Answers

1 Mary Yeats

Chartered Certified Accountants
Any street
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7 November 2017

Mrs Mary Yeats
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Re: Taxation issues

Dear Mary,

I refer to our recent meeting and am writing to give my advice on the issues discussed.

(i) Tax implications of accepting the current offer from Ceramico plc

Disposal of shares

Capital gains tax (CGT)
The disposal of your Liffey Ltd shares would trigger a capital gain of €740,000 (€750,000 – €10,000).

Retirement relief would not be available to you as you would be under 55 years old on the date of disposal.

However, you would satisfy the conditions for entrepreneur relief as follows:

– You are an individual.
– You would be disposing of chargeable business assets, i.e. a holding of 5% or more of the ordinary shares in a company carrying on a qualifying trade.
– You would have been the beneficial owner of the chargeable business assets for a continuous period of three out of the five years prior to disposal.
– You would have been a director or employee of the company, and spent 50% or more of your working time in the service of the company in a managerial or technical capacity for a continuous period of three out of the five years prior to disposal.

Entrepreneur relief reduces the CGT rate on the disposal of chargeable business assets from 33% to 20% for qualifying gains of up to €1 million.

Tutorial note: *The Finance Act 2016 reduced the CGT rate to 10% for qualifying disposals on or after 1 January 2017.*

Value added tax (VAT)
There is no VAT on the transfer of shares.

Disposal of personally held business premises

CGT
The disposal of the personally held business premises would trigger a chargeable gain of €175,000 (€300,000 – €125,000).

Entrepreneur relief is not available for assets personally owned outside a company, even where such assets are used by the company, so this gain would be taxed at a rate of 33%.

VAT
VAT would not apply to the disposal of the business premises as it is an old ('non-new') property.

Loss on the sale of the development land
The original base cost of the land will be reduced by the amount of the loan written off to give a CGT base cost of €170,000 (€200,000 – €30,000). Therefore, you will have an allowable loss of €10,000 (€160,000 – €170,000), which may be offset against the above gains.

CGT payable and net proceeds
The CGT payable would be €202,450 (as per the computation in Appendix 1).

Your net after-tax proceeds would therefore be €847,550 (€750,000 + €300,000 – €202,450).

(ii) Tax planning measures to reduce the tax payable in (i)

Negligible value claim in respect of your Descent Ltd shares
Under the normal rules, the loss on your Descent Ltd shares of approximately €30,000 would crystallise only when the company is sold or liquidated. As losses cannot be carried back to an earlier tax year for CGT purposes, this would be of no benefit to you in 2017. However, a negligible value claim could be made in respect of this loss.

Where an individual owns an asset which has fallen significantly in value such that the value of the asset has become small or negligible, they can make a negligible value claim to the Inspector of Taxes. Appropriate documentation such as the most recent

set of accounts of the company should accompany the claim. If the claim is accepted, they are treated as having disposed of the asset at market value and immediately re-acquired it at the same date. The loss is then available in the year in which the claim is made.

If such a claim is made in respect of your Descent Ltd shares in 2017, this would have the effect of bringing forward the loss of €30,000, (nil proceeds – cost of €30,000) to 2017.

Sale of Hopeful plc shares
The latent loss in this shareholding is also of no benefit until it is crystallised. It is, therefore, recommended that the shareholding should be sold before 31 December 2017. Based on the information, an allowable loss of €11,000 (€6,000 – (€12,000 + €5,000)) would arise on such a sale in 2017.

As the shares are of sentimental value to you, you can buy back the shares at the prevailing market price and still use the allowable loss of €11,000 to partly shelter any other gains (e.g. as calculated in relation to (i) above). However, any repurchase must be more than four weeks after the date of disposal in order to avoid the four-week 'bed and breakfast' anti-avoidance rule.

(iii) Tax implications of selling the Liffey Ltd shares and business premises in six years' time

In six years' time you will have reached the age of 55 and so be potentially eligible for retirement relief, provided you have also:

- owned the shares in Liffey Ltd for at least ten years prior to their disposal; and
- been a director of the company for at least ten years and a full-time working director for at least five years.

Where an individual who qualifies for retirement relief disposes of shares in a family company, they may be exempt from CGT on the gains on such a disposal, subject to a limit of €750,000 on the sales proceeds, where the disposal is to a third party (i.e. not a child of the vendor).

In addition, where a business premises was personally owned for at least ten years and throughout the last ten years of ownership it was used for the trade of the company, then the premises is also a qualifying asset for the purposes of retirement relief, provided it is sold at the same time and to the same person as the shares in the company.

