

TAX BRIEFING

Office of the Chief Inspector of Taxes

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Proposed Amendment Corporation Tax - 30% rate

Introduction

Section 44 Finance Act 1996, inserted into the Corporation Tax Act 1976, a new section, Section 28A, which provided for a 30% rate of corporation tax to be applied to the first £50,000 of a company's non-manufacturing income for a 12 month accounting period. The £50,000 is reduced in the case of an accounting period of less than 12 months duration or where the company has associated companies in the accounting period. The amount up to which income can be charged at the reduced rate is referred to in the legislation as the "specified amount".

Manufacturing Relief

Subsection (10) of Section 28A provides rules for the calculation of manufacturing relief in a case where income has been charged at the 30% rate. It provides that, in the calculation of manufacturing relief, total income is to be reduced by the specified amount and relevant corporation tax is to be reduced by 30% of that amount. Where the amount of income which is charged at the reduced rate is less than the specified amount the rule in subsection (10) does not produce the correct manufacturing relief.

Amendment

The Minister for Finance has announced that the **Finance Bill 1997**, will remove these unintended effects as respects accounting periods in relation to which the preliminary tax payment date is on or after **16 December, 1996**. The provision will amend subsection (10) of Section 28A to the following effect:

❖ in paragraph (a) by substituting the following for the definition of S "*S is an amount equal to so much of the profits of the company for the accounting period as are charged to tax in accordance with subsection (1)*",

and

❖ in paragraph (b) by substituting the following for subparagraph (ii) "*by an amount equal to so much of the profits of the company for the accounting period as are charged to tax in accordance with subsection (1)*".

Where the existing provisions result in a reduction of manufacturing relief for earlier accounting periods, manufacturing relief may be calculated for these periods on the basis of the altered rules in (i) and (ii) of this proposed amendment to Section 28A.

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Editorial

Christmas Greetings

On behalf of the **Tax Briefing** team I would like to take this opportunity to wish all our readers and contributors a very Happy and Peaceful Christmas and Best Wishes for the New Year.

It is an appropriate time to say a special "Thank You" to all our contributors from all parts of Revenue for the articles they supplied in 1996. Without your help and support **Tax Briefing** would not succeed.

A word of thanks also, to all the practitioners who have written to express their views and support. We look forward to receiving your views on content, or any topics of

general interest, which you would like to see included in future issues.

I would like to specifically acknowledge the contributions from the Technical Service Units of the Chief Inspector's Office for their articles in this issue on Corporation Tax, VAT, Lloyd's Scheme, Urban Renewal, UN Salaries & Pensions and a feature article on the Taxation Principles of Finance Leases.

Seasons Greetings to one and all.

John Leamy,
Editor.

TAX BRIEFING

Customer Service Unit,
Office of the Chief Inspector of Taxes,
4th Floor,
Setanta Centre,
Nassau Street,
Dublin 2.

Editor: John Leamy
Telephone No. (01) 671 6777, Extn. 4325.

Assistant Editor: Rosemary O'Rahilly
Telephone No. (01) 671 6777, Extn. 4310
Fax No. (01) 671 0960

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Completion of Form CT1

A certain amount of confusion has arisen in relation to the completion of the Form CT1 and in particular Section 12 "LR Entry," i.e. the amount chargeable at the reduced rate of 30%.

The following guidelines will be of assistance to practitioners:

Non-Manufacturing Companies

Where the accounting period spans 1 April 1996, it is treated as two accounting periods, one ending on 31 March 1996 and the other beginning on 1 April 1996. Trading Income should be apportioned between pre-1/4/96 and post-1/4/96 periods, and the £50,000 reduced by the number of months post-1/4/96 over 12.

- ❖ If the post-1/4/96 income is less than £50,000 (as reduced) it can be entered at LR in Section 12 (see example 1)
- ❖ If the post-1/4/96 income is greater than £50,000 (as reduced) it is reduced accordingly (see example 2)
- ❖ If the accounting period is less than 12 months, the £50,000 (as reduced) is apportioned accordingly (see example 3).

Example 1

Trading Income for accounting period year ended 30/7/96 £30,000

£30,000 x 4/12 £10,000

LR £10,000

The balance of £20,000 is taxable at the rate of 38%

Example 2

Trading Income for accounting period year ended 30/9/96 £120,000

£120,000 x 6/12 £ 60,000

However, the maximum amount at the reduced rate is:

£50,000 x 6/12 £25,000

Therefore, entry at LR £25,000

The balance, £95,000 is taxable at the rate of 38%

Example 3

Trading Income for accounting period 8 months ended 30/6/96 £160,000

£160,000 x 3/8 £ 60,000

Maximum reduced rate available:
£50,000 x 3/12 £ 12,500

LR £12,500

The balance, £147,500 is taxable at the rate of 38%

Manufacturing Companies

Manufacturing income is excluded from the reduced rate. The following steps should be taken in completing the CT1:

- ❖ Apportion total income between manufacturing and non-manufacturing income
- ❖ The non-manufacturing income is apportioned on a time basis as in example 1 above and entered at LR
- ❖ The manufacturing income plus the pre-1/4/96 non-manufacturing income is chargeable at the full rate of 38%
- ❖ Manufacturing Relief is calculated in the normal way (i.e. 28/38) and the figure is entered at R3.

Example

Accounting Period: year ended 31/7/96

Total Trading Income £60,000

Manufacturing income £45,000

Non-Manufacturing income £15,000

Non-Manufacturing (time apportionment)
£15,000 x 4/12 £ 5,000

LR entry £5,000

Chargeable at higher rate:

Non-Manufacturing (pre-1/4/96)
£15,000 x 8/12 £10,000

Manufacturing (total) £45,000

Total £55,000

(£55,000 x 38%) £20,900

Manufacturing Relief
£45,000 x 38% x 28/38 £12,600

R3 entry £12,600

Note: The above example has been calculated on the basis that the proposed legislation outlined in the front page has been enacted.

Group Companies

Where a company has associated companies, the £50,000 is divided between the associated companies. Associated companies may jointly elect to have the £50,000 apportioned in any manner specified by them. The information requested at Panel 27 does not amount to a joint election for the purposes of the reduced rate. A separate election must be made by all the associated companies. If they so elect, it is sufficient that the companies claiming the benefit of the reduced rate submit the election with their Form CT1. It is not necessary that a company disclaiming that benefit in favour of an associated company also submit a copy of the election. It should be indicated clearly on the front of the Form CT1, if the company is a member of a group and, if so, the total number of companies in the group.

The 30% rate does not apply to Capital Gains.

