiary a more attractive option once the French office is profitable.

(v) Bill William's severance package

Statutory redundancy and the pension lump sum are exempt from income tax.

As the pay in lieu of notice of €4,000 was not provided for in Bill's contract of employment, for the purposes of tax reliefs available, it is included with the *ex-gratia* payment (€60,000) and the company car (€20,000) and treated as a deemed lump sum payment.

This deemed lump sum payment of €84,000 is partially subject to income tax. The tax-free element of the package is calculated in Appendix, Schedule 1.

The standard capital superannuation benefit (SCSB) calculation gives the highest figure and therefore €65,333 is tax free. The taxable portion of the lump sum is therefore €18,667 (€84,000 – €65,333).

Income tax of €7,467 (€18,667 x 40%), calculated at Bill's marginal rate of 40%, together with USC of €887 (€18,667 x 4·75%), will be deducted at source by Red Ltd. There will be no pay-related social insurance (PRSI) liability.

(vi) Tax implications of the sale of land

VAT

The works carried out on the land were of an agricultural nature and did not materially alter the land (since it was a farm before and is still a farm after). Accordingly, the sale will be exempt from VAT as the land was not developed.

Tutorial note: *The 25% test does not apply to land.*

Capital gains tax (CGT)

The CGT computation is included in Appendix, Schedule 2 and indicates that no CGT will be payable.

Computational appendix

Schedule 1: Calculation of tax-exempt portion of severance package

Basic exemption

	€
(€10,160 + €765 x 26)	30,050

Increased basic exemption

	€
Maximum increase allowable	10,000
Less: Pension lump sum	(10,500)
Increase possible	Nil

Standard capital superannuation benefit (SCSB)

Average annual emoluments for three years ending on 30 November 2019

Period	**Emoluments**	
	€	
December 2016	3,250	((€34,000 + €5,000) x 1/12)
Year ended 31 December 2017	40,000	(€35,000 + €5,000)
Year ended 31 December 2018	43,000	(€37,000 + €6,000)
11 months ended 30 November 2019	45,000	(€40,000 + €5,000)
Total emoluments for three years	131,250	
Average annual emoluments	43,750	

SCSB

Average annual emoluments x complete years of service/15 – pension lump sum

€43,750 x 26/15 – €10,500 = €65,333

Schedule 2: CGT computation

	€
Proceeds	200,000
Less: Original cost (note 1)	(162,791)
Less: Enhancement expenditure (note 2)	(60,465)
Loss	(23,256)
CGT	Nil

Notes:

1 **Cost of part disposal**
Original cost
(€350,000 x €200/(€200 + €230)) = €162,791

2 **Enhancement expenditure**
(€130,000 x €200/(€200 + €230)) = €60,465

2 Anne Lynch

(a) Proposal to incorporate the business

The transfer of assets from a sole trade to a company constitutes a disposal for CGT purposes and if gains arise, they will be taxable. However, there is a relief (incorporation relief) which defers the tax payable to the extent that the consideration is taken in the form of shares in the company.

The following conditions must be complied with before incorporation relief applies:

– there must be a transfer of a business by a person to a company;
– the transfer must occur for *bona fide* commercial reasons;
– the business must be transferred as a going concern;
– the whole of the assets of the business or all of those assets other than cash must be transferred; and
– the transferor must receive shares in the new company in return for the business.

Based on the information received, it is possible for Anne to avail of incorporation relief, provided all of the assets of the business (including the property) are transferred to the company.

The following analysis provides a comparison of the tax costs of transferring the relevant assets under two scenarios:

Option 1: Taxes payable on the transfer of all assets (excluding cash) (incorporation relief applies).

Option 2: Taxes payable on the transfer of all assets excluding the property and cash (incorporation relief does not apply).

Entrepreneur relief
Entrepreneur relief, which could reduce the rate of CGT to 10%, is not available on this incorporation, because Anne has not held the assets for the requisite three-year period.

Tutorial note: *Entrepreneur relief may be restricted where an individual transfers a business to a company pursuant to s.600 TCA (incorporation relief). Relief will not be available in respect of the proportion of the gain which relates to non-share consideration received out of the assets of the company in respect of the disposal. However, the restriction does not apply in relation to* bona fide *commercial disposals which do not form part of a tax avoidance arrangement.*

Option 1: Taxes payable if incorporation relief applies

1. **Income tax**

   Cessation of trade:
   The sole trade will cease on 31 October 2019. The implications of this are:

   – The penultimate tax year 2018 will be reviewed, and if actual profits exceed assessed profits, the assessed profit will be revised upwards.