Accordingly, if you dispose of your shares in Liffey Ltd and the business premises in six years' time both you (as vendor) and the two assets will meet the necessary conditions for the relief, except for the sales proceeds limit of €750,000.

The current valuation of your shares and premises combined of €1,050,000 exceeds this limit. However, marginal relief may apply to reduce the CGT payable to an amount equal to one half of the excess of the proceeds over the €750,000 limit.

If, as predicted, the valuations increase over the next six years, it is not clear that retirement relief would be available or of much benefit if both the shares and the premises are sold together. If this were the case, it should still be possible to obtain entrepreneur relief (as discussed in (i) above) on the sale of the shares at that time.

(iv) Short to medium-term tax planning strategies if the company is not sold in December 2017

Assuming you defer the sale of the business for a further six years (as in (iii) above), it is recommended that the following steps are taken to optimise your tax position in the meantime.

Employment of spouse

- It is recommended that your husband, Jack, is paid an increased salary of up to €24,800 per annum, to avail of his 20% tax band.
- You can take a lower gross salary to compensate for the increase in the proposed salary to be paid to Jack
- As he has a clear role within the organisation, the payment of this amount of salary to him should not cause a problem with the Revenue.
- The annual tax saving arising from this recommendation will amount to €4,560 ((€24,800 – €2,000) x (40% – 20%)).
- Furthermore, Jack could be entitled to a termination payment on the ultimate sale of the business to which tax relief would apply.

Marking note: *Alternatively, Mary could remain on the same gross salary, which would be beneficial in relation to future pension benefits and possible termination payments and Jack could be paid his salary in addition to Mary's remuneration.*

Set up a corporate pension scheme
There are significant benefits in setting up a Revenue approved corporate pension scheme.

- It is a tax efficient method of extracting funds from a company. The contributions paid by the company (as employer) in an accounting period are fully tax deductible except where the contributions are considered to be excessive.
- The contributions made by the company are not subject to the same restrictions as those applicable to personal pension contributions made by an employee or director.
- Contributions made by an employer do not give rise to a benefit in kind for the employee/director.

This option should be considered in relation to both yourself and Jack (assuming his salary is increased, as suggested above).

(v) Exit related tax planning opportunities

The following options may enable you to achieve a more tax efficient outcome on a future sale:

Transfer of a 50% interest in the shares and premises to Jack
It would be advisable to transfer 50% of your shares in Liffey Ltd to your husband Jack and arrange for him to take a full-time role in the business as soon as possible. This is necessary to enable him to also meet the retirement relief requirements of being a full-time working director for five years.

Tutorial note: *The required period as a full-time working director can be any five years.*

Your period of ownership of the shares is taken into account as if it were a period of ownership by Jack so he will meet the ten-year ownership requirement.

The implementation of the above could result in the total sale proceeds eligible for retirement relief to be up to €1,500,000 (€750,000 x 2) on a future sale to a third party.

However, Jack will only qualify for retirement relief once he reaches the age of 55, so it will be necessary to wait at least seven years from now (not just six) before any sale of his shares.

It would also be advisable to transfer the premises into both names, as based on the higher overall limit, it is possible that the sale of the premises would also qualify for retirement relief if it were to be sold at the same time as the shares in the company (as explained in (iii) above).

It is very important that no business assets are transferred by you to Jack after you reach the age of 55 or vice versa, as these assets will then be counted for the purposes of the €750,000 limit.

Marking note: *Marks were also awarded to candidates who identified that Jack would be eligible for entrepreneur relief (instead of retirement relief) on the shares only and explained what he would need to do to meet the criteria for that relief. In particular, he would need to spend 50% or more of his working time in the company for a continuous period of three out of the five years prior to disposal. The advantage of Jack claiming entrepreneur relief is that he would not have to wait until he reaches age 55.*

Termination payments
There would be scope for the company to pay a tax free lump sum termination payment to both yourself and Jack prior to the proposed disposal of the shares in six years' time. The amount of the tax free lump sum would be based on the number of years of service with the company and your salary for the last three years. The tax free amount of the lump sum would, however, be reduced by any lump sum payable from a pension fund (see below).

Pension lump sum
There is an opportunity to maximise the pension lump sum payable to you and Jack on your retirement. Assuming both you and Jack would be proprietary directors, your final pensionable remuneration must be the average of any three consecutive years in the last ten years. A lump sum of one and a half times final pensionable remuneration is payable to employees with 20 years of service with the company. But this figure is reduced in situations where there is less than 20 years of service (as in this case).

