CIPFA

TAXATION
REPUBLIC OF IRELAND

Diploma stage examination

12 June 2006

MARKING SCHEME

AT THE HEART OF
YOUR CAREER

Question 1

(a) A "period of account" is a period of time for which a company makes up a set of accounts. An "accounting period" (for corporation tax purposes) is a period of time for which a corporation tax assessment is raised. *1*

In general, an accounting period is deemed to end on the *earlier* of:

- the expiration of 12 months from the beginning of the accounting period
- the end of a period of account. *1*

The consequences of this rule are as follows:

(i) A period of account of up to 12 months in length comprises a single accounting period and results in a single corporation tax assessment.

(ii) A period of account exceeding 12 months in length is subdivided into two or more accounting periods, each resulting in a separate corporation tax assessment. The first accounting period is the first 12 months of the period of account. The second accounting period is the next 12 months of the period of account (and so forth). If the length of the period of account is not an exact multiple of 12 months, the final accounting period will be of less than 12 months' duration. *1*

Therefore the period of account consisting of the 16 months to 31 December 2005 is divided into two accounting periods, which are the 12 months to 31 August 2005 and the 4 months to 31 December 2005. *1*

(4)

(b) Industrial buildings allowances

- The cost of the land (€250,000) is excluded from the qualifying expenditure. *1*
- The building's cost is £500,000 and the general offices (€140,000) account for 28% of this, exceeding the 10% limit. Therefore the cost of the general offices cannot be treated as qualifying expenditure. *2*
- No IBAs are available in the year to 31 August 2005, since the building was not acquired until 1 September 2005. *1*
- IBAs for the 4 months to 31 December 2005 are 4% x €360,000 x 4/12 = €4,800. *1*

Capital allowances on plant and machinery:

	General Equip.	Computer Equip	Cars	Total	W&T	
	€	€	€	€	€	
31/08/03 Additions	308,167	71,167	44,000	423,334		
31/08/03 W&T					(84,667)	
31/08/04 W&T					(84,667)	
31/08/05 Additions	108,800	0	46,300			
31/08/05 Disposals	(11,000)	(42,700)	(22,000)			
	405,967	28,467	68,300	502,734		
31/08/05 W&T					(109,947)	2
31/12/05 Additions	15,000					
	420,967	28,467	768,300	517,734		
31/12/04 W&T (4 months)					(34,645)	2

BALANCING ALLOWANCES/CHARGES

SALE OF LEXUS CAR

SALE PROCEEDS (RESTRICTED – 30,000 X 22,000/27,600) = €23,913

TWDV (60% OF RESTRICTED COST) = €13,200
BALANCING CHARGE = €10,713

RESTRICT TO CA'S CLAIMED (22,000 –13,200) = €8,800 2

SALE OF COMPUTER EQUIPMENT

SALE PROCEEDS = €29,500
TWDV = €25,620
BAL CHARGE = €3,880 1

SALE OF MACHINERY

PROCEEDS = €3,400
TWDV = €6,600
BAL ALLOW =€3,200 1

SUMMARY OF CAPITAL ALLOWANCES CLAIM

12 MONTH PERIOD TO 31.08.05

WEAR AND TEAR	*€88,914*
BALANCING ALLOWANCES	*€3,200*
BALANCING CHARGES	*(€12,680)*
TOTAL TO 31.08.05	*€79,434*

4 MONTH PERIOD TO 31.12.05

WEAR AND TEAR	*€30,263*
Industrial buildings allowance	*€4,800*
	€35,063

(13)

(c) Land sold July 2005

	Original cost	*Rebasing*	
	€	**€**	
Disposal proceeds		1,500,000	
Less: Part cost €1.5m/€2.25m x €120,000	80,000		*1*
Index factor 6.080	6.080	(486,400)	*1*
Chargeable Gain		**1,013,600**	

Chattel sold November 2005

		€	
Disposal proceeds		8,400	
Less: Cost	2,500		
Index factor 5.238	5.328	13,095	*1*
Loss		**(4,695)**	*½*
No Loss/No Gain			*1*