   – However, the business qualifies as a 'short-lived business' because it commenced and ceased within three tax years. Therefore, if assessed profits exceed actual profits for the lifetime of the business, a claim may be made to have the profits of year 2 (2018) assessed on an actual basis.

   Tutorial note: *The effect of short-lived business relief is that the business cannot be taxed on an amount greater than actual profits over its lifetime, as both the commencement and cessation years are already assessed on an actual basis.*

   Capital allowances
   The equipment has a current market value of €85,000 with a tax written down value of €70,000. The transfer would potentially trigger a balancing charge of €15,000. However, it is possible to jointly elect to transfer the assets into the company at their tax written down value to avoid this charge.

2. **Capital gains tax**

   The CGT calculation is as follows:

   First, the value of the assets immediately after the transfer is calculated and the proportion of the gain to be deferred is given by the fraction (value of shares/value of assets).

	€	€
Property		420,000
Goodwill		200,000
Equipment		85,000
Inventory		46,000
Trade receivables		50,000
Value of assets transferred		801,000
Trade payables	74,000	
Director's loan	60,000	(134,000)
Net assets (value of shares)		667,000
Value of shares/Value of assets		667/801

   Second, the capital gains tax payable is calculated in the normal way and the percentage deferral is applied to the gain, leaving the remainder taxable.

Chargeable gains

	€
Property (€420,000 – €300,000)	120,000
Goodwill (€200,000 – €0)	200,000
	320,000
Deferred gain (€320,000 x 667/801)	(266,467)
Taxable gains	53,533
CGT at 33%	17,666

CGT of €17,666 is payable on the transfer. The relief provides for a deferral of gains amounting to €266,467 until such time as the shares in the company are sold.

3. **Stamp duty**

Stamp duty at 6% will apply to the transfer of the property and goodwill.

Stamp duty at 6% will also apply on the transfer of the equipment and inventory, because it is being transferred in return for shares and therefore cannot pass by delivery. The reason for this is that the contract for the transfer of assets for shares will include these assets and this document is classified as an instrument for the purposes of stamp duty.

Stamp duty at a rate of 6% will apply to the receivables being transferred and they must be transferred to the company for the relief on incorporation to apply.

On this basis, the total stamp duty liability arising under option 1 amounts to €48,060 as per the following calculation:

Stamp duty liability

	€	€
Property	420,000	
Rate	6%	25,200
Goodwill	200,000	
Rate	6%	12,000
Equipment	85,000	
Rate	6%	5,100
Inventory	46,000	
Rate	6%	2,760
Trade receivables	50,000	
Rate	6%	3,000
Total stamp duty payable		48,060

4. **Value added tax (VAT)**

Provided both parties (transferor and transferee) are registered for VAT, the transfer of business (TOB) provisions apply and no VAT is chargeable. It is therefore essential that Ocean Salt Ltd is registered for VAT before the transfer takes place.

The property will be 'new' on the date of transfer as it is within five years of acquisition and the VAT of €56,700 (€420,000 x 13·5%) which would have applied in the absence of the TOB provisions will be deemed to apply to the transfer.

A new capital goods scheme (CGS) adjustment period of 20 years will commence from 1 November 2019.

Anne will have no CGS adjustment as she will be treated as having made a taxable supply.

Option 2: Taxes payable if incorporation relief does NOT apply

In the event that the property is not transferred to the company, incorporation relief would not apply and there would be no requirement to transfer all of the other business assets (excluding cash).

1. **Income tax**

The same issues arise as with option 1 in relation to the cessation and the transfer of equipment at tax written down value.

2. **Capital gains tax**

The only CGT arising under option 2 would be on the transfer of the goodwill which is valued at €200,000. The amount payable would be €66,000 (33% x €200,000).

3. **Stamp duty**

The only stamp duty liability will be on the goodwill and this will amount to €12,000 (6% x €200,000).

