

### Introduction

Happily, most tax practitioners have adapted their procedures to meet the requirements of Self Assessment and this has contributed greatly to the success of Self Assessment. However, there are still some areas of difficulty.

In this issue of Tax Briefing, we revisit some of the items that give rise to most problems. We do so with a view to encouraging those practitioners, who find it takes several supplementary submission before getting a correct assessment, to take a fresh look at their procedures. We urge them to adapt those procedures as necessary.

What is required under Self Assessment, is one comprehensive submission each year in which the Tax Return form, accounts, schedules and all other relevant items - including all claims for allowances and reliefs - are submitted together.

We recently came across a case in which an assessment was amended eight times before the correct liability was established. On examination, we found that each amendment arose because of some omission or error in the Returns submitted. This is, thankfully, an extreme case but there are many cases where, with a little more thought, the assessment could have been right first time.

With the advent of the Current Year basis of assessment from 1990/91, tax practitioners who find that it takes several amendments to an assessment before the correct liability is established should be asking themselves - why?

From now on, a single satisfactorily completed return should finalise each year. The necessity for supplementary submissions will indicate a deficiency in the original return.

On our side, as mentioned in a previous issue, we are committed to ensuring that any errors in processing are minimised and we are continuously looking at procedures accordingly.

### Revenue Arrears

#### Review Programme

The Revenue Commissioners are determined to tackle the problem of non-payment of taxes. When the 1988 Incentive Scheme was announced, it was emphasised that any taxpayers who did not avail of the Amnesty would be pursued vigorously.

After the Amnesty, the first phase in the pursuit of those taxpayers who had outstanding tax liabilities was the setting up of an Arrears Identification Programme. This was a coordinated approach, between the Inspector of Taxes and Collector-General staff, to establish a new pragmatic approach and revised procedures for dealing with the outstanding taxes. This programme has been in operation since My 1989 and has been highly successful to date. For example, some £66 million has been collected without recourse to enforcement.

Now, an Arrears Review Programme, which will build on the success of the initial phase, has recently been launched to extend and expand the arrears control function.

#### What Cases are chosen?

Cases are chosen based on the liabilities outstanding under any one taxhead - i.e. C.T., I.T., VAT or PAYE (Employers) - commencing with the largest amount and working downwards. Once a case is identified all taxheads are then dealt with by the one Inspector. Cases that have open appeals on record are dealt with separately.

#### How the Programme Works

Once the Inspector identified the total arrears position on record, he then fully researches the case by reference to existing information on file to verify the outstanding liabilities and to prepare his/her brief for the follow up action. The taxpayer and agent are approached, as appropriate, with details of the liability, initially by letter and subsequently by telephone, or, where necessary, by personal visit.

The case will not be dropped until payment is received, either voluntarily or as a result of enforcement action, as necessary. Payment must include tax, interest and costs (where enforcement action has already been initiated). **Where payment of verified tax is not forthcoming, the Inspector will immediately refer a case to his/her colleague in the Collector-General's Office with a recommendation that a particular avenue of enforcement be pursued.** The case will be pursued from that point by Collector-General staff.

Inspectors and Collector-General staff engaged on this programme are in continuous contact and work closely to ensure that there are no delays in finalising cases.

The enforcement measures currently being pursued are : judgement, judgement mortgage, sheriff, attachment, bankruptcy, liquidation and receivership.

## **Tax Practitioners' Role**

The cooperation of tax practitioners to date has played a significant part in the success of the programme for dealing with tax arrears. Your continued support will ensure that the next phase will be equally successful and that the arrears position will be speedily concluded. We would particularly appreciate if practitioners with clients who have not paid outstanding tax liabilities would advise them of the consequences of non-payment, as outlined above. In specific cases, practitioners will no doubt advise the Inspector of any allowances and reliefs due that may have been omitted from the original return. In a number of cases, accounts may have to be prepared for outstanding years and equitable liability computed on these. In these cases, long delays will not be permitted and enforcement procedures will continue, where appropriate. Where equitable liability is being claimed, full and immediate payments is expected.

