IIPA

# Advanced Taxation
# Module 9

# June 2011

# Suggested Solutions

**Solution 1**

a)
Value of asset transferred – liabilities taken over – cash = shares

€1,946,000 - €32,000 - €62,000 = €1,852,000 **2 marks**

**Gain**

| | | | |
|---|---|---|---|
| Goodwill | €350,000 | | **1 mark** |
| Premises | | | |
| Market Value | | €1,500,000 | |
| Cost | | | |
| €300,000 x 1.212 | | (€363,600) | |
| | | €1,136,400 | **2 marks** |
| Total Gains | | €1,486,400 | |

Deferred Gain

$$€1,486,400 \times \frac{€1,852,000}{€1,946,000} = €1,414,600$$ **2 marks**

| | | |
|---|---|---|
| Taxable Gain | | |
| €1,486,400 - €1,414,600 = | €71,800 | **1 mark** |
| Less: Annual exemption | € 1,270 | |
| | €70,530 | |

Capital Gains Tax €70,530 x 25% = €17,633 **1 mark**

b)
Base cost of shares for future disposal

| | | |
|---|---|---|
| Value of shares | €1,852,000 | **2 marks** |
| Less: deferred gain | (€1,414,600) | **2 marks** |
| | € 437,400 | |

c)
If Joe holds on to the premises in his own name he can avoid the future double tax exposure by having the premises in a company. He can also protect the premises from future creditor claims against the company. **2 marks**

The disadvantage is that he cannot claim deferral of CGT if he holds on to the premises. In order to claim relief Joe would need to transfer all assets of business except cash to new company in exchange for shares and possibly some other consideration. **1 mark**

**Solution 2**

a)
Members of Loss Group
A, B, C (as A Ltd owns 79% B Ltd and indirectly A Ltd owns 83.7% (Ltd).

| | A Ltd | B Ltd | C Ltd |
|---|---|---|---|
| | Y/E 31/12/09 | Y/E 31/10/09 | Y/E 31/12/09 |
| Sch D Case 1 | €100,000 | - | €78,000 |
| Sch D Case V | € 22,000 | €14,000 | €15,000 |

| | A Ltd | B Ltd | C Ltd |
|---|---|---|---|
| Sch D Case 1 | €100,000 | | €78,000 |
| Less: Loss from B | | | |
| €100,000 x $^{10}/12$ | (83,333) **1 Mark** | | |
| €78,000 x $^{10}/12$ | | | (65,000) **1 Mark** |
| | €16,667 | | €13,000 |
| Sch D Case V | €22,000 | €14,000 | €15,000 |
| | €38,667 | €14,000 | €28,000 |
| | ===== | ===== | ====== |
| Corporation Tax | | | |
| €16,667 x 12½% = | €2,083 | | |
| €22,000 x 25% = | €5,500 | | |
| €14,000 x 25% = | | 3,500 | |
| €13,000 x 12½% = | | | €1,625 |
| €15,000 x 25% = | | | €3,750 |
| | €7,583 | €3,500 | €5,375 |
| Less: Loss Relief | | | |
| Value Basis | | | |
| €5500 x $^{10}/12$ | (€4,583) **2 marks** | | |
| €3750 x $^{10}/12$ | | (€3,500) **2 marks** | (€3,125) **2 marks** |
| CT Due | €3,000 | - | €2,250 |

B Ltd

| | | |
|---|---|---|
| Sch D Case 1 Loss | €272,000 | |
| Used in B Ltd Case 1 | - | |
| Used in B Ltd Value Basis | (28,000) | |
| Used in A Ltd Case 1 | (83,333) | |
| Used in C Ltd Case 1 | (65,000) | |
| Used in A Ltd Value Basis €4,583 ÷ 12½% | (36,664) | |
| Used in C Ltd value basis €3,125 ÷ 12½% | (25,000) | |
| Available to carry forward against future Sch D Case 1 Profits B Ltd (Same trade) | (€34,003) | **2 marks** |

b)
Gain avoided due to capital Gains Group.

| | | |
|---|---|---|
| Market Value | €170,000 | |
| Cost €55,000 x 1.144 | (62,920) | **2 marks** |
| Gain | €107,080 | **2 marks** |

€107,080 x 25% = €21,416

Implication of A Ltd selling B Ltd

B Ltd will be liable to pay tax on the gain A Ltd avoided due to Group relief. This is because B Ltd is leaving the group within 10 years of the asset transfer. The purchaser of B Ltd will adjust the purchase price to take account of this latent gain. **4 marks**

A Ltd might also have a liability regarding the gain it will have on selling its shares in B Ltd.

| | |
|---|---|
| Sales proceeds | €500,000 |
| Cost | (€220,000) |
| Gain | 280,000 |

€280,000 x 25% = €70,000
**2 marks**

**Solution 3**

Any three disadvantages:

(1) Benefits to participants

Where a close company provides a benefit to a participator or his associates this is treated as a distribution.

- Net tax deductable in CT computation
- Company must withhold dividend withholding tax
- Individual Sch F income

(2) Interest payments to Director /Associates

If interest is paid to director with a material interest (owns >5%) excess interest is distribution.

Interest limit allowed lower of 13% x (total cost from directors with material interest)

or

13% x (material value of issued share capital and share premium)

Excess interest distribution

Disallowed in CT computation

- company must deduct dividend withholding tax
- individual Sch F income.

(3) Loans to participants

Where a close company makes a loan to a participator or associate of participator

- company must regross loan and pay income tax to Revenue
- If individual repays loan, company get refund income tax from Revenue.
- If loan never repaid individual taxed on gross amount and income tax not refunded.