A rollover relief claim is not possible as the disposal took place after 4 December 2002. *1 ½*

(6)

(d)

	y/e 31/8/05 €	**4 months to 31/12/05 €**	
Trading profit (€864,800 + €194,000)	794,100	264,700	*1*
Less: Donation	(10,000)		*1*
Less: Capital allowances	(79,434)	(35,063)	*1*
Schedule D Case I	704,666	229,637	
Schedule D Case V:			
Rent for 5 months	10,000		*1*
Rent for 4 months		8,000	*1*
Premium €25,000 x (100% - (4 x 2%)	23,000		*1*
Schedule D Case III			
Interest for 1 month	5,000		*1*
Interest for 4 months		20,000	*1*
Chargeable gains			
y/e 31/8/05 (1,013,600 -74,400)	939,600		*1*
4 months to 31/12/05		Nil	*1*
Total Profits	**1,682,266**	**257,637**	

	y/e 31/8/05 €	**4 months to 31/12/05 €**	
Corporation tax due:			
Trading profits @12.5%	88,083	28,705	*1*
Passive income @ 25%	9,500	7,000	*1*
Chargeable gains @ 20%	187,920		*1*
Total tax payable	**285,503**	**35,704**	

72% of the Corporation tax for the year to 31 August 2005 is payable on or before 21 July 2005, a further 18% is due on or before 21 February 2006 and the balance is due on or before 21 May 2006.

For the period ended 31 December 2005, 72% due on or before 21 November 2005, 18% due on or before 21 June 2006, balance due on or before 21 September 2006. *4*

(17)

(40)

Question 2

(a)

	€	€	
Salary		52,000	½
Bonus		10,000	½
Living accommodation:			
market value of rent	14,400		½
Furniture 5% x €18,500	925		1
Ancillary costs	4,355	19,680	½
Free meals 240 x €5		1,200	1
Mileage allowance:			
Taxable amount (technically but see below)		1,000	1
Parking space (exempt)		-	½
Beneficial loan:			
€24,000 x 3.5% x 151/365	348		2
€18,000 x 3.5% x 183/365	316		
€6,000 x 3.5% x 31/365	18	682	
Suggestion scheme award (all taxable)		1,000	1
		85,562	
Less: Pension contributions €52,000 x 10%		5,200	½
Taxable Employment income		80,362	
Tax Payable			
€29,400 @ 20%		5,880	½
€50,962 @ 42%		21,404.04	½
		27,284.04	
Less			
PAYE Tax Credit		1,270	½
Age Tax Credit (eligible because spouse >65)		205	½
Total Tax Payable		**25,809.04**	

(11)

(b) The deductions allowed against Schedule E income are limited to the following

- Expenses incurred wholly, exclusively and necessarily in the performance of the duties of the employment.
- Employee contributions to an exempt approved pension scheme, and in the case of a non-pensionable office or employment, premiums paid under certain approved retirement annuity contracts as well as certain contributions to PRSAs

In practice the Revenue also allows the following;

- Expenditure on special clothing worn in the performance of the duties
- Expenditure on tools used in the performance of the duties.
- Expenditure on books and newspapers is allowed to journalists
- Expenses incurred by commercial travellers who are required to bear traveling and hotel expenses in the course of performing their duties.

(5)

(c)

	€	
NIB investment account interest (Case IV)	118.75	½
BSI €4,960 x 100/80 (Case IV)	6,200.00	½
Irish dividends (Schedule F) €61,200/.8	76,500.00	½
Taxable income	82,818.75	
Income tax due:		
€35,718.75 x 20% (29,400 + 118.75 + 6,200)	7,143.75	½
€47,100 x 42%	19,782.00	½
	26,925.75	
Less		
Married persons tax credit	3,160.00	*1*
Age Tax Credit (> 65)	205.00	*1*
Dividend withholding tax	15,300.00	*1*
DIRT	1,263.75	*1*
Income Tax payable	**8,386.25**	

Notes:

Suzanne is over 65 and therefore both herself and Steven qualify for the Age tax credit. If one spouse is 65 or more then both persons are entitled to the credit. *1 ½*

(8)

(d) The 2005 tax return must be submitted by 31 October 2006 ½

The Revenue Commissioners have four years from the end of the Chargeable period to which the Return relates. So for example, the Revenue may initiate a query in relation to the 2005 Return at any time up to 31 December 2005. *1*

There is no time limit where a Fraudulent Return has been made ½

(2)

(e) Tax relief is available for donations to charities and approved bodies.