## **1. General**

**The Finance Act 1991 became law on 29 May 1991.**

### **1.1 Estimated Figures on Tax Returns**

It has been noticed that some Tax Returns (both Income Tax and Corporation Tax) are being submitted with estimated figures included (some estimates bear little relationship to the ultimate figures). In some cases the figures are stated to be estimates while in others this only becomes clear when the correct figure is subsequently substituted.

Tax practitioners should note that a Return form in either categories not a valid Return of Income for tax purposes. It does not avoid a surcharge being incurred in such cases.

In the past these Tax Returns were a generally processed as received. In future, Tax Returns with figures stated to be estimates will be sent back for correct completion. If satisfactory returns are not received fully completed on or before the return filing date, the surcharge will be applied. In the case of Returns where figures are not stated to be estimated but are discovered to be estimated, the surcharge will also be applicable, when the correct figures are subsequently obtained.

### **1.2 Appeals**

Where, in an appeal case which is going to counsel is briefed on behalf of a taxpayer, practitioners are requested to make the Inspector of Taxes aware of this at the earliest possible date. This will contribute to the earliest possible date. This will contribute to the earlier resolution of the issue by reducing the possibility of adjournments.

Is Tax Briefing circulated to all you staff? We get queries which suggest that Tax Briefing is not always circulated to staff within firms. Unless all tax staff are aware of the contents, practitioners are not likely to be getting full value from this Revenue Service.

If you change address, be sure to advise us to that we can keep our Mailing List up to date.

## **2. Income Tax**

### **2.1 Preliminary Tax 1991/92**

The due date for 199/92 Preliminary Tax is 1 November 1991.

Practitioners who wish to base clients' 1991/92 Preliminary Tax payments on their 1990/91 final tax liabilities (the 100% rule) should note that 1990/91 Tax Returns which are not submitted prior to mid-September 1991, are unlikely to be processed in time for notices of assessments for 1990/91 to be issued before the 1991/92 Preliminary Tax due date of 1 November 1991.

As mentioned in previous issues, early submission of 1990/91 Tax Returns is recommended accordingly.

### **2.2 Tax Returns 1990/91 - Problem Areas**

- i) We would ask practitioners to remind their staff of the guidelines on completion of Returns contained in the first issue of Tax Briefing. Tax Districts are reporting that Tax Returns 1990/91 received to date are not always completed as required, despite the previous request for greater care.
- ii) Some practitioners continue to send the following items to Tax Offices without the Tax Return: Accounts, forms P60, forms F45, RICT forms, Retirement Annuity Certificates, Deed of Covenant & forms R185. The submission of material in piecemeal fashion serves not useful purpose. Under Self Assessment what is required is one comprehensive submission each year in which the Tax Return form, accounts, schedules and all other relevant items - including all claims for allowances and reliefs - are submitted together.

There is no benefit to be obtained from the submission of items without a Tax Return. It simply creates unnecessary work for practitioners and for Tax Offices.

- iii) We are advised that some tax practitioners are sending in Tax Returns without entering the Case I/Case II profit figure for the "Corresponding Period". In such cases the Returns will be processed as submitted with no averaging adjustment being made. This could result in clients paying too much tax. It may also result in clients being selected for manual examination of the profits of the drop-out year and the bases period for 1990/91.

iv) In the case of farmers on “income averaging” we would remind practitioners that the profits of the “Corresponding Period” are the average profits of the three years ending on the date 12 months immediately before the end of the basis period for the year 1990/91 (see example overleaf).

### Example

Profits for	y/e 31/12/90	- £25,000
	y/e 31/12/89	- £20,000
	y/e 31/12/88	- £12,000
	y/e 31/12/87	- £ 8,000
	y/e 31/12/86	- £ 7,000

Average Profits for 1990/91 - £19,000

$(25,000 + £20,000 + £12,000) \times 1/3$

Average profits for “Corresponding Period”

$(20,000 + 12,000 + 8,000) \times 1/3$  - £13,333

[the average profits for 1989/90 - 9,000 - do not come into the reckoning.]