Both of the above planning opportunities (termination payments and pension lump sum) would have the effect of reducing the value of the company's shares, which could also be beneficial in relation to qualifying for retirement relief.

Sale of shares only and retention of premises
You may also consider only selling the shares to any prospective purchaser and availing of retirement relief or marginal relief thereon.

The business premises could then be sold at a later date and while any gain would be subject to tax at 33%, such a sale should not result in a clawback of any earlier retirement relief as the premises would no longer be a qualifying asset, since it would not have been sold at the same time as the shares.

(vi) VAT treatment of equipment

Where goods are installed or assembled by or on behalf of the supplier, the place of supply is the place where the goods are installed or assembled. Therefore, in this case the place of supply will be Ireland and as Liffey Ltd is registered for Irish VAT, it should self-account for the VAT on the supply and claim a simultaneous input credit as the goods will be used for taxable business.

(vii) Paul Klimt's Irish income tax position

Paul will qualify for the special assignee relief programme (SARP) as he:

- has a base salary of at least €75,000;
- will have been a full-time employee of a company tax resident in a country with which Ireland has a double taxation agreement for six months immediately prior to his arrival;
- will arrive in Ireland to perform duties for his employer; and
- will become tax resident in Ireland, not having been tax resident in Ireland for the five tax years immediately preceding the year of arrival.

The SARP relief applicable to Paul will be €19,500 ((€140,000 – €75,000) x 30%) and his taxable income in Ireland for 2018 will be €125,500 (€145,000 – €19,500).

If you have any queries in relation to any of the above, please contact me.

Yours sincerely,

A N Accountant

Appendix 1

CGT computation re Ceramico plc offer

	Shares	Premises	Total
	€	€	€
Proceeds	750,000	300,000	
Less: Cost	(10,000)	(125,000)	
Gain	740,000	175,000	
Less: Loss forward		(10,000)	
Taxable gain	740,000	165,000	
CGT rate	20%	33%	
CGT payable	148,000	54,450	202,450

2 Elaine Robinson

(a) Capital acquisitions tax (CAT) payable on inheritances

Cecilia

	€
Dwelling house	950,000
Cash and other savings	65,000
Value of inheritance	1,015,000
Less: Class 2 threshold	(30,150)
Taxable benefit	984,850
CAT at 33%	325,001

Joe

	€
Value of inheritance	520,000
Less: Class 3 threshold	(15,075)
Taxable benefit	504,925
CAT at 33%	166,625

Tutorial note: *The prior inheritance from Simon, Joe's uncle, is class 2 and therefore is not aggregated in computing the tax on the current benefit from Elaine.*

Ben

	€
Value of inheritance	120,000
Less: Class 2 threshold	(30,150)
Taxable benefit	89,850
CAT at 33%	29,651

Tutorial note: *The prior inheritance from Ben's father is class 1 and therefore is not aggregated in computing the tax on the current benefit from Elaine.*

(b) Tax issues on a lifetime transfer of the office unit and the painting

Value added tax (VAT)

The transfer of ownership of the office unit will not result in a charge to or clawback of VAT as it is an old building and it has not been developed since its construction.

Capital gains tax (CGT)
A gift of property is chargeable to CGT as if it were a sale at full market value. The deemed gain is calculated in the normal way and taxed at 33%. The tax is payable by the person making the disposal.

CAT
CAT is payable at 33% on the value of the benefit less the small gift exemption and the exempt threshold. A credit may be claimed against the CAT payable on the gift for any CGT payable on the same event. However, the asset must be held for two years to avoid a clawback of this credit.

Stamp duty (SD)
SD applies to transfers of property, and in the case of non-residential property, such as the office unit in Dublin, it is at a rate of 2%.

It is assumed that the painting would be transferred by delivery and therefore SD would not apply.