Stamp duty savings will arise from:

– Retaining the property in personal ownership and renting it to the company;

– Transferring equipment and inventory by delivery in consideration for a director's loan to the company;

– Not transferring receivables, and instead collecting the debts and using the proceeds to pay off the suppliers (trade payables).

4. **Value added tax (VAT)**

Assuming that the company is VAT registered, the VAT consequences are as in option 1, with the exception of the property.

If the property is retained and Anne chooses to rent it to the company (as suggested above to avoid stamp duty), Anne should opt to tax the letting of the premises for VAT purposes, to avoid a CGS adjustment.

Summary

	CGT	Stamp duty	Total
	€	€	€
Option 1: claiming incorporation relief	17,666	48,060	65,726
Option 2: not claiming incorporation relief	66,000	12,000	78,000
Difference			(12,274)

Recommendation
The total tax payable is higher by €12,274 under option 2.

However, option 2 is often chosen in practice because it is generally preferable to retain assets (such as property) which have the potential to appreciate in private hands rather than transferring them to a company, as this avoids the double charge to CGT on a subsequent disposal of the asset by the company.

In addition to the above, it should be noted that the CGT relieved under incorporation relief is only a deferral (i.e. the base cost of the shares in Ocean Salt Ltd will be reduced by the deferred gain in the event of a future disposal), whereas the stamp duty costs are a permanent cost.

Therefore the long-term tax cost of claiming incorporation relief may be substantially more than the cost of not claiming it.

Tutorial note: *It is a condition of entrepreneur relief (ER) that periods of ownership of assets before and after incorporation of a business may not be aggregated for the purpose of the three-year ownership condition. In this case, it may be possible for Anne to qualify for ER on a disposal of her shares in Ocean Salt Ltd which would take place three or more years after the incorporation of the company. This would apply to the subsequent sale of the company shares under both option 1 and option 2. However, entrepreneur relief would not apply to any gains arising on the sale of the property if it was personally held and rented to the company (see option 2).*

(b) Marion's inheritance in January 2010
The capitalised value of the right of residence was €450,000 (€1,000,000 x €18,000/€40,000).

The taxable value was €324,270, being the capitalised value multiplied by the relevant factor for a female aged 55 (€450,000 x 0·7206).

Anne's inheritance in January 2010
Anne inherited the remainder which had a taxable value of €550,000 (€1,000,000 – €450,000).

Anne's inheritance in May 2019
The capitalised value of the right of residence using May 2019 valuations was €625,000 (€1,500,000 x €25,000/€60,000). This is the taxable value of Anne's inheritance in May 2019.

Tutorial note: *A right of residence is a right to live in a property and does not give the holder ownership of the property. For capital acquisitions tax purposes, the value of a non-exclusive right of residence is a lesser value than a life interest. In the absence of an expert valuation of the right of residence, the Revenue accept a valuation of 10% of the value of the property.*

3 Tablet Ltd

(a) Tax relief in relation to the patents

(i) Capital allowances
Companies carrying on relevant trades which incur costs on certain specified intangible assets are entitled to claim capital allowances on that expenditure.

A relevant trade is one which is involved in 'managing, developing or exploiting specified intangible assets'.

The specified intangible assets are intellectual property assets, examples of which are patents, registered designs, inventions, trademarks, brands, domain names and copyrights.

Two options are available in relation to calculating the capital allowances:

– writing off in line with the depreciation or amortisation for accounting purposes; or
– writing off over a 15-year period, being 7% for years 1 to 14 and 2% for year 15.

The second option will always apply where the intangible asset is considered to have an infinite life.

A company will generally choose the option which offers the quickest tax relief. When the second option is chosen, the company is required to make a claim in its tax return.

Interest

Interest on borrowings incurred in relation to the acquisition of specified intangible assets is also tax deductible.

Restrictions

The following restrictions apply to the capital allowances and interest deductible in any year:

(1) The allowances must be claimed against income from the relevant trade. This income must be separately identified.

(2) The relief for capital allowances and certain interest costs is restricted to 80% of the gross income (i.e. income excluding such allowances and interest) from the deemed separate activity. The interest deduction must be claimed in priority to the capital allowances. Unused capital allowances and interest may be carried forward to future periods.