The “transitional averaging” provision is applied to the above average profit figures to establish the amount of the assessment for 1990/91 i.e.  $(13,000 + 19,000) \times 1/2 = 16,166$ . However the application of the “125% Rule” in this example, gives an assessable profit for 1990/91 of 16,666 (i.e.  $13,333 \times 125\%$ ).

## 2.3 Pension Scheme for Doctors in the General Medical Service - Tax Treatment of Contributions.

Under Section 12 of Finance Act 1991 the Revenue Commissioners are authorised to approve the Pension Scheme for general practitioners within the GMS, who have accepted the common contract, as if it were an employer/employee type Pension Scheme. Although the scheme has not yet been formally approved by Retirement Benefits District, it is possible to outline the principal features of the scheme as they affect practitioners preparing tax submissions.

- Contributions to the scheme will be 15% of fee income viz. 10% contributed by Health Boards. 5% contributed by General Practitioners (GP)
- The contribution by the Health Board will not be regarded as part of the GP’s Income.
- The GP’s income under the common contract is treated for the purposes of retirement annuity relief (but not for assessment purposes) as derived from a pensionable office or employment. Retirement Annuity Relief will not be available against this part of a doctor’s income.

- Retirement annuity relief will continue to be available against a GP’s private practice income, subject to the existing limits.
- The income from the GMS (common contract) and the income from private practice will be arrived at by apportionment of the Case II income by reference to gross fees.
- Professional services withholding tax will apply to the doctor’s contributions (5%), but not to the Health Board contribution (10%).
- The approval of the scheme as an employer/employee scheme will be retrospective to the date on which the Doctor came within the common contract.

The Common contract became available to GP’s from 1/1/1989. If the application of the above has a material effect on Returns already made, (see example below) tax practitioners should contact the appropriate Tax District.

### Example

Doctor with gross GMS fees of £50,000 (net of 10% Health Board contribution) and with gross private practice fees of £15,000. His overall practice expenses were (say) £25,000, leaving a net income from the practice of £40,000.

Retirement annuity relief for 1989/90 may have been claimed by reference to 15% of 40,000 - £6,000.

which included the 5% contribution to the GMS Scheme of £2,500).

Under the revised procedure, the maximum retirement annuity relief allowable in relation to the private practice is calculated as follows:

$$\text{Net relevant earnings } £40,000 \times \frac{15,000}{50,000} = 12,000$$

$$\text{Retirement Annuity Relief} = 12,000 \times 15\% = 1,800$$

The Contributions in respect of the Pension Scheme for doctors in the GMS do not come into the reckoning. If retirement annuity premiums in excess of £1,800 were paid for 1989/90 any balance above the 15% maximum can be carried forward.

## 3. Corporation Tax

### 3.1 Submission of accounts without form CT1

The Form CT1 is the key documents in the Self Assessment system for companies and it must be submitted for each accounting period of the company.

Corporation Tax Districts report that accounts are still submitted without the relevant form CT1 in a number of cases.

Submission of the company's accounts or any other document without a form CT1 is not sufficient and is not regarded as the making of a return.

If the form CT1 is not submitted within 9 months from the end of the accounting period, surcharge under Section 48 Finance Act 1986 will be imposed, whether or not the accounts for the period have been submitted.

### 3.2 Payment of Corporation Tax

- (i) As advised in issue 1 of Tax Briefing (December 1990), Preliminary tax Payments made by companies for accounting periods ending on or after 1 April 1990 should include Income Tax on payments (S151 CT Act 1976) and surcharge on undistributed income (sections 101 and 162 CT Act 1976). These items are treated as Corporation Tax by virtue of Sections 47 to 49 of the Finance Act 1990.

Preliminary tax payments should be set of Advance Corporation Tax.

Advance Corporation Tax should be paid separately, using form ACT/P, within 6 months from the end of the accounting period (i.e. one month before the due date of payment of Preliminary Tax), The A.C.T. Return, on Form ACT, should be made to the Inspector with the form CT1, within 9 months from the end of the accounting period. Further supplies of forms ACT/P are now available from CT Districts.

