Final Admitting Examination

Chartered Accountants Ireland

PAPER 3 ADVANCED TAXATION NORTHERN IRELAND

SUMMER 2016 (Friday 19th August 2016: 10.00 am – 2.30 pm)

INSTRUCTIONS TO CANDIDATES

1. The first 30 minutes of this examination is dedicated to reading time.

During this time, candidates may make notes on this examination paper or on their own pages and refer to their materials.

Candidates are **NOT** permitted to open their answer books until instructed to do so.

2. Answer **BOTH** Simulations.

3. Candidates should answer the paper in accordance with the law and practice of the United Kingdom and in accordance with the appropriate provisions up to and including the Finance Act 2015.

4. All workings should be shown.

5. **SIMULATION 1** begins on Page 2 overleaf.

SIM 1: THE KELLY FAMILY

(Suggested time: 120 minutes)

You are Ben Shiels, a recently qualified chartered accountant working in the tax department of TML & Co., a medium sized accounting and tax practice. It is 22 August 2016 and Tom McLaughlin, a tax partner, calls you into his office to brief you on new clients, Patsy and Mary Kelly. Tom met with them yesterday and has told them to call back to the office on Wednesday to discuss a number of tax issues raised.

By way of background, Tom tells you that Patsy (62) and Mary (59) Kelly are married with no children. Patsy and Mary are both directors and shareholders in Kelly Contracts Ltd ("KCL"). Patsy owns 75% of KCL and Mary owns the remaining 25%. KCL is a trading company involved in the construction industry. The company prepares its financial statements to 30 November each year.

Mary loaned £ 100,000 to KCL in January 1995 when the company was incorporated. This money has not been paid back to date. With the help of this loan, the company has grown substantially over the years. Patsy has been a full-time working director since incorporation. Mary has always worked part-time with the company taking a gross salary of £ 30,000 per annum, but has never been a director. Due to ill health, Mary needs to cease working for the company immediately. She will retain her shares but would like to get a cash lump sum of £ 140,000 from the company now to fund her medical needs. Tom states that Patsy and Mary would like our advice on how to extract the £ 140,000 for Mary as tax efficiently as possible. Detailed calculations are not required. The company currently has a cash balance in excess of £ 200,000.

Tom also informs you that Patsy would like to retire within the next three to five years. Patsy has had a few offers in the past for the company's trade (as opposed to the shares) but he feels that with the market improving, he might be able to further build up the value of the company's trade. He anticipates that he will be able to sell the company's trade to a competitor company for £ 1,200,000. He has heard that other companies, like KCL, just get liquidated after their trade is sold. He would like a calculation of how much money he and Mary will be left with if this happens and if there are any tax reliefs that may be available to them in the event of liquidation. Tom states that for the purposes of giving Patsy some figures, we are to base our advice on the assumption that KCL's statement of financial position (see **Appendix I**) immediately after the sale of the company's trade shows a value of £ 1,000,000. You are to assume that this value is after all company expenses and taxes have been paid, and that no sale of the shares will occur. You should also assume that all tax rates and reliefs remain unchanged from 2015/16.

Patsy said that as the company is now in a healthy position he has recently increased his salary to £ 100,000 per annum going forward (this shouldn't affect the anticipated future sale price of £ 1,200,000) and he would like to know if he/KCL should undertake any other tax planning before the company's trade is sold. The company has recently set up an occupational pension scheme, but Patsy has never made any contributions to the scheme nor has the company made any contributions on his behalf. Patsy also informs you that a friend has recently started up a small technology start-up company that operates out of the Northern Ireland Science Park in Belfast. It has 10 employees and total assets of £ 150,000. His friend is looking for new investors to come on board and subscribe for shares, and Patsy would be interested to know if he would be entitled to any tax relief in the event that he makes an investment.

Tom finishes the meeting by saying "can you have a briefing note ready for Wednesday's meeting. In addition to the retirement and liquidation planning issues we have talked about, I need you to look at an email I have just sent you (see **Appendix II**) regarding VAT queries which Patsy needs help on. Please include your analysis of the VAT implications on the sale of the two properties in your briefing note for Wednesday's meeting. You don't need to consider any other taxes for now."

APPENDIX I: PROJECTED STATEMENT OF FINANCIAL POSITION IMMEDIATELY AFTER SALE OF KCL'S TRADE:

Assets	**Note**	**£**
Bank	1	1,000,000
Share capital & Reserves		
Issued share capital	2	20,000
Retained earnings		980,000

Note 1 – Proceeds for sale of company trade after **all** company expenses and taxes are paid.
Note 2 – 20,000 shares with a nominal value of £ 1.