Tax liabilities

Joe

	€	€
CGT		
Deemed proceeds		520,000
Less: Cost	390,000	
Indexation factor	1·277	(498,030)
Gain		21,970
Annual exemption (utilised against painting)		–
Taxable gain		21,970
CGT at 33%		7,250
SD		
Taxable amount		520,000
SD at 2%		10,400
CAT		
Market value		520,000
Less: Stamp duty		(10,400)
Small gift exemption		(3,000)
		506,600
Less: Class 3 threshold		(15,075)
Taxable benefit		491,525
CAT at 33%		162,203
Less: Credit for CGT		(7,250)
CAT payable		154,953
Summary		
CGT		7,250
Stamp duty		10,400
CAT		154,953
Total tax payable		172,603

Ben

	€	€
CGT		
Deemed proceeds		120,000
Less: Cost (probate value)	5,000	
Indexation factor	1·144	(5,720)
Gain		114,280
Annual exemption		(1,270)
Taxable		113,010
CGT at 33%		37,293

CAT

	€
Market value	120,000
Less: SD	0
Small gift exemption	(3,000)
	117,000
Less: Class 2 threshold	(30,150)
Taxable benefit	86,850

	€
CAT at 33%	28,661
Less: Credit for CGT (maximum)	(28,661)
CAT payable	0

Summary

CGT	37,293
CAT	0
Total tax payable	37,293

(c) Preferable option for Elaine

If the lifetime transfer option is chosen, the total additional tax payable by Elaine and the beneficiaries would be as follows:

– The transfer to Joe would result in an additional €5,978 (€172,603 – €166,625).
– The transfer to Ben would result in an additional €7,642 (€37,293 – €29,651).

However, the CGT element on the lifetime transfer to Joe would be €7,250 and on the lifetime transfer to Ben would be €37,293. These amounts would be additional amounts payable by Elaine if she chooses this option. It is therefore recommended that she transfer the assets on her death, unless it can be agreed that all taxes payable as a result of a lifetime transfer must be paid by the beneficiaries.

(d) Mitigation of CAT on Cecilia's inheritance of the Galway house

An inheritance of a dwelling, together with its grounds to an area of up to one acre, is exempt from CAT where all of the following conditions are satisfied:

– The dwelling house has been occupied as the only or main residence of the beneficiary for a period of three years immediately preceding the date of the inheritance.

– The beneficiary is not, at the date of the inheritance, entitled to any interest in any other dwelling.

– If the beneficiary is under the age of 55 at the date of the inheritance, they must continue to occupy the residence for a period of six years thereafter, to avoid a clawback of the relief.

Cecilia can only qualify for this relief if she disposes of her own apartment before taking the inheritance of Elaine's principal private residence. In that event, she would qualify for the relief if she resides in the dwelling house continuously for the three-year period up to the date of the inheritance from her aunt. As Cecilia is currently aged 51, if she inherits the property within the next four years, she will also be required to occupy it for six years.

Cecilia would incur CGT on the sale of the apartment but this would be considerably less than the CAT arising on the inheritance of the dwelling house from Elaine. This is not only because the absolute value of the apartment is less but also because of the principal private residence relief available on the apartment.

(e) Incorporation of Ben's architect's practice

Following incorporation, corporation tax at the rate of 12·5% will apply to the practice's retained profits. On the assumption that Ben takes a salary equivalent to his current drawings amount of €90,000, the company's retained profits would be €30,000.

However, the professional services surcharge will effectively add tax of a further 6·56% ((100% – 12·5%) x (50% x 15%)), if the profits are not distributed within 18 months of the year end.

Therefore, Ben's immediate tax savings if no distribution occurs within this period would be €10,482 ((€10,000 x (52% – (12·5% + 6·56%)) + €20,000 x (55% – (12·5% + 6·56%))).

However, if Ben subsequently extracts the after-tax retained funds from the company, either as a salary or as a dividend, he will be taxed at his marginal income tax rate of 40% plus PRSI and USC, i.e. potentially at 52% to 55% (because of the additional USC surcharge on Case II earnings over €100,000).

Incorporation would, however, give the opportunity for the company to make a contribution of the excess €30,000 to a Revenue approved pension fund on behalf of Ben. This would be tax efficient insofar as the company would receive a corporation tax deduction for the amount contributed and there would be no income tax implications for Ben. But this assumes that the €30,000 is not otherwise required to fund the continued expansion of the practice.

3 (a) Yellow Ltd and its shareholders – Corporation tax (CT) for 2016

The applicable relief is consortium relief. All the shareholder companies qualify for the relief except for River Ltd. River Ltd does not qualify because it is resident in neither the EU nor the EEA.

Yellow Ltd
Yellow 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	60,000
CT at 25%	15,000
Less: Loss relief on a value basis	(15,000)
CT payable	Nil

After the above loss relief claim, the loss available to surrender to the consortium members is €280,000 (€400,000 – (€15,000 x 100/12·5)).