Set-Off of ACT against Surcharge

A number of enquiries have been received from practitioners asking whether ACT is available for offset against liability to a surcharge under Section 101 or 162 Corporation Tax Act 1976.

The following is the Revenue view: Section 39(1) Finance Act 1983 provides that advance corporation tax (ACT) paid by a company in respect of any distribution made by it in an accounting period shall be set, so far as possible, against its liability to corporation tax on any **income** charged to corporation tax for that accounting

period. Subsection (4) provides that the definition of "income" is the same as set out in Section 28(4) of the Corporation Tax Act 1976, which states:

"the income of a company for an accounting period shall be taken to be the amount of its profits for that period on which corporation tax falls finally to be borne exclusive of the part of the profits attributable to chargeable gains...."

The surcharge is defined in Section 101(1) of the Corporation Tax Act 1976 as an additional duty of

corporation tax charged on the company and it cannot be seen, therefore, as a charge on income, notional or otherwise.

The surcharge quite clearly does not come within the definition of income charged to corporation tax for the purposes of Section 39 Finance Act 1983, and the possible set-off of an ACT liability against a surcharge liability does not arise.

Therefore, any ACT paid by a company cannot be set against a surcharge liability arising under Section 101 of the Corporation Tax Act 1976.

Revenue take action to counter “Phoenix Syndrome” abuse

Introduction

Significant tax is being evaded by a small section of the business community through abuse of the protection provided by limited liability. Each year companies go out of business leaving substantial unpaid debts and no assets to meet the outstanding liabilities. In some of these a pattern can be detected.

Phoenix Syndrome

This pattern is generally referred to as the “**phoenix syndrome**”. The company ceasing business will have little or no assets and the business will be taken over by another company under the control of the same persons. Some minor changes in the business arrangements or in the composition of the controlling group may be introduced to camouflage the fact that a phoenix operation is involved. Essentially the objective is to avoid payment of the amounts due to creditors while the promoters continue in business under the protection of another company. A feature of these schemes is that frequently tax will be a major outstanding debt and may even be the only debt remaining.

Competitive Advantage

This abuse is a significant matter for Revenue but must also be of concern to traders in direct competition who meet their tax obligations in full and on time. The competitive advantage gained through non payment of VAT and PAYE/PRSI can be very significant. Furthermore the general body of taxpayers is disadvantaged since the burden of tax is increased for them if significant tax is being evaded by the few.

Even where a tax debt is not involved a phoenix based scheme can impact adversely on Revenue if cash flow problems are created for other taxpayers such as subcontractors or suppliers of the insolvent company.

Assurance

The purpose of this article is to draw attention to the measures being introduced by Revenue to counter “**Phoenix syndrome**” abuse. At the same time we want to assure the business community that these measures are not aimed at genuine business failure or the promoters of risk ventures which entail a high degree of business failure. Special care will be exercised to ensure that only clearly identified cases of “**phoenix**” abuse are targeted. Some of the measures outlined in this article will also apply to a company managed in a manner which is detrimental to some or all creditors even if the business is not continued under a new guise. However the “**phoenix syndrome**” is clearly the main problem and is therefore the main focus of this article.

Revenue Approach

Over the past number of years, Revenue has adopted a more proactive approach to the “**phoenix**” problem. A managed strategy operates across all branches of the organisation and relevant information from many sources within the Office is collated so as to:

- ❖ Identify “**phoenix**” situations at the earliest possible stage
- ❖ Ensure rapid follow up action aimed at preventing the build up of tax arrears

- ❖ Mount an effective challenge through the courts where evidence of fraudulent or reckless trading is uncovered
- ❖ Provide a rigorous and ongoing monitoring of all those identified as having evaded tax through a “**phoenix**” operation.

Identification

In normal working a “**phoenix**” operation would not come to light until the collection process had reached the final stages of enforcement. A substantial tax arrear could have accumulated and all the company’s assets could have disappeared by that stage. In this connection it is worth noting that a very high proportion of tax which had to be written off as irrecoverable in recent years related to insolvent companies. Examination of the “**phoenix**” type cases reveals that deliberate measures would have been taken by the promoters to conceal the fact that a tax debt was accumulating. The time thus gained facilitates the evasion of greater amounts of tax.

It is clear that much faster identification is needed; simply waiting for cases to emerge from the enforcement process is far too slow to prevent serious tax loss. To be effective, identification must be achieved as soon as the new “**phoenix**” company is registered for tax purposes or as soon as possible thereafter but not later than the due date for the first payment of tax by that company.

PHOENIX CASES

In future, identification will be organised as a task in itself carried out by staff specialising in that function. These staff will be assisted in the work by the organisation of all Revenue data into linked data bases which will be accessible on a continuous basis through a powerful computer network.

The co-operation of company personnel and of practitioners is sought particularly in dealing with:

- ❖ Staff working in Revenue registration sections
- ❖ Revenue officers on visits to the business premises of newly registered companies
- ❖ Staff dealing with the tax compliance of companies.

Follow-up

In challenging all aspects of a “**phoenix**” operation Revenue will:

- ❖ Mount a rigorous follow up action directed at the old company to secure payment of the maximum amount of Revenue debt
- ❖ Pursue debt recovery action against directors for any Revenue debt remaining if this action is sustainable
- ❖ Initiate liquidation proceedings where necessary.
- ❖ Attend creditor’s meetings where appropriate but priority will have to be given to meetings where there is the possibility of significant loss to the Exchequer
- ❖ Co-operate with other creditors in having a liquidator appointed in cases where the apparent assets of the company seem insufficient to meet liquidator’s costs
- ❖ Work closely with liquidators to reduce the risk to the Exchequer.

Mounting a challenge

As a creditor, Revenue will be particularly concerned that the facts and circumstances surrounding each phoenix type case are examined with a view to mounting a challenge through the courts for fraudulent or reckless trading against the directors.

Consideration will also arise as to whether the actions of any professionals or other parties involved have been such that they can be joined in any court action.

Where it is proved that the directors of a company have improperly allowed the business to continue to trade while insolvent, to the detriment of its creditors, Irish company law provides for a number of sanctions to be taken against them.

The sanctions available against directors are:

Criminal liability for fraudulent trading

- ❖ On summary conviction - liable to a term of imprisonment not exceeding 12 months, or to a fine not exceeding £1,000, or both,
- or
- ❖ On conviction on indictment - liable to imprisonment for a term not exceeding seven years, or to a fine not exceeding £50,000, or to both.

Civil liability for fraudulent or reckless trading

- ❖ Personal responsibility without limitation for all or part of the company’s debts
- ❖ Restriction (Section 150 Companies Act 1990) or disqualification (Section 160 Companies Act 1990) to act as a director.