- (ii) Companies who avail of the Voluntary Self Assessment facility on the form CT1, by computing their liability to Corporation Tax and including that amount in Panel 22 of the form, should pay only the exact amount calculated to be due. The liability that will be recorded is that shown on the VSA calculation. Rounding up or down of the figure for payment purposes should be avoided as this creates small overpayments or underpayments which give rise to unnecessary administrative work.

### 3.3 New Companies

Some new companies have been issued with forms CT1 or Preliminary Tax letters within a short period from their commencing to trade. We regret this inconvenience but are happy to advise that a computer development, due to be in operation before the end of the summer, will ensure that forms CT1, Preliminary Tax letters etc. will not in future issue to new companies in their first year of trading.

### 3.4 Agreement of Returns

Returns are being submitted to Corporation Tax Districts under covering letters which in one way or another request agreement of the submissions made. The requesting of agreement in such circumstances is contrary to the basic principle of a Self Assessment system - which is that the company Return is accepted as submitted. Such requests for

agreement are not accordingly being responded to by Districts.

While the notice of assessment issues in accordance with the return submitted, the Inspector does of course have authority, under Section 15 of the Finance Act 1988, to make enquiries and amended assessments, as appropriate.

### 3.5 Surcharge S.48 Finance Act 1986

Where a form CT1 has not been submitted within 9 months from the end of the accounting period, the Preliminary Tax contained in the notice given by the Inspector, increased by 10%, becomes payable immediately if it is greater than the amount paid by the company.

The issue of demands for the Preliminary Tax charge, plus surcharge, has given rise to several telephone calls to C.T. Districts. If the Preliminary Tax is excessive, the only way it can be altered is by submission of the form CT1 - a surcharge cannot of course be avoided at that stage.

### 3.6 Interest on Overpayments

Practitioners are reminded that:

- 1) interest is not payable on an overpayment of Preliminary Tax where it (the interest) amounts to less than £10 (Section 12(7) proviso (a) Finance Act 1988).
- 2) Interest is not payable on repayments of DIRT or Withholding Tax (professional services).
- 3) The rate of interest payable by Revenue on tax overpaid is 0.6% per month or part of a month, with effect from 1 August 1990

### 3.7 Losses Forward - S.16(1) C.T. Act 1976

Relief for losses forward under Section 16(1) may be claimed against relevant trading income of the accounting period only. The losses may not be set against other income of the accounting period.

## 4. Capital Gains Tax

### 4.1 Self Assessment

The Finance Act 1991 is now law and the scheme of Self Assessment for Capital Gains Tax, as outlined in the last issue of Tax Briefing is now in force.

It applies to all taxpayers - including taxpayers who pay income tax under PAYE

## 4.2 Preliminary Tax - Capital Gains Tax - 1990/91

Taxpayers on Revenue records who receive Notices of Preliminary Tax - Income Tax for 1991/92, will also receive a Preliminary Tax - Capital Gains Tax Payslip for 1990/91.

Other taxpayers/practitioners can obtain these payslips from any Tax Office.

Because chargeable gains are generally made intermittently, Notices of preliminary Tax - Capital Gains Tax will not be issued by Inspectors of Taxes. Taxpayers must specify and pay their own Preliminary Tax liability - the payslips are to be used for this purpose.

## 4.3 Making Returns of Chargeable Gains

For taxpayers who make a Tax Return (form 11, 12 AG12 etc.) details of the chargeable gains should be included in the sections provided in these forms.

A separate Capital Gains Tax Return (form CG1) is also available from any Tax Office. This form is for use by persons who have a Capital Gains Tax liability in a year but

- do not have an income tax liability.
- Have been advised by their Inspector of Taxes that they need not make a Return for income tax purposes.

The form CG1 is also the forms that companies, which have a capital gains tax liability from disposals of land with development value or from shares deriving their value from such land, must use.

## 4.4 Companies Capital Gains Tax - Development Land

Companies are chargeable to Capital Gains Tax rather than Corporation Tax in respect of chargeable gains arising from disposals of land with development value or shares deriving their value from such land.