(4) Surcharge on undistributed estate or investment income

After tax estate or investment income of a close company. If it is not distributed within 18 months of the end of the year, surcharge 20%.

**Any three 6 marks each, 2 marks presentation**

**Solution 4**

Joe 10/1/10

| | | |
|---|---|---|
| Sales Proceeds | €18,000 | |
| Cost | | |
| €5,000 x 1.087 | (5,435) | |
| Gain | €12,565 | **2 marks** |

Lola

€18,000 taxable Gift less €3,000 exemption from any disposal
⇨ €15,000 Gift
Under Group A threshold no CAT **1 mark**

Joe 15/3/10

| | | |
|---|---|---|
| Sales Proceeds | €120,000 | |
| Cost | | |
| €60,000 | (60,000) | |
| Gain | €60,000 x 25% = €15,000 | |
| | | **2 marks** |

Bob

| | | |
|---|---|---|
| Gift | €120,000 | |
| Less: Exemption | ( 3,000) | |
| | 117,000 | **2 marks** |
| | ====== | |

| | | |
|---|---|---|
| Taxed | | |
| €20,740 x Nil | | |
| €96,260 x 25% = | €24,065 | |
| Less: CGT / CAT credit | (15,000) | **2 marks** |
| CAT due | 9,065 | |
| | ====== | |

Tim 27/5/10

| | | |
|---|---|---|
| Gift | €170,000 | |
| Less: Exemption | ( 3,000) | |
| | 167,000 | **2 marks** |
| | ====== | |

| | | |
|---|---|---|
| Taxed | | |
| €20,740 x Nil | | |
| €146,260 x 25% = | €36,565 | **2 marks** |

Joe 29/11/10

No CGT and no CAT between spouses **2 marks**

Joe 15/12/10

| | | | |
|---|---|---|---|
| Sales proceeds | | | |
| (90% x 1,200,000) | = | €1,080,000 | |
| Cost | | | |
| €90 x 1.406 | | ( 126) | |
| | | €1,079,874 | **2 marks** |

No CGT as retirement relief.

| | | |
|---|---|---|
| Sam | | |
| Business property relief | | |
| Market value | €1,080,000 | |
| Less: Business relief | ( 972,000) | **2 marks** |
| | 108,000 | |

Under CAT threshold, no CAT

Joe B

| | | | |
|---|---|---|---|
| Total Gains | | € | |
| 10/1/10 | | 12,565 | |
| 15/3/10 | | 60,000 | |
| | | 72,565 | |
| CGT x 25% | = | 18,141 | **1 mark** |

**Solution 5**

| | | |
|---|---|---|
| Bob | | |
| Inheritance | €1,200,000 | |
| | | |
| €414,799 @ Nil | | |
| €785,201 @ 25% | € 196,300 | **2 marks** |
| | | |
| Sally | | |
| Inheritance | € 120,000 | |
| €41,481 @ Nil | | |
| €78,519 @ 25% | € 19,630 | **2 marks** |
| | | |
| Niall | | |
| Inheritance | € 75,000 | |
| Less: Funeral expenses | € ( 10,000) | **1 mark** |
| | € 65,000 | |
| | | |
| €20,740 @ Nil | | |
| €44,260 @ 25% | €11,065 | **2 marks** |
| | | |
| Maeve | | |
| Spouses, exempt from CAT | | **2 marks** |
| | | |
| Mick | | |
| Farm | €762,000 | |
| Les: Agricultural relief | (685,800) | |
| | 76,200 | **1 mark** |
| | | |
| Under Group A threshold, no CAT | | **2 marks** |

Total CAT Liabilities

| | | |
|---|---|---|
| Bob | €196,300 | |
| Sally | € 19,630 | |
| Niamh | € 11,065 | |
| | €226,995 | **2 marks** |
| | ====== | |

S. 60 Policy €82,000

Allocated as follows:

Bob $\frac{€196,300}{€226,995}$ x €82,000 = €70,912 **1 mark**

Sally $\frac{€19,630}{€226,995}$ x €82,000 = €7,091 **1 mark**

| | | |
|---|---|---|
| Niamh | $\frac{€11,065}{€226,995}$ x €82,000 = €3,997 | **1 mark** |

Final CAT liabilities

| | | |
|---|---|---|
| Bob | €196,300 - €70,912 = €125,388 | **1 mark** |
| Sally | €19,630 - €7,091 = € 12,539 | **1 mark** |
| Niamh | €11,065 - €3,997 = € 7,068 | **1 mark** |

**Solution 6**

Limited Company
The advantage of a Limited Company is for a new business there is a corporation tax exemption for the first 3 years. After that the corporation tax rate is 12½% which is much lower than 55% for sole traders.

Any loses in the company can only be used against future profits in the company, thus saving you tax at 12½%.

If you set up a company you could avail of seed capital relief. This is because you are setting up a manufacturing company. This would mean you could invest up to €600,000 and get relief at 41%. You could borrow from the bank to invest and when you get refund you could repay €246,000 of the loan and only have €254,000 loan remaining. Interest relief as a charge will not be available if you claim this option.

Ellen could invest in a business scheme of the company once her shareholding is less than 30%. She could invest up to €150,000 a year and get relief at her marginal rate of income tax. She may need advice on high earners restriction. She will not be allowed interest as a charge for any money borrowed for this investment.

If you were to initially set up as a sole trader you could claim your costs against ones income saving 41%. However you would miss the opportunity to avail of BTD and seed capital relief. It is for this reason I recommend a limited company.

**Any 4 relevant points 5 marks each**