In 1995, a total of 57 directors were restricted and their names were published in Iris Oifigiúil and in the annual report of the Companies Office.

Ongoing Monitoring

The primary objective of this element of the overall strategy is to police the tax compliance record of the “**new**” company to prevent any build-up of Revenue debt.

We have already mentioned how early identification of the “**phoenix**” company can contribute to this objective. On an ongoing basis, where there is a reasonable suspicion that company promoters may repeat a previous tax default pattern, any new companies sponsored by the same promoters will be monitored. Information on defaulting companies and on tax at risk is constantly being updated by outdoor officers in Compliance, Audit and Local Collection. An early warning system between the Inspector’s Office and the Collector General’s Office is invoked and any response deemed necessary is initiated.

Introduction

The level of interest in Small Self-Administered (SSA) pension schemes has increased in recent times. This article is a summary of the principal Revenue requirements for SSA schemes.

The total assets of Irish Pension Funds amount to almost £16 billion and annual cash flows into schemes are over £663 million. At 31 December 1995, 44,702 schemes were registered with the Pensions Board. Of these, 37,362 are individual insured arrangements. There are approximately 500 SSA schemes.

SSA Schemes

A scheme will normally be defined as SSA if:

- ❖ There are 12 or fewer members or
- ❖ If 65% or more of the scheme assets relate to the provision of benefits for 20% Directors.

Briefly, a 20% director is an individual who together with a spouse and children controls more than 20% of the shares in the employing company.

In a SSA scheme, the individuals involved have, at least, three different interests. They are the owners of the business, the scheme trustees and the scheme beneficiaries. This could give rise to a conflict of interests and lead to actions concerning the scheme being taken for reasons other than the provision of benefits or retirement. In common with all schemes seeking exempt approved status, a SSA scheme must comply with the mandatory approval condition in Section 15(2)(a) Finance Act 1972. It must be shown that *"the scheme is bona fide established for the sole purpose of providing relevant benefits"*.

Revenue have an obligation to ensure that the generous tax reliefs available for retirement provision are not abused. The tax exempt investments held for the provision of scheme benefits should not be of a kind, or used in such a way, so as to produce a non relevant benefit for the beneficiaries or the employer. To meet these concerns Revenue have laid down special requirements for the ongoing approval of SSA schemes.

Pensioner Trustee

Revenue insist on the appointment of a pensioner trustee. The purpose of the appointment is to inhibit the termination of a scheme for tax avoidance purposes and an appropriate undertaking is required. In addition to this specific responsibility, **the function of the pensioner trustee is to protect the Revenue position.** The pensioner trustee should ensure that the contributions paid in, the nature of the scheme investments, and the level of benefits paid out all comply with Revenue regulations. There is also a responsibility to supply all information required by Revenue, including annual accounts and actuarial reports.

Any person wishing to act as a pensioner trustee must have prior Revenue approval. The applicant should be an experienced pensions professional and in considering any application Revenue will seek to establish the individual's "bona fides". The applicant should also have a good knowledge of, together with practical experience, of the specific Revenue requirements in this area.

Funding

All schemes must submit an initial actuarial valuation and further reports every three years thereafter.

Investments

All investments should be on an arms length basis. The following are prohibited:

- ❖ Loans to scheme members or associates
- ❖ Loans to the employer
- ❖ "Pride in possession" articles including works of art, yachts, etc.
- ❖ Holiday homes
- ❖ Assets acquired from or let to the employer.

A proposal to acquire property may be approved if it can be shown that:

- ❖ The vendor is at arms length from the scheme and the employer
- ❖ The transaction does not involve borrowing

- ❖ The property will be let, and eventually sold, on an arms length basis
- ❖ The scheme investments match the scheme liabilities.

A transaction which involves the scheme trustees directly in the acquisition and development of property with a view to its disposal would not constitute an investment to which the exemption in Section 16(2) Finance Act 1972 applies. Only investment income is exempt from tax, trading income is not.

All SSA schemes must submit annual accounts to Retirement Benefits District.

Benefits

Members of SSA schemes are subject to the same benefit restrictions as members of other schemes. The pension must be secured by the purchase of an annuity from a Life Office. If there is provision in the scheme rules for full commutation of pension where the member is "in exceptional circumstances of serious ill-health", no commutation should take place without prior Revenue approval. Where early retirement benefits are provided for 20% Directors, it must be shown that the retirement is genuine.

Further Information

The above is a general outline of SSA Schemes.

Further information can be obtained from:

*Office of the Inspector of Taxes,
Retirement Benefits District,
Lansdowne House,
Lansdowne Road,
Dublin 4.*

Telephone: (01) 668 9400

Fax No.: (01) 668 9690

Introduction

This article sets out the Irish Taxation implications for Irish Names following acceptance of Lloyd's recent Reconstruction and Renewal Scheme. The treatment has been agreed by Revenue with the Irish Taxation advisor to Lloyds and with Lloyd's Taxation Department.

Irish Taxation - General Principles

Equitas additional premium

The Equitas additional premium will be an allowable syndicate expense and will be included in arriving at the Lloyd's result for the 1996/97 tax year.

Debt credits and litigation settlement fund

These items will be taxable trading receipts for the tax year 1996/97. However, a deduction will be allowed for 1996/97 to reflect any Central Fund indebtedness (previously taxable) that is effectively repaid by the debt credit allocation. The net tax payable on this income will vary depending on the brought forward losses and/or expenses available for offset.

Triple release

Any profit for the 1993 Year of Account will be taxed in the normal way. Early releases from the 1994 and 1995 accounts will be taxed when the full profits for these years are declared.

Members special contribution

Names paying the special contribution levied on the 1993, 1994 and 1995 underwriting accounts will obtain a tax deduction for this item as a syndicate expense of the underwriting year. Any special contribution rebate in due course for Names who have ceased will be assessed in the tax year of receipt.

Finality bills

The amount of Names finality bills is not, in itself, a reliable guide to likely tax liabilities or repayments. Much of the bill is likely to represent underwriting results already declared for which tax relief has already been given. However, to the extent that a Name has been assessed for tax on Central Fund drawdowns and the payment of the finality bill represents, in whole or in part, the repayment of a Central Fund debt, then a deduction will be due.

Payment of finality bills

The tax position will be largely unaffected by the way in which you pay your finality bill - either through a single payment or through a structured payment plan. Interest charged under structured payment plans should, however, be an allowable expense (see below).