Companies with such chargeable gains in 1990/91 must accordingly pay Preliminary Tax - Capital Gains Tax on or before 1 November 1991 and file a return of those chargeable gains on or before 31 January 1992 on form CG1 - pending the redesign of Form CT 1, panel 30 thereon need not be completed.

The explanatory booklet entitled "Notes on Capital Gains Tax", revised to highlight the new Self Assessment system for Capital Gains Tax, will be available from Tax Offices shortly.

## Capital Gains Tax

### MULTIPLIERS - 1991/92 Disposals

#### Disposals in 1991/92

1974/75	5.355
1975/76	4.326
1976/77	3.726
1977/78	3.194
1978/79	2.951
1979/80	2.663
1980/81	2.305
1981/82	1.905
1982/83	1.603
1983/84	1.425
1984/85	1.294
1985/86	1.218
1986/87	1.165
1987/88	1.126
1988/89	1.105
1989/90	1.070
1990/91	1.026

## 5. Capital Taxes

### 5.1 Stamp Duty

#### a) Finance Act 1991 changes

The Finance Act 1991 provides for a fundamental overhaul of stamp duty law in addition to providing for the reimposition of a levy on banks, as in previous years, and certain other relieving and charging provisions.

Sections 94-109 form an interlinked package of provisions designed to put stamp duties on a compulsory footing and to implement collection and enforcement procedures similar to those operating in all other taxes. Essentially, these provisions have two main aims:

- (1) To create a tax regime which actively and effectively discourages evasion of duty.
- (2) To revise penalty provisions for, in most cases, the firm time in one hundred years.

Sections 94, 96-103 and 105-109 will not come into force until 1 November 1991 and will not apply retrospectively. This will allow the Revenue Commissioners to publicise the changes widely before they come into effect.

Two other sections contained in the package come into effect from the date of the passing of the Act.

**Section 95** enables the Minister for Finance to make orders to vary the rate of duty payable on certain instruments. It is the intention that the Minister will make orders before 1

November 1991 relieving certain instruments used in the financial services industry from stamp duty.

**Section 104** deals with instruments where it is not possible to ascertain the amount or value of the consideration or the average annual rent. The duty will now be payable on the value of the property conveyed or transferred, or, in the case of a lease, on the consideration other than rent which could be obtained from a tenant leasing the property for full consideration.

Of the eight sections not contained in the package outlined above, four merit special mention:

**Section 89** implements the Budget proposal to impose a levy of £36 million on the banks.

**Section 93** exempts from stamp duty the issuing and transfer of licences and leases issued by the Minister for Energy in respect of oil exploration.

**Section 110** exempts from companies capital duty investment companies to which the provisions of Part XIII of the Companies Act 1990, relate. These are essentially a new form of managed fund, with variable capital.

**Section 111** exempts from the levy on certain premiums of insurance (Section 92, Finance Act 1982) investments made by one unit linked fund in another. The aim is to avoid a double charge to tax.

A Statement of practice (SP-SD/1/91) detailing the provisions relating to the new stamp duty collection and enforcement regime in the Finance Act 1991, will be available on request from the Stamp Duty Offices from mid-July 1991. Phone 6792777 Exts. 2254 & 2256.

#### **b) Stamping Office - Cork**

Address: Government Buildings,  
Sullivan's Quay,  
Cork.  
Telephone No. (021) 968010.

Opening hours: 9.15 am to 1.00pm and 2.00pm to 5.30pm

The Stamping Office in Cork is not providing a comprehensive range of stamping services, including the stamping of counterparts, collaterals and penalties, and the issuing of refunds. The range of services will be augmented in Autumn 1991 when the office will provide an adjudication service for instruments.

#### **c) Levies**

Payments in respect of the levy on collective Investment Undertakings (Section 109, Finance Act 1990) and the levy on Certain Premiums of Insurance (Section 92, Finance Act 1982

as amended) for the quarter ending 30 June 1991 are due on or before 30 July 1991.