Big Ltd
Big Ltd is entitled to 45% of the available loss and its CT is as follows:

	€
Case I profit	210,000
Loss from Yellow Ltd (45% x €280,000)	(126,000)
Net taxable profit	84,000
CT payable at 12·5%	10,500

Coyote Ltd
Coyote Ltd is entitled to 28% of the available loss, which is €78,400 (28% x €280,000). However, the amount surrendered cannot exceed the actual profits of Coyote Ltd of €70,000. Therefore, its CT payable is as follows:

	€
Case I profit	70,000
Loss from Yellow Ltd (maximum)	(70,000)
Net taxable profit	Nil
CT payable	Nil

Trees Ltd
Trees Ltd is entitled to 7% of the available loss, but none of this can be utilised as Trees Ltd itself has made a loss in 2016. Therefore, Trees Ltd will have a nil CT liability and an unused loss to carry forward of €17,000.

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

Loss memorandum

	€
Case I loss in Yellow Ltd	400,000
Less: Used in Yellow Ltd on a value basis (€15,000 x 100/12·5)	(120,000)
Available for surrender	280,000
Claimed by Big Ltd	(126,000)
Claimed by Coyote Ltd	(70,000)
Unused loss for carry forward	84,000

The unutilised loss of €84,000 will be carried forward in Yellow Ltd and may only be used to shelter future trading profits of Yellow Ltd.

(b) Hendrix Ltd

(i) Tax relief in relation to specified intangible assets

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

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 activities related to 'managing, developing or exploiting specified intangible assets' (income from the relevant trade). This income must be separately identified.

(2) The relief for capital allowances and certain interest costs is restricted to 100% 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 2016

Intangible asset capital allowances
Option 1: Accounting treatment: Annual amortisation of patents €300,000 (€3,000,000/10).

Option 2: Writing off over 15 years at 7% per annum: €210,000

Option 1 will be claimed because it is the higher.

Taxable income

	€
Relevant trade (excluding allowances and interest)	380,000
Intangible asset capital allowance	(280,000)
Interest costs incurred	(100,000)
Taxable income from relevant trade	0
Add: Non-relevant trade income	140,000
Total taxable income	140,000

The maximum relief available is €380,000 (100% x €380,000). The €100,000 interest is allowed in full and the capital allowances are restricted to €280,000. The unutilised capital allowances of €20,000 (€300,000 – €280,000) are carried forward to be offset against future years' relevant trading income.

4 Tavares Ltd

(a) (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 eight 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).

Tavares Ltd (employer)
Revenue approval is not required for share awards and the shares do not need to be offered to all employees.

Tavares 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.

Tavares 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, Tavares 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.*

(b) Income tax relief for foreign travel

Foreign earnings deduction (FED) relief applies to individuals on assignment in qualifying countries. These countries include China, India and Russia, but not Austria and France.

Tutorial note: *Qualifying countries originally included Brazil, Russia, India, China and South Africa (known as the 'BRICS' countries). The list of countries was extended to include 22 more countries including, Egypt, Japan, UAE, Kuwait and Singapore.*

The conditions for relief are that:

– The individual must be present in the relevant state for at least three consecutive qualifying days for the performance of the duties of the office or employment. Weekends and/or public holidays will be counted towards qualifying days.

– In any year or 12-month period, the individual must have spent at least 40 qualifying days in the qualifying countries.

It appears that Tony satisfies these conditions, so the relief will be:

– granted from income tax but not from PRSI or USC;
– reduced by any double taxation credits; and
– restricted by the higher earners' restriction.

Where FED is claimed, the employee may not claim other reliefs relating to employment income in the same year, such as split year residence relief, cross border workers relief, remittance basis on employment income, special assignee relief programme (SARP) or the surrender of R&D credit relief for key employees.

The amount of the deduction is the lesser of €35,000 and the proportion of employment income relating to the number of qualifying days worked in a relevant state in the tax year (the specified amount). For this purpose, income from employment includes any taxable share options derived from the employment, less any qualifying pension premium but excludes any tax deductible expense payments, benefits in kind, termination payments and payments under restrictive covenants.

Therefore, Tony will be entitled to an income tax refund on a specified amount of €24,658 (€150,000 x 60/365), being €9,863 (€24,658 x 40%).

(c) Circumstances in which a charge to Portuguese corporation tax could arise

Under the OECD tax treaty, the business profits of an enterprise can only be taxed in a country where the enterprise is either resident or has a permanent establishment (PE).