Interest on loans to fund finality bills

Interest incurred wholly and exclusively for business purposes is an allowable expense. This will include interest on money borrowed to fund finality bills in the case of Names continuing to underwrite during the interest payment period. The position in relation to Names ceasing to underwrite is more complex. Generally, expenses incurred after cessation of an underwriting trade, unlike in the UK, can only be offset against Lloyd's related income received post cessation insofar as not previously taxed.

Estate Protection Plan

The terms of this plan have varied between years of account but certain general tax principles will apply. The Equitas premium is a business expense and may create or augment an underwriting loss for the year of payment. Debt credits and settlement monies are profits

which, under the terms of the plan, are payable to the insurers as additional premiums. Payments from the plan to meet losses are taxed as trading receipts. Because the reconstruction plan brings to a close all 1992 and prior years of account, the tax position for many deceased Names will be resolved and final balance under the plan can be calculated. Any resultant repayments will be taxable as trading income.

New style Special Reserve Fund

Names with profits for the 1993 Year of Account after deducting the Equitas additional premium, will be able to make transfers into the new style Special Reserve Fund, subject to the normal time limits. Conversely, where a loss arises a withdrawal must be made where a Special Reserve Fund balance exists.

Return premiums

If in future Names become entitled to a return premium under the terms of the Equitas reinsurance contract, then any recovery will be taxable as a trading receipt. For Names who are trading at Lloyd's at the time of the recovery, it will be attributed to the tax year beginning in the calendar year in which the return premium is paid. For Names who have ceased to trade at Lloyd's, the recoveries will be attributed to the year of receipt.

Losses brought forward

Because debt credits and settlement monies are derived from a Name's Lloyd's activity, Lloyd's trading losses brought forward may be offset against this income.

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Non-Lloyd's income

Where the Equitas additional premium creates or augments a loss for the tax year 1996/97, Names may obtain relief for the loss under the normal taxation provisions, including by offset against non-Lloyd's income.

Capital Gains Tax (CGT)

The disposal of assets to meet the finality bill, whether these assets form part of funds at Lloyd's or not, may produce a liability to CGT. Gains will be computed in the normal way after indexation relief and the set-off of any CGT losses brought forward.

Adjustments for taxation

The figures provided in finality statements will be commercial rather than tax numbers. In recent years the Inland Revenue has disallowed for tax, part of the reserves of some syndicates. Reinsurance by Equitas should not be subject to a disallowance and any previous adjustments, to the extent that they relate to 1992 and prior liabilities, will be reversed. This will benefit Names by increasing any allowable tax losses or reducing taxable profits.

Other Issues

There may be some other Irish tax issues arising as a result of Reconstruction and Renewal which may be peculiar to individual Names. These will be looked at on a case by case basis.

Personal Stop Loss (Irish Names)

Recoveries due under personal stop loss policies are taxed for the year of assessment in which the declared loss giving rise to the recovery is allowed. These recoveries are taken into account for tax purposes without regard to the amounts actually received.

Under the Reconstruction & Renewal proposals further amounts may become recoverable under personal stop loss policies either as a result of previously declared losses being called or additional losses from the Equitas reinsurance. In addition, the allocation of debt-credits/litigation settlement funds may give rise to repayments under these policies.

The net personal stop loss recovery or repayment position on accepting the offer can therefore be analysed into three parts each with different tax implications:

- ❖ Recoveries in respect of uncalled losses declared at 31 December 1994 (or an earlier year end). These will already have been taxed and therefore no further liability arises.
- ❖ Recoveries due as a result of the Equitas reinsurance after allocating debt-credits/litigation settlement funds. These will be taken into account for tax purposes for the year of assessment 1996/97 as they relate to losses declared at 31 December 1995.
- ❖ Repayments resulting from the Equitas reinsurance and the allocation of debt-credits/litigation settlement funds. These will be trading expenses of 1996/97.

International Issues

Current Position on Ireland's Double Taxation Agreements

Ireland has comprehensive Double Taxation Agreements with twenty nine countries, twenty seven of which are currently in force. The treaty with Czech Republic comes into effect in January 1997. The Hungarian treaty, which has already been ratified by Ireland, will come into force when it is ratified by Hungary.

The Irish treaty network continues to be expanded and updated. Negotiations for the conclusion of treaties are taking place with Mexico, Greece, South Africa, India, Malaysia and the Baltic States.

Treaties currently in the process of renegotiation include: the United States, Belgium and Italy.

Copies of existing Double Taxation Agreements may be purchased from:

*Government Publications Sales Office,
Sun Alliance House,
Molesworth Street,
Dublin 2.*

Telephone: (01) 661 3111
Fax: (01) 475 2760

International tax matters are dealt with in the following areas in the Revenue Commissioners;

Administration of tax treaties (claims etc.) and residence rules.

*International Claims, Residence and Charities Unit,
Revenue Commissioners,
Government Offices,
Nenagh,
Co. Tipperary.*

Telephone: (067) 33533
Dublin Callers: (01) 677 4211
Fax: (067) 32916

International tax policy and treaty negotiations.

*Direct Taxes: International,
Revenue Commissioners,
Dublin Castle,
Dublin 2.*

Telephone: (01) 679 2777
Fax: (01) 679 3314

Tax Implications for Life Assurance Companies

E.C. (Insurance Undertakings: Accounts) Regulations, 1996

Introduction

The above regulations give effect to the Insurance Accounts Directive adopted per Council Directive No. 91/674/EEC of 23 December 1991. While the Directive applies to accounting periods commencing on or after 1 January 1995 it is unlikely to be fully implemented by companies until accounting periods commencing on or after 1 January 1996.

Outline of Main Accounting Changes Introduced by the Directive in respect of Life Assurance Companies

The main accounting changes from a tax perspective are as follows:

- ❖ The Profit & Loss account is effectively split into two parts - the technical account (formerly the Revenue account) and the non-technical account (formerly the P/L account)
- ❖ The account formerly known as the Investment Reserve account is also being reclassified into two non-distributable reserves - the Fund for Future Appropriations and the non technical account P/L reserves
- ❖ There are accounting restrictions on the use of the Fund for Future Appropriations account for non-profit offices. The effect of these is that the full investment return is brought through both the technical and non-technical parts of the Profit & Loss account. For accounting purposes, it is no longer acceptable for non-profit offices to transfer investment gains and losses from non linked business to the Investment reserves albeit that the allocation of such gains and losses has not yet been determined by the appointed actuary.

- ❖ The Directive requires a proportion of annual acquisition expenses to be deferred commensurate with unearned income. Deferred acquisition costs carried forward should be amortised over the period in which they are expected to be recoverable out of matching revenues.

- ❖ Accounting profit in the non technical account will be split into the non-distributable portion and the distributable remainder.