Payments in respect of the levy on Certain Statements of Interest (Section 94, Finance Act 1986) for the period ending 31 July 1991, are due on or before 30 August 1991.

Payments in respect of the levy on Banks (Section 89, Finance Act 1991) for the year 1990 are due on or before 12 September 1991.

## **5.2 Capital Acquisitions Tax**

Tax Amnesty - Capital Acquisitions Tax and Estate Duty:

### **Response**

The amnesty in respect of interest and penalties for outstanding Capital Acquisitions Tax and Estate Duty, which was announced by the Minister for Finance in his Budget Speech on 30 January, 1991, has been confirmed by legislation enacted in this year's Finance Act.

To date the response to the amnesty has been encouraging. More than £2.5 million has been collected on foot of amnesty payments. Enquiries about the scheme continue to run at a very high level, averaging one hundred per week, with up to thirty taxpayers per week actually availing of the scheme.

Essentially, the taxpayer in arrears with Capital Acquisitions Tax would seem to be taking account of the fact that at the rate of 1.25% per month, interest on overdue tax can rapidly accumulate to a sizeable amount. It appears that the amnesty is prompting such taxpayers to raise finance with a view to settling their tax liabilities in the short term. Indeed, certain taxpayers have almost halved their bills by availing of the amnesty.

### **Enforcement**

There is little doubt that the announcement of new and more vigorous enforcement powers in respect of Capital Acquisitions Tax has also acted as a spur to taxpayers in arrears. The collection of outstanding tax will now be underpinned by additional enforcement powers. When the amnesty deadline expires on 30 September, 1991, the Revenue Commissioners will be in a position to pursue any remaining hard-core defaulters using:

- (1) Power of attachment - which obliges financial institutions and debtors to pay direct to the Revenue Commissioners sums owed to the defaulter.
- (2) Warrants issued to the Sheriff - who is then empowered to seize the defaulters goods.
- (3) The Court judgement procedure - which can result in the publication of judgement and the placing of a charge on the defaulters house or land.

Given that the amnesty is due to expire on 30 September 1991, the Revenue Commissioners again urge any taxpayer having a liability to the taxes in question to act immediately and join the significant numbers already taking advantage of this once-off opportunity. To this end, officers of the Capital Taxes Branch, Dublin Castle will be happy to give advice and deal with any enquiries.

Freephone 1800 437437

### **Amnesty - Key Points**

The amnesty applies to gifts/inheritances taken before 30 January 1991, and to Estate Duty.

If outstanding tax is paid before 30 September 1991, interest will be waived (except for interest accrued between 30 April 1991, and the date of payment).

A completed self assessment return, together with a cheque for the amount outstanding, should be sent to the Capital Acquisitions Tax Section, Capital Taxes Branch, Dublin Castle, Dublin 2.

The taxpayer should apply for a waiver of interest under the scheme.

## **6. VAT**

### **6.1 Automated Entry Processing (AEP)**

Following the introduction of AEP on 1 April 1991, certification by Customs officers of the Single Administrative Document (SAD) for VAT purposes has ceased.

A Statement of Practice (SP-VAT/2/91) relating to the new arrangements is available on request from VAT Branch, Castle House, Sth. Great George's St., Dublin 2 - Phone 6792777 Exts. 2440-2443 - or from any VAT office. It outlines the documentation now required (1) by an importer to claim a deduction of VAT paid at importation and (2) to verify exportations.

### **6.2 Jockeys**

With effect from 30 May 1991, the VAT on services supplied in the course of their profession by jockeys is reduced to 12.5%.

## **7. Collector-General**

### **7.1 Delays in paying PAYE/PRSI and VAT**

Where taxpayers fail to lodge their P30 return by the 14th of the relevant income tax month, or their VAT3 return by 19th of the month following the relevant taxable period, the Collector-General estimates the amount due and notifies the taxpayer. In the absence of payment, or a return showing "Nil" (if no payment is due), or a claim for repayment in the case of VAT, enforcement of the estimated amount is pursued very rapidly.