An 'approved body' is one named on a list as issued by the Revenue Commissioners. ½

Conditions of relief

- Minimum donation of €250.
- No maximum figure unless the individual is associated with the Charity in which case the max donation is capped to 10% of individuals total income;
- Donation must be in the form of money and must not be repayable;
- The donation must not confer any benefit on the donor or any person connected with the donor;
- The donation must not be conditional on, or associated with, any arrangements involving the acquisition of property by the charity or the approved body. *2*

Relief

PAYE individual

The relief is given on a 'grossed-up' basis to the eligible charity or approved body, rather than by way of a tax credit to the donor. This in effect means that the charity is treated as having received a donation net of income tax. ½

Example

Individual donates €500

(A) Individual on standard rate of income tax i.e. 20%

Charity receives €500 from the individual and claims €125 from the Revenue at the end of the tax year. ½

(B) Individual on higher rate of tax i.e. 42%

Charity receives €500 from the individual and claims €362 from the Revenue at the end of the tax year.

The PAYE individual must complete an 'Appropriate Certificate' - CHY 2 and forward it to the eligible charity or approved body so they may claim the amount of tax on the grossed up donation. ½

(4)

(30)

Question 3

(a) For VAT purposes, a taxable person is a person (otherwise as an employee of another person) who is making supplies, within the State, of taxable goods or services, in the course or furtherance of business, and who is (or who should be) registered for VAT.

Persons must register if their turnover of taxable items exceeds a prescribed threshold and might register voluntarily even if turnover is below the threshold. The term "person" can refer to an individual, partnership or company, as well as any other body which supplies goods or services in the course of business. *(3)*

(b) Registration is compulsory when taxable turnover exceeds or is likely to exceed the applicable registration threshold in any 12 month period;

- Persons supplying services - €25,500
- Persons supplying goods - €51,000
- Persons making intra-community acquisitions - €41,000
- Persons making mail order or distance sales into Ireland - €35,000
- Traders with no establishment in Ireland – no threshold – must register. *2*

Some persons may choose to register voluntarily so as to recover input tax. This is likely to be the case if the person concerned pays substantial amounts of input tax and believes that charging output tax to customers would not trigger a loss of custom. It may be that the person supplies only zero-rated items or makes supplies wholly or mainly to customers are also VAT-registered (and can therefore recover any VAT charged to them). *3*

Another (less compelling) reason to register voluntarily is to give the impression of an established business.

(5)

(c) A person who joins the cash accounting scheme accounts for output tax in the tax period in which payment is received from the customer and reclaims input tax in the tax period in which payment is made to the supplier. This allows the person to delay the payment of output tax to the Revenue Commissioners until the tax has actually been received from customers, which is beneficial if customers are given extended credit. The scheme also provides automatic relief for bad debts. On the other hand, input tax cannot be reclaimed until that tax has actually been paid to suppliers. *2*

A registered person may not join the cash accounting scheme unless at least 90% of their turnover is derived from supplies to non-taxable persons, or the value of their turnover is less than €635,000. *1*

A person wishing to account for VAT on a cash receipts from the sale of goods must notify the Revenue of the following;

- The nature of his business
- The percentage turnover derived from supplies to unregistered persons in the previous 12 months (or since trading commenced) and the estimated percentage for the next 12 months
- The amount of his debtors prior to election

The cash receipt basis is not allowed in respect of sales of goods and services between connected persons. *1*

(4)

(d) The Revenue may cancel any person's authorisation to account for VAT on a cash basis, either at the request of the taxable person, or because he no longer qualifies, i.e. less than 90% of his supplies are to non taxable persons. *1*