Notional Case I (NCI) Computation

Historically the NCI computation is derived from the transfer made to shareholders from the Revenue account, regrossed to take account of tax deducted in arriving at the Revenue account surplus. The transfer is increased by any investment income or profits on disposals allocated directly to the shareholders in the Profit & Loss Account. This figure is then adjusted having regard to capital allowances due and normal disallowable expenditure (e.g. entertainment expenses) to give the final NCI profit for the year. The changes in the Insurance Accounts Directive which could impact on the existing method of NCI calculations are:

- ❖ Deferral of Acquisitions costs
- ❖ Inclusion of realised and unrealised gains/losses on non-linked investments
- ❖ Allocation of part of the Life Fund Investment Return to the shareholders.

These changes have the effect of recognising non-distributable amounts as profits. As with embedded value accounting the result can be very different to the statutory result (as shown on form 28 of the Department of Enterprise and Employment (DEE) return), on which the NCI computation is historically based.

Having regard to the above and on the basis that the non-distributable part of the non-technical account is comprised of what are essentially unrealised profits it is confirmed that there will be no change for tax purposes to the starting point in the NCI computation. This confirmation ensures:

- ❖ Case I principles will continue to apply and therefore unrealised gains/losses will continued to be excluded from the computation
- ❖ Continuity of the existing practice that any surpluses carried forward unallocated are regarded as reserved for policyholders under Section 35 CTA 1976

- ❖ That companies wishing to publish embedded value accounting results will not suffer adversely for NCI purposes. This confirms the existing practice whereby the preparation of accounts on the embedded value basis is not prejudicial as regards the calculation of NCI.
- ❖ The Deferred Acquisitions Cost adjustment will not impact on the profit attributable to shareholders for NCI purposes.

As the methodology of accounting for the shareholders profit in Life Assurance Companies is still being developed, the changes outlined in this article may be subject to review in light of accounting developments at some future date. Any changes as a result of any future review will be applied from a specified future date.

Further Information

For further information contact:

*Office of the Inspector of Taxes,
Dublin Audit District 5,
Lansdowne House,
Lansdowne Road,
Dublin 4.*

Telephone: (01) 668 9400
Fax: (01) 668 9706

Urban Renewal Relief - Incentives in Enterprise Areas

Introduction

In October 1994, as part of the 1994 Urban Renewal Scheme, the Ministers for Finance and Enterprise & Employment extended the Urban Renewal Scheme to six areas, known as enterprise areas. These designated enterprise areas aim to attract modern manufacturing industries and internationally traded service ventures, such as computer services, research and development enterprises, telemarketing and commercial laboratories, to the heart of these urban centres. The legislation was contained in Section 35 Finance Act 1995, which inserted a new Section 41A into Chapter IV, Part I, Finance Act 1994.

Details of the Enterprise Areas

A total of six areas have been designated as enterprise areas. These areas are located in:

Dublin

East Wall,
Macken Street / Grand Canal Street

Galway

Westside

Cork

Spring Lane, Blackpool,
Dublin Street, Kilnap, Fitz's Boreen

The Incentives

(Definitions of Qualifying Building, Qualifying Activities and Qualifying Period are given later.)

Capital Allowances

The full amount of expenditure on construction or refurbishment of a qualifying building in an enterprise area and which is incurred in the qualifying period qualifies for industrial buildings allowances. The rates are:

Owner-occupier

- ❖ 50% free depreciation and 4% annual allowance
- or
- ❖ 25% initial allowance and 4% annual allowance.

Lessor

- ❖ 25% initial allowance and 4% annual allowance.

Balancing Charge

Where an event which would otherwise give rise to a balancing charge occurs in the case of a qualifying building, no balancing charge can be imposed where the event occurs more than 13 years after:

- ❖ The building is first used in the case of construction expenditure or
- ❖ The incurring of the expenditure in the case of refurbishment.

This 13 year limit applies even where the building is one which would ordinarily be classed as an industrial building e.g. a factory.

Notwithstanding this restriction on the imposition of a balancing charge, the building still has a 25 year "life" for the purposes of industrial buildings allowances. There is no prohibition on the granting of a balancing allowance after the expiry of the 13 year period.

Double Rent Deduction

Section 42 Finance Act 1994 makes provision for a double rent deduction. This deduction is available to the lessee of a qualifying building, subject to the usual conditions:

- ❖ Construction or refurbishment expenditure, which is capital in nature, must be incurred on a qualifying building in the three year qualifying period
- ❖ Where the expenditure is on refurbishment, it must amount to 10% or more of the site-exclusive market value of the building before the expenditure is incurred
- ❖ The lease under which the rent is paid must be entered into during the three year qualifying period
- ❖ The lease under which the rent is paid must be on bona fide commercial terms
- ❖ The lessor and lessee must not, directly or indirectly, be connected with each other.

Rate Remission

Remission of rates is provided on a sliding scale over 10 years, tapering from 100% remission in the first year to 10% remission in the tenth year. Full rates are payable thereafter. In the case of new buildings, the remission is based on the full rateable valuation of the building. For refurbished buildings, the rates remission is based on the increase in rateable valuation following refurbishment. Further details are available from the Local Authorities involved.

Definitions

Qualifying Building

The incentives are available only where the building is a "qualifying building" as defined. To qualify for the incentives the building must meet the following conditions:

- ❖ The site of the building must be located wholly within an enterprise area
- ❖ The building must be used for a qualifying activity, after it is constructed or refurbished
- ❖ The qualifying activity must be carried on by a company (either as owner-occupier or lessee).

A building will not qualify if it is occupied by an unincorporated trader. However, the lessor of a building need not be a company. All that is required is that the building be occupied by a company for qualifying activities.

Any part of a building in use as a dwelling house does not qualify for the incentives.

Qualifying Activities and Certification Process

In order to qualify for the incentives, the company occupying the premises must:

- ❖ Have been approved for financial assistance by Forbairt or the Industrial Development Agency (Ireland)
- ❖ Hold the necessary certificate.

URBAN RENEWAL

The certificate referred to on page 10 is a certificate from the Minister for Enterprise and Employment stating that the company is a qualifying company. In deciding whether or not to issue such a certificate, the Minister must be satisfied that the trade being carried on, or which will be carried on, by the company is a qualifying trade and that the carrying on of the trade will contribute to the balanced development of the area.

A **qualifying trade** is one which consists of either:

- ❖ The manufacture of goods within the meaning of Chapter VI, Part I, Finance Act 1980 i.e. qualifying for the 10% manufacturing rate of corporation tax

or

- ❖ An internationally traded service within the meaning of the Industrial Development Act 1986.