Clawback

Where a specified intangible asset is disposed of within five years of its acquisition, there will be a clawback of the capital allowances granted. In the case of a disposal after more than five years, there will be no clawback, unless the asset is sold to a connected company which then claims capital allowances on the asset.

(ii) Taxable income for the year ended 31 December 2018

Intangible asset capital allowances

Option 1: Accounting treatment: Annual amortisation of patents €400,000 (€4,000,000/10).

Option 2: Writing off over 15 years at 7% per annum: €280,000

Option 1 will be claimed because it is the higher.

Taxable income

	€
Income from the relevant trade (excluding allowances and interest)	450,000
Less: Intangible assets relief (see note below)	(360,000)
Taxable income from relevant trade	90,000
Add: Non-relevant trade income	160,000
Total taxable income	250,000

Note: The maximum relief available is €360,000 (80% x €450,000). The €130,000 interest is allowed in full and the capital allowances are restricted to €230,000. The unutilised capital allowances of €170,000 (€400,000 – €230,000) are carried forward to be offset against future years' relevant trading income.

(b) Employee shares

(i) Tax implications of the proposed share awards

Employees

The market value of the free shares awarded will be treated as notional pay at the time the shares are awarded.

This notional pay is subject to:

– income tax at the employee's marginal rate;
– universal social charge (USC); and
– employee PRSI.

Therefore, the effective tax burden for higher rate taxpayers (such as the nine employees) will be 52% (40% + 8% + 4%).

Capital gains tax (CGT) will arise on a subsequent sale of the shares by the employees if the shares are sold at a price higher than their market value on the day they were awarded to the employee (the CGT base cost).

Tablet Ltd (employer)

Revenue approval is not required for share awards and the shares do not need to be offered to all employees.

Tablet Ltd must account for the income tax, USC and employees' PRSI on the share award through the PAYE system in the same way as it does for other benefits in kind (BIK) and remit these to the Revenue in the month following the share award.

Share awards are not subject to employer's PRSI.

Tablet Ltd can collect the taxes due from the employee in future payroll periods provided the liability is paid in full by 31 March of the following tax year. Otherwise another BIK charge will arise on the outstanding balance. Alternatively, Tablet Ltd may withhold or sell sufficient shares to fund the taxes due on the award of the shares, before transferring the balance of the shares to the employees.

(ii) **Mitigation of the tax arising**

The Revenue will allow a reduction in the taxable value of the free of charge shares, if the shares are subject to a restriction on disposal for a fixed period following the award (the 'clog' period). The longer the 'clog' period, the greater the reduction in taxable value as follows:

Period of restriction	Percentage reduction
One year	10%
Two years	20%
Three years	30%
Four years	40%
Five years	50%
Over five years	60%

The CGT base cost of the shares for the purposes of any subsequent sale by the employee will be reduced by the same percentage reduction as the taxable value of the award.

Tutorial note: *The effective tax saving will only be 19% (52% – 33%), with the remaining 33% tax saving only being deferred until the sale of the shares (provided at least market value is realised).*

During the 'clog' period, the shares must not be sold, assigned, charged, transferred or pledged as security for loans by the employee, and a written contract must be entered into to this effect.

The employer will place the shares in a trust for the benefit of the relevant employees.

The employer must report to the Revenue (on a standard electronic form RSS1) before 31 March in the tax year following the event, where:

- restricted shares have been awarded to employees; or
- restricted shares have been forfeited; or
- restricted shares have been disposed of prior to the end of the 'clog' period.

Tutorial note: *A recommendation to set up a Revenue approved profit sharing scheme (APSS) would not be appropriate because an APSS must be open on similar terms to all employees who have been employed for a minimum period set by the employer, not exceeding three years.*

4 (a) Aladdin Ltd and its shareholders – Corporation tax (CT) for 2018

(i) The applicable relief is consortium relief.

A loss consortium exists if at least 75% of the share capital of a company (the 'consortium company') is owned by five or fewer EU or EEA resident companies, and none of the companies owns more than 75% of the share capital of the consortium company. In this case, Aladdin Ltd is a qualifying consortium company because 80% of the company is owned by three EU resident companies. All the shareholder companies qualify for the relief except for Change Ltd. Change Ltd does not qualify because it is resident in neither the EU nor the EEA.