APPENDIX II: EMAIL ON VAT QUERIES:

EMAIL
TO: b.shiels@tml.ie
FROM: t.mclaughlin@tml.ie
RE: Kelly Contracts Ltd – VAT

Ben

Please include details of KCL's VAT obligations on the sale of the following properties in your briefing note for Wednesday's meeting:

- A commercial unit near Banbridge town centre is to be sold for £ 400,000 plus VAT (if any). KCL bought the unit in August 2010 when it was brand new for £ 260,000 plus VAT. The unit has always been used in KCL's trade but is no longer considered essential for the trade, hence the proposed sale. Interest in this property has been slow however, the estate agent has informed Patsy that a dentist has viewed this property a couple of times and she intends to move her dental practice to the unit if she buys it. She is however concerned about VAT being charged on the purchase of the property because her business is VAT exempt. Please provide supporting calculations where relevant;
- A pub premises in Portadown is to be sold for £ 250,000 plus VAT (if any). KCL completed the development of this property in March 2015 and has now identified a willing purchaser.

You should assume that any property sales will take place on 30 June 2017.

Thanks

Tom

END OF SIM 1

SIM 2: PETER MCGOWAN

(Suggested time: 120 minutes)

You are Joyce O' Connor, a tax senior at Carmody Tax Partners, a medium sized firm based in Newry. You and Garrett Carmody, the firm's tax partner, have just come out of a meeting with Peter McGowan, a new client of the practice. Peter is looking for some taxation advice on a number of issues and Garrett has asked you to prepare a briefing memo for him regarding the same. You can assume today's date is 1 February 2016.

Peter McGowan who is currently UK resident and domiciled owns 100% of Ice ("ICE") Limited, a company engaged primarily in the research and development of new technologies for smart phones and devices. Peter also owns 100% of Polar ("POLAR") Limited, a company engaged in the development and manufacture of "smart" devices. Both companies are UK resident and have a 31 March year end. The two companies have never formed a group, and Peter wonders whether this is something that would be beneficial for tax purposes. The company's financial controller has estimated that POLAR will have current year adjusted trading profits in line with previous years. ICE has substantial trading losses forward as well as substantial estimated current year trading losses. Both ICE and POLAR are medium sized enterprises under the EC definition. As ICE is loss making Peter feels that there is little benefit in the company making an R&D tax claim.

The first issue on the agenda at today's meeting was that an investment company has recently approached Peter and is interested in acquiring POLAR's head office in Newry. POLAR acquired this office in the 1980s and should the sale go ahead it is likely to generate a substantial gain for the company.

In the meeting Peter said "I am delighted about the prospect of this sale as a significant gain should be generated. The sale is not likely to happen for at least another 9 to 12 months (i.e. in the accounting period ending 31 March 2017) which gives us plenty time to find a new head office, however a significant capital gain is likely to arise on the sale. As time is on our side I want you to consider ways the resulting corporation tax liability could be minimised. In particular, is there any pre-sale structuring that you could recommend?"

Peter then goes on to tell us about ICE's R&D activities. He explained to us that neither he nor the company's financial controller know much about R&D tax relief but he is confident that ICE does undertake qualifying R&D activity. Due to the losses historically made by ICE, Peter confirmed that no R&D tax claim has ever been filed by the company because in Peter's words, "making a claim would only increase the trading loss being carried forward, so it doesn't seem worthwhile at the moment."

Peter informs you and Garrett that they are looking at ways to make ICE profitable again. ICE is looking to expand its operations into Ireland over the next few years. During the year ending 31 March 2017 ICE intends to acquire a warehouse in Dublin for storage and display purposes only. All key decisions regarding the Irish operations will continue to be made by the head office in Northern Ireland. From 6 April 2017 onwards Peter intends to split his time between Northern Ireland and Ireland. Peter intends to keep his family home in Newry and his wife and children will remain in Newry during this period. In the year ending 31 March 2018, while in Ireland he will be negotiating contracts on behalf of ICE. Peter anticipates that he will spend 18 days out of every month in Ireland, and he will stay in hotels in Dublin during his time in Ireland.

Peter is interested in finding the taxation implications for ICE regarding its Irish operations in particular for the years ending 31 March 2017 and 2018. Peter also states "I have done some research of my own and in the tax year ending 5 April 2018 I think I could be Irish resident as well as being UK resident. Could this be possible? I would also like your advice in this regard as I do not want any unexpected surprises from the Irish Revenue Commissioners."

Finally Peter ends the meeting by saying that his wife Avril is also looking for tax advice. Avril is happy for Carmody Partners to bill her separately for this advice. She is an architect and currently runs this business as a sole trader. Due to the upturn in the economy the business is doing well and last year alone tax adjusted profits of £ 120,000 were generated. She only takes drawings of approximately £ 50,000 each year and the excess is placed in a deposit account which earns interest. She has heard that incorporating is beneficial from a tax perspective but she is keen to understand more about how she can achieve this and whether any tax reliefs are available. Goodwill associated with the business has been valued at £ 50,000. The business' balance sheet contains no stock or fixed assets. Avril will be a 100% shareholder in this newly formed company.

Garrett has asked you to prepare a briefing memo on the taxation issues that have arisen from the above meeting.

END OF SIM 2

END OF PAPER