A certificate may be withdrawn by the Minister at any time. This may happen if the company fails to carry on a qualifying trade, ceases to carry on such a trade, or if it fails to comply with conditions set out in the certificate. The withdrawal will be effective from a date specified on the notice of withdrawal. Should a certificate be withdrawn, no further capital allowances or double rent deduction will be due as the building is no longer a qualifying building.

The issue or withdrawal of a certificate is a matter for the Minister for Enterprise and Employment.

Qualifying Period

The legislation has retrospective effect to 1 August 1994, and runs for the three year period to 31 July 1997.

Further Information

An information booklet on the Enterprise Areas has been jointly issued by Forfas, Forbairt and IDA Ireland. The booklet and further information on the scheme may be obtained by contacting any of these organisations.

Review

The Minister for Finance has recently announced that the Minister of State at the Department of the Environment has appointed a consultancy team to review the entire Urban Renewal Scheme. The consultants' report will look at the impact of the scheme in fiscal, social and architectural terms.

This content is more than 5 years old.
Where still relevant it has been incorporated
into a Tax and Duty Manual
or other website text.

Revenue Publishes New Guides for Small Businesses

The Revenue Commissioners have given a commitment to the small and medium size business sector to simplify and streamline procedures and to minimise compliance costs. As part of this commitment, a number of new guides have recently been published. The aim of these guides is to make the tax system easier to understand, to help businesses to comply with their tax obligations and to reduce compliance costs.

Starting in Business

This guide is aimed at people starting in business in a small way. Such people have to account for and pay their own tax annually and may also have to account for VAT and/or PAYE/PRSI on a regular basis.

The guide answers many of the basic questions people ask in relation to tax when setting up a business particularly in relation to completion of returns and payment of tax.

It is hoped that by providing this information from the start people will be fully aware of their tax obligations and this should assist them in paying their taxes, making their tax returns on time and reducing their compliance costs.

Reference: IT 48

Issued: December 1996

VAT for Small Businesses

This guide provides a simple outline of the VAT system for a small business.

It covers such items as registration, payment of VAT, VAT repayments and keeping records.

It also provides detailed examples and advice on completion of the Form VAT3 and Annual Return.

The more comprehensive “Guide to Value Added Tax” will still be available to cater for more complex situations.

Reference: IT 49

Issued: December 1996

Further Information

The four guides are available individually or as part of a pack - **Revenue Guides for Small Businesses**.

The pack can be obtained from any tax office or from the Revenue Forms & Leaflets Service at

(01) 878 0100

(available 24 hours a day).

PAYE/PRSI for Small Employers

This simplified guide shows how the PAYE/PRSI system is operated. It is designed to cater for employers new to the operation of PAYE/PRSI or those who have a small number of employees.

The guide outlines the first steps to be taken in the operation of the PAYE/PRSI system and contains simple examples and instructions on completion of forms with particular emphasis on the completion of the Tax Deduction Card (TDC).

It also gives guidance on such matters as payment of tax, completion of the end of year forms, calculation of PRSI and definition of Pay.

The more comprehensive "Employer's Guide to PAYE" will still be available to cater for more complex situations.

Reference: IT 50

Issued: December 1996

Tax Reliefs for Business - A Guide to Recent Developments

The tax system contains many reliefs and incentives for businesses at various stages in the business lifecycle from the start-up phase through expansion and development to the final disposal by way of sale, gift or inheritance.

This guide briefly outlines the main developments in these reliefs and incentives in recent years which have been specifically aimed at helping enterprise.

It covers the reliefs which are available when starting up a business such as the seed capital scheme and the Capital Gains Tax and Capital Acquisitions Tax reliefs which are available when disposing of a business.

Reference: CAT 9

Issued: December 1996

New Leaflets for Over 65's and Incapacitated Persons

As part of our ongoing aim to provide information to all our customers on their tax entitlements new leaflets are now available.

The leaflets are:

Allowances for Over 65's

A comprehensive guide to the allowances and reliefs available.

Dependent Relative Allowance

This leaflet contains information on the allowance due to people who support or maintain a relative.

Incapacitated Person - Allowance for employing a Carer

This leaflet gives detailed information on the allowance which can be claimed by an incapacitated individual who employs a carer.

Blind Persons - Allowances & Reliefs

This leaflet provides information on the allowances and reliefs available to blind persons.

The leaflet is available in large print to facilitate the partially sighted and is also available in Braille and on cassette.

The leaflet is being issued in conjunction with the announcement of a comprehensive tax support service to facilitate blind persons in their dealings with the tax office.

For further information or clarification on any point, blind persons are encouraged to contact the *Central Telephone Information Office* at (01) 878 0000 or their tax office.

New Charity Leaflets

Charities Section has introduced the following leaflets:

CHY 1

Applying for Relief from Tax on the Income & Property of Charities.

An application form for charitable organisations applying for exemption from tax on the basis of being established for charitable purposes only.

CHY 2

Applying for Relief from Income & Corporation Tax for certain Sporting Bodies.

An application form for sporting bodies applying for exemption from tax on the basis of being established for the sole purpose of promoting athletic or amateur games or sports.

CHY 7

Trading by Charities - Exemption from Tax.

A leaflet which describes the most common types of trading activities carried out by charities and how these are treated for tax purposes.

All of the leaflets referred to above can be obtained from any tax office or from the Revenue Forms & Leaflets Service (01) 878 0100 (available 24 hours a day)

United Nations & Specialised Agencies of the United Nations

Salaries & Pensions

Background

A number of queries have arisen as to which of the following:-

- ❖ Salaries and emoluments payable by the United Nations to Irish resident officials
- ❖ Salaries and emoluments payable by a specialised agency of the United Nations to Irish resident officials
- ❖ Pensions payable by the United Nations and by a specialised agency of the United Nations to Irish resident individuals,

are relieved from the charge to Irish tax under the provisions of the **Diplomatic Relations and Immunities Act 1967**.

[Note - the charge to Irish tax referred to is a charge under Case 111 of Schedule D].

Officials of the United Nations

Under the provisions of Section 18(b), Article V, Third Schedule of the Diplomatic Relations and Immunities Act 1967, Irish resident officials of the *United Nations* are relieved from the charge to Irish income tax on the salaries and emoluments paid to them by the *United Nations*.

Officials of the Specialised Agencies of the United Nations

Under the provisions of Section 19(b), Article VI, Fourth Schedule of the Diplomatic Relations and Immunities Act 1967, Irish resident officials of a *specialised agency* of the United Nations are relieved from the charge to Irish income tax on the salaries and emoluments paid to them by such *specialised agency*.