(ii) **Tax computation**

Aladdin Ltd
Aladdin Ltd must first use its Case I loss to eliminate any tax arising on its Case V income. The CT payable is as follows:

	€
Case I profit	0
Case V profit	40,000
CT at 25%	10,000
Less: Loss relief on a value basis	(10,000)
CT payable	Nil

After the above loss relief claim, the loss available to surrender to the consortium members is €420,000 (€500,000 – (€10,000 x 100/12·5)).

Major Ltd
Major Ltd is entitled to 40% of the available loss, which is €168,000 (40% x €420,000). However, the amount surrendered cannot exceed the actual profits of Major Ltd of €100,000. Therefore, its CT payable is as follows:

	€
Case I profit	100,000
Loss from Aladdin Ltd (maximum)	(100,000)
Net taxable profit	Nil
CT payable	Nil

Space Ltd
Space Ltd is entitled to 16% of the available loss, but none of this can be utilised as Space Ltd itself has made a loss in 2018. Therefore, Space Ltd will have a nil CT liability and an unused loss to carry forward of €32,000.

Diamond Ltd
Diamond Ltd is entitled to 24% of the available loss and its CT is as follows:

	€
Case I profit	2,000,000
Loss from Aladdin Ltd (24% x €420,000)	(100,800)
Net taxable profit	1,899,200
CT payable at 12·5%	237,400

The allocation of the loss arising in Aladdin Ltd is summarised below:

Loss memorandum

	€
Case I loss in Aladdin Ltd	500,000
Less: Used in Aladdin Ltd on a value basis (€10,000 x 100/12·5)	(80,000)
Available for surrender	420,000
Claimed by Major Ltd	(100,000)
Claimed by Diamond Ltd	(100,800)
Unused loss for carry forward	219,200

The unutilised loss of €219,200 will be carried forward in Aladdin Ltd and may only be used to shelter future trading profits of Aladdin Ltd.

(b) (i) Gift
A €50,000 gift would be reduced by the €3,000 small gifts exemption and the applicable class 2 threshold of €32,500 would be reduced by the previous inheritance received from the other class 2 disponer, Sharon's brother, Jack. The CAT payable by Sharon on a gift of €50,000 from Julie to Sharon would be €10,725 ((€50,000 – €3,000 – (€32,500 – €18,000)) x 33%).

Loan
The deemed annual gift to Sharon of the free use of money is valued at its opportunity cost, which in this case is the 1% per annum bank interest which would be foregone by Julie if she were to place the money on deposit. The value of the annual gift would therefore be €500 (€50,000 x 1%). This would be covered by the small gifts exemption and no CAT would be payable.

Should Sharon not repay the loan in full, any outstanding balance would be treated as a gift.

(ii) Alternative proposal

1 **Gift sufficient funds to Sharon to use the remaining class 2 threshold with the balance being given as a loan**
A gift of €17,500 would be fully sheltered by the small gifts exemption and the unused tax-free threshold (€3,000 + €32,500 – €18,000) could be made in the current year with no tax payable.

Next year, the remaining €32,500 could be loaned to Sharon from 1 January onwards and the deemed gift of free use of money would be €325 (1% x €32,500). Julie could forgive €2,675 of the loan balance (€3,000 – €325) to use up the small gifts exemption.

This process could be repeated as required in the following years until the loan is fully forgiven.

OR

2 **Pure disclaimer**
Julie could disclaim her inheritance on the intestacy. In that situation, the full residue of the estate would be inherited by Sharon from her husband and no CAT would be payable by her.

Tutorial note: *The effect of a pure disclaimer on intestacy is that the person disclaiming their share on an intestacy is deemed to have died, immediately before the death of the intestate.*

Julie should take care NOT to do a disclaimer in favour of Sharon as this would have the same tax consequences as accepting the inheritance and giving a gift to Sharon.

Marking note: *It is understood that candidates may not be fully familiar with the consequences of disclaimers on intestacy. Marks were awarded to candidates who identified either of the above proposals or provided alternative viable proposals.*

(c) Favoured nephew/niece relief

The conditions are:

(i) The assets which are subject to the gift or inheritance must be trading assets. Where the disponer carries on their business through a limited company, the relief applies to shares in that company.

(ii) The nephew/niece must have worked substantially on a full-time basis in the trade or profession for a period of five years ending on the date of the gift or inheritance.