On the basis that Tavares Ltd is an Irish company which is managed and controlled in Ireland, it would be Irish resident and not Portuguese resident.

Only if Tavares Ltd is considered to have a PE in Portugal will it be subject to Portuguese corporation tax.

The following points are relevant to the establishment of a PE:

– A PE is 'a fixed place of business in which the business of the enterprise is wholly or partly carried out'.
– A branch or office is a PE, but facilities used for the storage, display or delivery of the goods belonging to the enterprise, such as the warehouse in this case, are not considered to be a PE.
– An agent or employee based in the foreign country, but not working from a fixed place of business of the enterprise will be considered a PE if he/she has and habitually exercises the authority to conclude sales contracts for the enterprise.

Therefore, whether Tavares Ltd will be deemed to have a Portuguese PE will depend on the authority allowed to the Portugal-based salesperson. If that individual can follow up queries and pass over orders but cannot conclude a sales contract, then there would be no Portuguese PE. However, if they can conclude sales contracts, there would be a Portuguese PE and the profits earned in Portugal would be subject to Portuguese corporation tax.

Recommendation
Unless there are good commercial reasons for doing so, Tavares Ltd should NOT give authority to conclude contracts to its Portugal based salesperson as this will avoid the setting up of a Portuguese PE.

Marking note: *Marks will be awarded for referring to either the OECD tax treaty or the Ireland/UK tax treaty.*

5 Suresale Ltd

(a) Capital goods scheme

A developed property has a value added tax (VAT) life of 20 years and a life of ten years on any redevelopment of the property. The VAT incurred on the acquisition or development of a property is deductible in accordance with the normal rules relating to deductibility.

When a property is acquired, an immediate estimate of the VAT recovery rate is required to be made. A person who is engaged in a fully taxable economic activity is entitled to deduct 100% of the VAT charged on the acquisition or development of a property to be used in the business. A person who is engaged in partly taxable and partly exempt economic activities is only entitled to deduct the percentage of the VAT charged which corresponds to the percentage of taxable use.

At the end of the first 12 months following completion (or acquisition, where the property is acquired following completion), the taxpayer must review the amount of VAT deducted on the acquisition or development of the property. If the proportion of taxable use of the property during that 12-month period differs from the proportion of the VAT deducted on the acquisition or development of that property, then an adjustment is required. If too much has been deducted, the taxpayer must pay back the excess. If too little has been deducted, the taxpayer is entitled to claim the deficiency as an input credit.

Similar annual comparisons must be performed using the first year recovery rate as the benchmark rate for the remaining VAT life of the property. However, where there is a very substantial change in the use of the property (i.e. 50% or more), this is called a 'big swing' and further adjustments are required, including the re-balancing of the benchmark figure.

Every owner is obliged to keep a capital goods record in respect of each property owned, which must be kept up to date and passed on to the future purchaser in the event of a sale of the property.

(b) VAT implications of transactions

(i) Sale of North Dublin premises

The sale of the building on 30 April 2016 took place within five years of the completion of the repair and decoration work on 30 June 2014. However, the repair and decoration work:

(1) did not materially alter the building, (as it was still an office after its completion); and
(2) did not cost more than 25% of the sales consideration (€160,000/€800,000 = 20%).

Therefore, the work done would be considered minor development and so not have the effect of making the building a 'new' building. As the building remained a 'non-new' building after the work was done, the sale of the building would be exempt from VAT.

Tutorial note: *This is not a single let property, so transfer of business relief does not apply.*

(ii) Sale of South Dublin branch

The transfer of the assets of a business is VAT exempt where those assets constitute an undertaking or part of an undertaking capable of being operated on an independent basis. For this relief to apply, the purchaser must also be a VAT registered entity. The sale of the South Dublin branch satisfies both criteria and therefore Suresale Ltd was correct in not charging VAT on the transaction.

There are no VAT implications for Suresale Ltd in relation to the ending of their short-term lease of the South Dublin premises.

(iii) City centre premises

At the end of the initial interval period, i.e. 31 August 2016, Suresale Ltd calculated that the use to which the property had been put during the initial interval was only 75% taxable. As Suresale Ltd deducted 100% of the VAT charged initially, it is now obliged to make an adjustment (because there is a difference between these two figures).

The total reviewed deductible amount is €101,250 (€1,000,000 x 13·5% x 75%), so there will be a clawback of the difference of €33,750 (€135,000 – €101,250).