Former officials of the United Nation and its Specialised Agencies

The relief from Irish tax outlined above only applies to serving officials of the United Nations and to serving officials of a specialised agency of the United Nations. The provisions of the Diplomatic Relations and Immunities Act 1967 do **not** relieve from the charge to Irish tax, pensions payable by the UN [or by a specialised agency or the UN] to Irish resident individuals.

List of Specialised Agencies of the United Nations

<i>Food and Agricultural Organisation [FAO]</i>	<i>International Telecommunications Union [ITU]</i>
<i>World Trade Organisation [WTO]</i>	<i>UN Educational Scientific and Cultural Organisation [UNESCO]</i>
<i>International Trade Centre [ITC]</i>	<i>UN Industrial Development Organisation [UNIDO]</i>
<i>International Atomic Energy Agency [IAEA]</i>	<i>International Union for the Protection of New Varieties of Plants [UPOV]</i>
<i>International Consultative Group on Food Irradiation [ICGFI]</i>	<i>Universal Postal Union [UPU]</i>
<i>International Civil Aviation Organisation [ICAO]</i>	<i>World Health Organisation [WHO]</i>
<i>International Fund for Agricultural Development [IFAD]</i>	<i>World Intellectual Property Organisation [WIPO]</i>
<i>International Labour Organisation [ILO]</i>	<i>World Meteorological Organisation [WMO]</i>
<i>International Maritime Organisation [IMO]</i>	<i>World Tourism Organisation [WTO]</i>
<i>International Monetary Fund [IMF]</i>	

Finance Leasing

Introduction

A finance lease is a lease that transfers substantially all the risks and rewards of ownership of an asset to the lessee. Most finance leases operate for a primary period during which the lessee effectively pays for the asset and for a secondary period during which the lessee may continue to lease the asset for a nominal amount.

This article sets out the tax treatment applicable to finance leases of assets used for the purposes of a trade or profession.

Payment under a finance lease may be in the form of recurring payments or initial leasing charges (i.e. a lump sum payable at commencement of the lease, which may represent a trade in of another asset against the leased asset). Various other types of payment may arise in more complex leases including lump sum payments made by the lessee at the end of the lease-term (balloon payments).

Principles of Taxation for Finance Leases

General

For tax purposes, profits are calculated and capital allowances are allowed on the basis of the legal form of the transaction. The lessee is allowed a deduction for lease rentals in so far as these have been laid out wholly and exclusively for the purposes of the lessee's trade; the lessor is charged on these rentals and is entitled to claim capital allowances in respect of the asset.

Tax adjustments required

In accounting for finance leases, the lessee recognises the leased asset in the balance sheet and charges depreciation and finance charges in relation to the asset in the profit and loss account.

In adjusting the profit for tax purposes, the depreciation and finance charges are added back and relief is allowed for lease rentals. Where the leased asset is a passenger motor vehicle, the lease rentals are restricted by reference to the relevant limit in Section 27 Finance Act 1973 (at present £14,000).

Timing of allowance

In considering the period in which a deduction for lease rentals is allowed, regard must be had to the ordinary principles of commercial accounting. The timing of the deduction is by reference to the accruals concept (SSAP 2) which provides for the matching of revenues with associated costs.

In practice this operates as follows:

- ❖ Ordinary recurring payments under a finance lease should be written off on a straight line basis over the period during which it is expected that the asset will be leased
- ❖ Initial lease rentals under the lease or up-front payments made by the lessee represent a payment in advance of lease rentals and are allowed over the period during which it is expected that the asset will be leased.

In practice most finance leases terminate at the end of the primary period.

Rebates of Rentals

At termination of the lease, the asset is sold by the leasing company for its market value. The majority of finance leases provide for a rebate of rentals to the lessee on termination. The amount of the rebate is generally equivalent to the market value of the asset less a transaction fee charged by the leasing company.

Where the lessee does not wish to acquire the asset, the finance company issues a cheque for the difference between the amount realised on sale less amounts owing to the finance company.

Where the lessee wishes to acquire the leased asset, the leasing company will set the rebate of rentals against the cost to the lessee of the asset (i.e. market value) and the lessee pays any balance owing on the lease to the leasing company.

Where the lessee wishes to trade-in the leased asset against another leased asset, the rebate of rentals is set against the cost of the new asset. Where the new lease is issued by a different finance company, that company generally issues a cheque to the dealer for any amount owing on the old lease.

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The dealer passes this cheque to the old finance company. The lease agreement will generally show the up-front payment as an initial payment made under the lease.

A balancing allowance or balancing charge arises to the lessor by reference to the difference between the amount realised on disposal (market value) and the written down value of the asset.

The amount of the rebate of rentals, whether paid to the lessee, set against the cost of acquisition by the lessee of the leased asset or set against the cost of a new leased asset, represents a return of leasing charges already allowed for tax purposes to the lessee. It should be included in calculating the trading profits of the lessee for the basis period in which it arises. Since the rebate is a cash receipt (or equivalent, where set against the cost of a new asset) it should be included in calculating trading profit in all cases.

Example

Market Value of asset at end of lease (i.e. cost to lessee)	£5,000
Net final payment due by lessee to finance company	£ 500

The lessee should include the market value of the asset as a trading receipt for the period in which the transaction takes place and claim capital allowances by reference to the cost of the asset i.e. £5,000. The lessee is entitled to a deduction for the final payment to the finance company i.e. the net amount on which the lessee is taxable is £4,500:

Final payment made by lessee (balance owing on lease)	£ 500
Rebate of rentals i.e. market value of asset (£5,000)	

Net amount to be included in calculating trading profits (£4,500)

Treatment of trade-ins/up-front payments

A trader may wish to finance only part of the cost of an asset by way of finance lease. The balance of the cost is met either by way of:

- ❖ An up-front payment made by the lessee to the supplier of the asset
- or
- ❖ Trade-in of an existing asset including a leased asset (both are referred to hereafter as up-front payments).

The lease agreement will generally show the up-front payment as an initial payment made under the lease.

For tax purposes, the lessor qualifies for capital allowances on the full cost of the asset.

As indicated above the initial lease payment under the lease or an up-front payment made by the lessee is regarded as an advance payment of leasing charges. The lessee is allowed to write off the payment over the period of expected use of the asset by the lessee. In general, this is taken as the primary period of the lease.

Example

Leased Asset cost	£25,000
Up-front payment paid by lessee to supplier	£10,000
Total payable to finance company including finance charges	£20,000

Payable under finance lease:
Up-front payment of £10,000 plus £5,000 per annum over 4 years (primary period)

The lessee is allowed the annual amounts payable under the new finance lease plus £2,500 per annum in respect of the up-front payment.