The 'full-time basis' is defined as at least 24 hours per week.

Where the business is exclusively carried on by the disponer, his/her spouse and the favoured niece or nephew, then this requirement is relaxed to 15 hours per week.

This marking scheme is given as a guide to markers in the context of the suggested answer. Scope is given to markers to award marks for alternative approaches to a question, including relevant comment, and where well-reasoned conclusions are provided. This is particularly the case for essay-based questions where there will often be more than one definitive solution.

			Available	*Maximum*
1	**(i)**	Need for annual adjustment considered after first 12 months	1·0	
		Calculation of repayment of €12,150	1·5	
		First year recovery rate (85%) is a benchmark for the remaining life of the property	1·0	
		Date additional VAT is payable	0·5	4·0
	(ii)	**Transfer of two tablet computers to the insurance broking department**		
		VAT	1·0	
		CT and capital allowances	1·0	
		Gift of one tablet computer to Louise Smyth		
		VAT	0·5	
		CT and capital allowances	0·5	
		DWT	2·0	
		IT	1·0	6·0
	(iii)	Eligibility for cash receipts basis	1·0	
		Benefit of cash receipts basis	1·0	
		After the changeover, VAT not charged on amounts previously accounted for on the invoice basis	0·5	
		Alternative suggestions regarding improving cash flow	1·0	
			3·5	2·0
	(iv)	**Branch structure**		
		Branch losses automatically utilised against Irish profits	1·0	
		Branch profits liable to 12·5% Irish corporation tax if an Irish trade	1·0	
		Also, subject to French tax as permanent establishment	1·0	
		Credit available for French tax paid subject to maximum of Irish tax liability	1·0	
		Excess unused foreign tax credit can be carried forward	1·0	
		Subsidiary structure		
		Losses can only be offset in restricted circumstances	1·5	
		French subsidiary liable to French not Irish corporation tax	0·5	
		Dividends liable to Irish corporation tax under Schedule D Case III	0·5	
		Credit available for both withholding tax and underlying corporation tax in France	1·0	
		Excess unused foreign tax credit can be carried forward	0·5	
		Dividends will not count for close company purposes	1·0	
		Recommendation	2·0	
			12·0	10·0
	(v)	**Termination payment**		
		Statutory redundancy exempt	0·5	
		Pay in lieu of notice may be included in the lump sum if not in the contract	0·5	
		Include company car in calculation of lump sum	0·5	
		Basic exemption calculation	1·0	
		Increased basic exemption calculation	1·0	
		Calculation of average annual emoluments	0·5	
		SCSB calculation	1·0	
		Identification of income tax and USC to be deducted at source	0·5	
		PRSI not applicable *(If PRSI not included anywhere, give the ½ mark)*	0·5	
			6·0	5·0

			Available	Maximum
(vi)	**VAT**	The work did not materially alter the land	0·5	
		The land was not developed	0·5	
		Thus the sale is not VATable	0·5	
	CGT	CGT computation with part disposal	2·5	4·0

Professional marks		
Format and presentation of the memorandum	1·0	
Effectiveness of written communication	1·0	
Appropriate use of support schedules/appendix	1·0	
Logical flow of calculations	1·0	4·0
		35

2	**(a)**	**Proposal to incorporate the business**		
		Conditions which must be satisfied for incorporation relief	1·5	
		Entrepreneur relief is not possible because assets were not held for three years	0·5	
		Option 1: Claiming the relief		
		Income tax		
		Implications of cessation and short-lived business relief	1·0	
		Capital allowances, balancing charge and joint election	1·0	
		Capital gains tax		
		Calculation of proportion of gain to be deferred	3·0	
		Calculation of the CGT	2·0	
		Stamp duty: Calculation and explanation	2·0	
		Value added tax		
		Requirement to register the company	0·5	
		Implications of transfer of property	2·0	
		Option 2: Not claiming the relief		
		No requirement to transfer all of the business assets	0·5	
		Income tax		
		Cessation and capital allowances issues as with option 1	0·5	
		Capital gains tax		
		Goodwill, CGT calculation	0·5	
		Stamp duty		
		Goodwill, calculation	0·5	
		Transfer by delivery, savings	1·0	
		Collection of receivables, savings	1·0	
		Value added tax		
		Requirement to register the company	0·5	
		Election to tax the letting to avoid CGS adjustment	1·0	
		Summary of taxes payable under both options	1·0	
		Recommendation		
		Choose option 2 and do not claim the incorporation relief	0·5	
		Reasons		
		Clarification that incorporation relief is only a deferral	0·5	
		Retention of property to avoid future double charge to tax	1·0	
			22·0	20·0
	(b)	Taxable value of Marion's inheritance in January 2010	2·0	
		Taxable value of Anne's inheritance in January 2010	1·0	
		Taxable value of Anne's inheritance in May 2019	2·0	5·0
				25