The annual reference deduction amount is now €5,063 (€101,250/20). At the end of the second and subsequent intervals (i.e. 31 December 2016 and each 31 December thereafter), the proportion of taxable use will need to be reviewed.

(iv) Repairs to city centre premises

VAT reclaimable
Suresale Ltd will be entitled to reclaim input VAT in proportion to the use to which the premises has been put, i.e. 75% for the taxable activity.

VAT element of the invoice (€1,000 x 13·5/113·5)	€119
Allowable amount (75%)	€89

Proposed unsupported cash payment
The method of payment (cash, cheque or bank transfer) is not relevant from a tax viewpoint. However, if Suresale Ltd were to make a payment in cash, without receiving a supporting invoice, it would not be entitled to claim a VAT input credit or a corporation tax deduction for the work done.

It appears that the electrician is attempting to evade tax by receiving a cash payment. In the event of a Revenue audit, payments such as these could be queried with potential serious consequences for the company.

Suresale Ltd should explain to the electrician that they will make payment only on receipt of a valid invoice. If the electrician is not satisfied with this arrangement, the company should seek a different electrician.

(v) UK solicitor

This is a business to business (B2B) transaction, so the place of supply of the legal services is where Suresale Ltd's (the customer's) business is established, i.e. Ireland. Therefore, Suresale Ltd is the taxable person and VAT should be accounted for on the reverse-charge basis.

The VAT of €1,380 (€6,000 x 23%) should be included in Suresale Ltd's VAT return as output VAT and it will also be entitled to reclaim the total amount as input VAT, as the legal services relate exclusively to its taxable activity.

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)**	Disposal of shares		
		Retirement relief not available	0·5	
		Entrepreneur relief and conditions	2·0	
		20% rate on sale of shares	0·5	
		VAT will not apply	0·5	
		Disposal of premises		
		33% rate on premises (no entrepreneur relief)	1·0	
		Loss on development land can be offset	0·5	
		Calculation of allowable loss	1·0	
		Calculation of CGT payable	1·0	
		Calculation of net proceeds	0·5	
			7·5	6·0
	(ii)	Identification of €30,000 latent loss in Descent Ltd	0·5	
		Recommendation re negligible value claim	1·0	
		Explanation of requirements of negligible value claim	2·0	
		Effect in terms of 2017 loss	0·5	
		Recommendation to sell shares in Hopeful Ltd in 2017	1·0	
		Calculation of allowable loss	0·5	
		Suggest buy-back of shares after four weeks	1·0	
			6·5	5·0
	(iii)	Retirement relief (RR) conditions re the vendor (0·5 x 3)	1·5	
		Applicability of RR to premises, with conditions	1·5	
		Problem of combined proceeds exceeding €750,000/marginal relief	1·5	
		Entrepreneur relief would still be available re shares	1·0	
			5·5	4·0
	(iv)	Employment of spouse	3·0	
		Company pension scheme	3·0	
			6·0	5·0
	(v)	Transfer 50% of shares to Jack	0·5	
		Jack to take a full-time role in the business for five years	0·5	
		Mary's share ownership period transfers to Jack	1·0	
		Need to delay the sale of shares until Jack reaches 55	0·5	
		Transfer premises into joint names	0·5	
		Do not transfer between spouses after age 55	1·0	
		Lump sum termination payments	1·0	
		Pension lump sums	1·0	
		Effect of lump sum payments on retirement relief	0·5	
		Sale of shares only and retention of premises to later date	0·5	
			7·0	6·0
	(vi)	Place of supply is where equipment was installed	1·0	
		Self-account for the VAT with entitlement to input credit	1·0	2·0