This involves additional costs for the taxpayer as follows:

- i) Cost of enforcement action
  - either Sheriff's poundage and costs or
  - solicitor's costs,
- ii) Possible adverse commercial implications of
  - the issue of warrant to the Sheriff or
  - the publication of a judgement or
  - the issue of a notice of attachment.
- iii) Interest on late payment (at 1.25% per month or part of a month since the due date) which is not allowable as a business expense.

It does not make good commercial sense for a taxpayer to risk incurring these costs by delaying payment. It would be appreciated if practitioners would continue to emphasise this to their clients.

### **7.2 New Sheriff in Cork City**

Following the death of Mr. Patrick Powell, Cork City Sheriff, Mr. Martin A. Harvey has been appointed by the Minister for Justice with the consent of the Minister for Finance to the post, with effect from 29 April 1991.

### **7.3 1990/91 P35 Return**

The Collector-General's Office would like to take this opportunity to thank Tax Practitioners for their response in lodging 1990/91 P35 returns. Your efforts combined with the 1991 Advertising Campaign have improved on last year's success.

## 8. Stock Relief and the Current Years Basis

Many practitioners have sought clarification on how the change from a “preceding year” basis to a “current year” basis interacts with stock relief / clawback and transitional averaging.

Notwithstanding the transition to a current year basis of assessment, the so called “drop-out period” is still an accounting period in respect of which there may be an increase or decrease in stock values for the purposes of stock relief.

The following is the order in which the adjusted assessable Case 1 Farming Profits should be calculated:

- i) Calculate the adjusted profits as usual. If income averaging is claimed, this first step is done for each accounting period.
- ii) If stock relief / clawback applies, adjust the profits at (i) to arrive at the stock relief adjusted profits (for each accounting period in income averaging cases).
- iii) If transitional averaging is due, calculate this in respect of the adjusted profits at (i) or the stock relief adjusted profits at (ii), as appropriate.

### Stock relief and future exposure to clawbacks.

There are three main categories in which it is necessary to look at the amount of stock relief **effectively allowed / clawed back** as a result of transitional adjustments:

1. A farmer not on Income Averaging **whose stock values fall in the “drop-out” period** and who has claimed stock relief in an earlier period will have the clawback treated as a trading receipt of the “drop-out” period but, because the profits of the drop out period are not accessible, the clawback is not in effect assessed. The exposure to future clawback is however reduced by the amount of stock relief **effectively clawed back**.

### Example.

Y/e 31/12/1988	
Stock increase	£12,000
Stock relief claimed for 1989/90	
£12,000 @ 110%	£13,200
y/e 31/12/1989 (drop-out period)	
stock decrease	£ 5,000

The profits of the y/e 31/12/1989 will be increased by the clawback of £5,500, (5,000 @ 110%). However the increased profit figure is not assessed because it arises in the “drop-out year”. Future exposure to clawback is limited to £7,700 (7,000 @ 110%), despite the fact that the clawback of £5,500 was not charged to tax.

The position in relation to future exposure to clawback (as set out above) is not altered if part of the clawback of £5,500 comes into charge under the transitional averaging rule (Section 16, Finance Act 1990). For the purposes of transitional averaging, the profit of the “drop-out” year includes the amount of the clawback.

2. A Farmer not on Income Averaging whose stock increase in the “drop-out” period and who claims stock relief in respect of that increase will be exposed to future clawback only to the extent that relief has effectively been given (see the following two examples).

## EXAMPLE

Year ended	Stock value	Profits
31 March 1989	£ 80,000	
31 March 1990	£100,000	£30,000
31 March 1991	<u>£105,000</u>	<u>£25,000</u>
Profit y/e 31 March 1990 (“drop-out” year)		£30,000
Stock relief £20,000 x 110%		<u>£22,000</u>
Case I profit		<u>£ 8,000</u>
Profit y/e 31 March 1991 (1990/91)		£25,000
Stock Relief £5,000 x 110%		<u>£ 5,500</u>
Case I profit		<u>£19,500</u>

### Assessable Case 1 Figure

The transitional averaging reduces the Case 1 profit for 1990/91 to £13,750 being the average of £8,000 and £19,500.