			Available	Maximum
3	(a)	**Specified intangible assets**		
	(i)	Capital allowances available	0·5	
		Definition of relevant trade	1·0	
		Examples of specified assets	1·0	
		Options for calculating the capital allowances	1·0	
		Claim required to use second option	0·5	
		Rule in relation to clawback	1·0	
		Interest is allowed on borrowings re specified assets	0·5	
		Restrictions		
		Claim can only be against income from managing, developing or exploiting the asset	1·0	
		Total relief restricted to 80% of the gross income from relevant trade	1·0	
		Allow interest in priority to capital allowances	0·5	
			8·0	7·0
	(ii)	Calculation of €400,000	0·5	
		Calculation of €280,000	0·5	
		Calculation of taxable income, including the restriction	3·0	
		Carry forward of €170,000 capital allowances	0·5	
			4·5	4·0
	(b)	**Employee shares**		
	(i)	Implications for employees		
		Market value of free shares is treated as notional pay	0·5	
		Subject to IT, USC and employee PRSI (52%)	0·5	
		CGT on subsequent sale – explanation	1·0	
		Implications for employer		
		Revenue approval not required	0·5	
		Shares do not need to be offered to all employees	0·5	
		Account for all payroll taxes, similar to BIKs	0·5	
		Not subject to employer's PRSI	1·0	
		Arrangements for payment and deduction of payroll taxes over future periods	1·0	
		Alternative of withholding/selling shares	0·5	
			6·0	5·0
	(ii)	A restriction (clog) on disposal reduces their taxable value	1·0	
		Table showing deductions available	0·5	
		Effect on employee's CGT base cost	1·0	
		Restrictions on selling, assigning, transferring, pledging, etc	0·5	
		Employer places shares in a trust for the employee	0·5	
		Reporting requirements for the employer	0·5	4·0
				20

				Available	Maximum
4	(a)	(i)	Identification and conditions of consortium relief	4·0	
			Applicability to Aladdin Ltd	0·5	
				4·5	4·0
		(ii)	Aladdin Ltd: corporation tax (CT) computation	1·5	
			Aladdin Ltd: determination of consortium relief available	0·5	
			Major Ltd: CT computation	0·5	
			Major Ltd: explanation of limitation on consortium relief	0·5	
			Change Ltd: cannot avail of consortium relief	0·5	
			Space Ltd: explanation of inability to avail of consortium relief	0·5	
			Space Ltd: treatment of own loss	0·5	
			Diamond Ltd: CT computation	1·0	
			Diamond Ltd: explanation of computation	0·5	
			Aladdin Ltd: loss memorandum, calculation of unutilised loss	0·5	
			Explanation regarding remaining unused loss in Aladdin Ltd	0·5	7·0
	(b)	Assistance to her mother			
		(i)	CAT payable on a gift of €50,000		
			Small gifts exemption	0·5	
			Category 2 threshold reduced by prior inheritance from brother	1·0	
			Calculation	1·0	
			CAT payable on a loan of €50,000		
			Free use of money calculation	1·0	
			Covered by the small gifts exemption	0·5	4·0
		(ii)	Alternative proposal		
			Gift of €17,500 to utilise small gifts exemption and unused threshold		
			Loan and annual debt forgiveness		
			OR		
			Simple disclaimer		
			Either of the above		2·0
	(c)	Assets must be trading assets		0·5	
		If business is in a limited company, shares in the company qualify		0·5	
		Nephew/niece must have worked substantially full time in the five-year period ending on the date of the gift or inheritance		1·0	
		Full time means 24 hours per week		0·5	
		Alternative of 15 hours per week		0·5	3·0
					20