			Available	Maximum
	(vii)	Conditions of relief (4 x 0·5)	2·0	
		Calculation of taxable income	1·5	
			3·5	3·0
	Professional marks			
		Format and presentation of the letter	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)**	CAT computation: Cecilia	1·0	
		Dwelling house relief not available	1·0	
		CAT computation: Joe	1·0	
		Business property relief not available	0·5	
		Ignore prior inheritance	0·5	
		CAT computation: Ben	1·0	
		Ignore prior inheritance	0·5	
			5·5	5·0
	(b)	No charge to VAT on the transfer of the office and explanation	1·0	
		CGT is payable by person making the disposal	0·5	
		Explanation of CAT issues including credit for CGT	1·0	
		Explanation of SD issues including transfer by delivery	1·0	
		Joe CGT computation	1·5	
		SD computation	0·5	
		CAT computation	2·0	
		Summary	0·5	
		Ben CGT computation	1·5	
		CAT computation	1·5	
		Summary	0·5	
			11·5	10·0
	(c)	Comparison	1·0	
		Choice of options	0·5	
		Reason for choice	1·5	3·0
	(d)	Dwelling house relief: house plus one acre exempt from CAT	1·0	
		Conditions (3 x 0·5)	1·5	
		Cecilia needs to dispose of her own apartment	0·5	
		Reside for three years continuously with Elaine	0·5	
		Comment re CGT v CAT position	1·0	
			4·5	3·0
	(e)	12·5% CT rate applies to retained profits only	1·0	
		Surcharge of effectively 7·5%	1·0	
		18-month time limit for distribution	0·5	
		Income tax at marginal rate plus PRSI and USC to extract retained funds	1·0	
		Benefits of company making pension contributions	1·0	
			4·5	4·0
				25

				Available	Maximum
3	(a)		Identification of consortium relief	1·0	
			All companies qualify except River Ltd	1·0	
			Yellow Ltd: corporation tax (CT) computation	1·5	
			Yellow Ltd: determination of consortium relief available	0·5	
			Big Ltd: CT computation	1·0	
			Big Ltd: explanation of computation	0·5	
			Coyote Ltd: CT computation	0·5	
			Coyote Ltd: explanation of limitation on consortium relief	1·0	
			Trees Ltd: explanation of inability to avail of consortium relief	1·0	
			Trees Ltd: treatment of own loss	0·5	
			Yellow Ltd: loss memorandum, calculation of unutilised loss	0·5	
			Explanation regarding remaining unused loss in Yellow Ltd	1·0	
				10·0	9·0
	(b)	(i)	Capital allowances available	0·5	
			Examples of specified assets	1·0	
			Options for calculating the capital allowances	1·0	
			Rule in relation to assets with an infinite life	0·5	
			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 100% of the gross income	1·0	
			Restriction applies firstly re the capital allowances, then the interest.	0·5	
				7·5	7·0
		(ii)	Calculation of €300,000	0·5	
			Calculation of €210,000	0·5	
			Calculation of taxable income, including the restriction	3·0	
			Carry forward of €20,000 capital allowances	0·5	
				4·5	4·0
					20

				Available	Maximum
4	(a)	(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	0·5	
			Arrangements for payment and deduction of payroll taxes over future periods	1·0	
			Alternative of withholding/selling shares	0·5	
				5·5	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	1·0	
				4·5	4·0
	(b)		Identification of foreign earnings deduction	0·5	
			Explanation of the conditions	2·0	
			Relief available/restrictions	2·0	
			Method for calculating relief	1·5	
			Refund due	1·0	
				7·0	6·0
	(c)		Explanation of charge to foreign tax	1·0	
			Irish not Portuguese tax resident	0·5	
			Points regarding permanent establishment (3 x 1)	3·0	
			Identification of agent position as key issue and recommendation	1·5	
				6·0	5·0
					20

				Available	Maximum
5	(a)		Tax life of 20 or ten years	1·0	
			Initial recovery rate on acquisition	1·5	
			Review and adjustment after one year	1·5	
			Annual comparisons with first year recovery rate for remainder of life	1·0	
			More substantial adjustments if there is a 'big swing'	1·0	
			Capital goods record	0·5	
				6·5	6·0
	(b)	(i)	Sale within five years	0·5	
			No material alteration of the building	1·0	
			Cost of works less than 25% of consideration	1·0	
			Conclusion: not 'new' so exempt	0·5	
		(ii)	Exemption for transfer of undertaking	1·0	
			Requirement for purchaser to be VAT registered	1·0	
			Correct not to charge VAT	0·5	
			No VAT implications in relation to short-term lease of premises	0·5	
		(iii)	Explanation of need for an adjustment	1·0	
			Calculation of reviewed deductible amount €101,250	1·0	
			Clawback of €33,750	0·5	
			Annual reference amount €5,063	0·5	
			Reference to need for subsequent reviews	0·5	
		(iv)	Calculation of allowable input VAT	1·5	
			VAT and CT consequences of not receiving an invoice	1·0	
			Potential consequences of a Revenue audit	1·0	
			Recommendation	0·5	
		(v)	Place of supply is Ireland, with reason	1·0	
			Account for VAT on a reverse-charge basis	0·5	
			Calculation of output VAT	0·5	
			Explanation of input VAT credit	0·5	
				16·0	14·0
					20