The authorisation may be withdrawn if, on a review of a period of six months or more, an Inspector of Taxes is satisfied that the moneys received basis is yielding less than 80% of the tax which would apply if no authorisation had been granted. *1*

(2)

(e) Sanjay's cumulative taxable turnover for the 12 months to date, ignoring sales of fixed assets, is as follows:

2005	**€**	**2006**	**€**
February	1,450	January	54,440
March	4,010	February	59,910
April	6,790	March	63,130
May	9,930	April	65,450
June	13,590	May	67,200
July	17,780		
August	22,110		
September	27,330		
October	33,640		
November	40,590		
December	47,760		

4

Traders whose turnover in any 12 month period is likely to exceed the relevant threshold limit must register for VAT. For Sanjay the relevant threshold limit is €51,000.

The registration threshold is passed in January 2006. Sanjay should register within 30 days of the date it becomes likely he will exceed the threshold which in this case is December 2005.

Technically, there is no basis for the Irish Revenue to allow someone not to register even if the turnover was in decline for the remainder of 2006. *4*

(8)

(f) Once registered a trade may be de-registered:

- If he or she ceases to be a taxable person
- He or she falls below the relevant registration threshold, ceases to trade or
- If he or she was registered in error. *(3)*

(g) The cash accounting scheme gives automatic relief is given for bad debts. But persons who are not members of this scheme might account to the Revenue for the output tax relating to a supply and then find that a bad debt occurs. *1 ½*

Bad debts are subject to agreement with the Inspector of Taxes but there does not appear to be any reason why a trader should seek advance approval from his Inspector of Taxes before claiming a VAT deduction for bad debts. Once the debt is recognized to be bad, the trader may deduct the amount from his liable turnover in the period the debt becomes bad. *1*

There is one situation where VAT relief in respect of bad debts is not available. This is where the bad debt is in respect of VAT arising on the grant of a long term lease (10 years or greater (of immovable goods). *½*

(3)

(h) The VAT consequences of offering discounts to customers are as follows:

(i) If a trade discount is given, output tax is based upon the price charged to the customer after this discount has been deducted. However, the person who issued the invoice should issue a credit note. This note should state the amount of the reduction in the price and the appropriate VAT. The supplier may then reduce, by the amount credited, his or her liability for the accounting period in which the credit note is issued, and the recipient must increase his or her liability by the same amount. All credit notes must contain a reference to the corresponding invoice *1*

(ii) If a cash discount is offered for prompt payment, output tax is based upon the price that would be charged to the customer if the maximum available cash discount were deducted. This is the case whether or not the customer actually takes advantage of the cash discount. Again, a credit note must be issued to the customer. *1*

(2)

(30)

Question 4

(a) Although trading profits and chargeable gains are both assessed to corporation tax, it is important to distinguish between them because:

- the rules of computation are different (in particular, the rules on allowable deductions differ and chargeable gains attract indexation allowance). *2*
- trading losses may be set against total profits (for a limited period) or carried forward and set against future trading profits, whilst a capital loss may only be set against chargeable gains of the same period or future periods. *2*

The badges of trade are:

- the subject matter of the transaction
- the length of the period of ownership
- the frequency of transactions
- supplementary work
- the reason for the sale
- motive for acquiring the asset.

½ mark for each plus further 1 mark for explanation up to a maximum of 9

(13)

(b) *Correction of market failure*
- public goods *2*
- merit/demerit goods *2*
- externalities *2*
- monopoly *1*

Redistribution of wealth
- the need for redistribution *1*
- the role of taxation *1*

Stabilisation of the economy
- the use of taxation as a tool for managing the economy. *1*

(10)

(c) User charges:

- explanation of the concept of a user charge *1*
- examples of user charges *1*
- advantages:
  - equity (charges reflect value of benefit received)
  - rationing device
  - users more likely to economise their use of goods/services
  - enhanced public accountability *3*
- disadvantages:
  - difficulty in collecting user charges for public goods
  - "free rider" problem
  - regressive nature of user charges. *2*

(7)

(30)