### Stock Relief Calculation

If there had been no stock relief claim in either period the assessable Case 1 profit for 1990/91 would have been £25,000. It is accepted that the exposure to future clawback is restricted to the relief effectively allowed in 1990/91 i.e. £11,250 (£25,000 - £13,750).

### Example

#### [Farmer with both high profits and a high stock increase in the drop-out year].

Using the same figures as in the Example above, except that the profits before stock relief of the years ended 31 March 1990 and 31 March 1991 are £38,000 and £27,000 respectively.

### Assessable Case I Figure.

Profit y/e 31 March 1990 (“drop-out” year)	£38,000
Stock Relief £20,000 x 110%	<u>£22,000</u>
Stock Relief adjusted profits	<u>£16,000</u>
Profit y/e 31 March 1991 (1990/910)	£27,000
Stock relief £5,000 x 110%	<u>£ 5,500</u>
Stock relief adjusted profit	<u>£21,500</u>

Applying the transitional averaging rule the assessable figure for 1990/91 would be £18,750 (i.e. 16,000 + 21,500 x 1/2). However the minimum 125% rule gives a figure of £20,000. (i.e. £16,000 @ 125%), so this is the assessable Case I figure for 1990/91.

### Stock relief calculation

If there was no claim to stock relief the Case 1 profit of the year 1990/91 would have been £27,000 (i.e. the transitional averaging would not have applied). The effective stock relief granted for 1990/91 is therefore £7,000 (27,000 - 20,000) and it is accepted that only this amount is liable to future clawback.

3. A farmer on Income Averaging (Section 20B, Finance Act 1974) will be assessed for 1990/91 on the average profit (after stock relief) on the three years ended in that year. For example, a farmer who prepares accounts to 31 March in each year will be assessed for 1990/91 on the average of the profit of the three years ended 31 March 1989, 1990 and 1991.

If stock relief is claimed in any or all of the years ended 31 March 1988, 1989 or 1990, the farmer will effectively get relief only for two-thirds of the increase at 110%. It is accepted that in these circumstances any future clawback will be restricted to the relief actually granted (see example 1).

#### Example 1

	<b>Profit</b>	<b>Stock Relief</b>	<b>Adjusted Profit</b>
Y/e 31 March 1988	£10,000	£1,100	£8,900
1989	£11,000	£2,200	£8,800
1990	£13,000	£3,300	£9,700
1991	<u>£ 9,000</u>	<u>£1,650</u>	<u>£7,350</u>

#### Assessable Case I figure 1990/91

Average of the three years ended 31 March 1991 = £8,617.

#### Stock Relief Calculation

As only 2/3rds of the stock relief figures for y/e 31/3/1988, 31/3/1989 and 31/3/1990 are effectively allowed (because of the interaction of the drop out year and income averaging) only 2/3rd of those figures can be subject to possible clawback in the future.

Where there is a decrease in any or all of the years mentioned in the last paragraph, and stock relief has been claimed in earlier years, the full amount of the decrease at 110% will be taken into account in calculating the profit of the year before averaging. As the full amount has been taken into account, there will be no further exposure to clawback in respect of that amount, even though only two-thirds of the decrease will effectively have been clawed back (see example 2).

#### Example 2

	<b>Profit</b>	<b>Stock Clawback</b>	<b>Adjusted Profit</b>
Y/e 31 March 1988	£10,000	£4,400	£14,400
1989	£11,000	£1,100	£12,100
1990	£13,000	£ nil	£13,000
1991	<u>£ 9,000</u>	<u>nil</u>	<u>£ 9,000</u>

#### Assessable Case I figure 1990/91

Average of the three years ended 31 March 1991 = £11,366.

#### Stock Relief/Clawback Calculation

As only 2/3rds of the stock relief clawback figures for £4,400 and £1,100 are effectively brought into charge (because of the interaction of the drop out year and income averaging) the amounts of £4,400 and £1,100 are regarded as fully clawed back.