Payable under finance lease £5,000
Up-front payment spread £2,500
Total Allowed to lessee/charged on lessor £7,500

Note

In practice, lessees frequently seek to deduct the up-front payment in the year in which the lease is taken out i.e. in the above example they claim £15,000 for year 1 (i.e. up-front payment of £10,000 and first annual payment of £5,000) and £5,000 for each subsequent year.

This is incorrect.

Trade-in of asset on lease

Where the leased asset is traded-in against another leased asset, the market value of the trade-in is in effect a rebate of rentals already paid and should be treated as a trading receipt of the lessee for the period in which the trade-in takes place. This amount will be treated as an up-front payment and dealt with accordingly.

Example

A leased asset is traded-in for £5,000 against a replacement asset which is leased for a primary leasing period of 4 years @ £7,000 per annum. At the time of the trade-in the leasing company is owed £500 on the leased asset. The lessee should include the amount realised on trade-in (£5,000) as a trading receipt and claim a deduction for this amount over the primary leasing period. The net amount to be claimed by the lessee in year 1 of the new lease is:

Rebate of rentals (net) (i)	(£4,500)
Leasing charge for new asset	£7,000
Up-front payment (trade in £5000 x 25%)	£1,250
Allowable (ii)	£8,250

Net amount allowable
Year 1 (ii) less (i)

(continued on page 18)

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Revenue Policy Statement

The text of a policy statement issued by Revenue in 1981 is given on page 20. It was issued in an attempt to counter tax avoidance devices which were in operation in the leasing sector. Although tax avoidance was not confined to vehicle leasing, it was particularly apparent in this area.

As a result of the statement of Revenue Policy the practices to which it referred have more or less ceased and the LADCO arrangements discussed below, have been adopted to facilitate the disposal of leases assets.

LADCO transactions

In recent years, Revenue has agreed with the Irish Finance Houses Association certain procedures known as LAD - leased asset disposal) to be adopted by leasing companies for end of lease transactions. The procedures are acceptable for income tax, corporation tax and VAT purposes.

The transactions involve the use of a special purpose company set up under the auspices of the Irish Finance Houses Association called the Leased Asset Disposal Company (LADCO). The transactions can be summarised as follows:

- ❖ The leasing company invoices LADCO for the sale of the asset i.e. the leasing company sells the asset to LADCO. The sale must be at market value
- ❖ Where the lessee wishes to acquire the asset, LADCO invoices the lessee for the asset i.e. LADCO sells the asset to the lessee
- ❖ The lessor issues a rebate of rentals credit note to the lessee. The rebate usually equates with the bulk of the sale consideration.

To reverse the disposal e.g. where a mistake has been made or at the request of the lessee, the following transactions take place:

- ❖ The lessor issues LADCO with a credit note for the asset
- ❖ LADCO issues a credit to the lessee for the asset
- ❖ The lessor issues a cancelling reversal of rebate invoice to the lessee.

Standard invoicing documentation is used to give effect to these transactions.

Early Settlements

An early settlement of a lease usually involves payment of a sum by the lessee to the lessor in order to settle the lease early. The sum paid will be an amount which at least adequately compensates the lessor for any cost to him of the early settlement of the lease. The circumstances in which early settlements may occur include emigration or death of a lessee. Where the lessee has sufficient funds, he may wish to settle the lease with a lump sum. The early settlement of a lease should not result in the lessee gaining legal title to the leased asset. (In general, if there is any arrangement whereby the lessee can acquire the asset the lease will be treated as a hire purchase transaction.)

Where there is a genuine change in the intentions of the lessor and the lessee which was not envisaged at the start of the lease Revenue continue to treat the arrangement as a lease rather than a hire purchase transaction.

Capital Gains Tax

Under Section 18 Capital Gains Tax Act 1975, gains on the disposal of assets which are tangible moveable property and which are wasting assets, are exempt from CGT. The exemption does not extend to the disposal of such assets if, for the period of

ownership of the person making the disposal, they are used solely for the purposes of a trade or profession and that person has or could have claimed capital allowances in respect of expenditure attributable to the asset - Section 18(2) Capital Gains Tax Act 1975.

As most leased assets are precluded, by virtue of Section 18(2), from the Section 18(1) exemption, a CGT charge can arise on the disposal of such leased assets. A disposal occurs, where at the end of the lease period the asset is sold by the lessor to LADCO. There is a further disposal where the asset is sold either to the lessee or to a third party.

Where the formerly leased asset is acquired by the lessee, the cost of the asset for CGT purposes is the amount for which the asset is sold to the lessee (i.e. market value), before deducting any amount in respect of rebate of rentals. The lease rentals paid by a lessee for the lease of an asset are not payments to acquire ownership of the asset. They are simply payments for the use of the asset.

Lease Termination - Income Tax / Corporation Tax returns already submitted

Tax practitioners may have been unsure as to the correct treatment of lease termination transactions outlined in this article. Where lease terminations have been dealt with incorrectly in a return of income for the years 1994/95 and subsequent years, the taxpayer will be treated as having corrected the error without unreasonable delay **provided the error is corrected before the end of February 1997.** (Section 48(1)(b)(ii) Finance Act 1986 refers).

In general, Revenue will not reopen 1993/94 and prior years because of an alteration arising from this statement unless the amounts involved are material.

VAT and Leasing

The VAT treatment of leasing transactions in the hands of a VAT registered lessee is illustrated in the following examples.

The examples refer only to commercial vehicles and other assets in respect of which the lessee is entitled to a VAT credit. A lessee is not entitled to a VAT credit in respect of the leasing or purchase of passenger motor vehicles. Such transactions have no VAT implications and should be excluded from VAT returns.

Example 1 Trade-in of asset against new leased asset

A VAT registered person trades-in an old van for £5,000 plus VAT against a new van (cost £16,000 plus VAT). The balance of the cost of the van is being met by finance lease. The example deals with the cases where the van is:

- ❖ owned by the lessee
- ◆ leased by the lessee under a finance lease.

❖ Old van not on lease:

Lessee issues VAT invoice to dealer for old van;

Invoice

To Dealer
From Lessee

Old Van	£5,000
VAT @ 21%	<u>£1,050</u>
Total due	£6,050

Lessee includes invoice in VAT return.

Finance company includes trade-in value in the finance lease as an initial lease payment. Lessee receives VAT invoice, for initial lease payments, from Finance company at commencement of lease and includes this invoice in VAT return. Lessee also receives VAT invoices for leasing charges as they are invoiced by the Finance company.

◆ Old van on lease; £2,000 owing on lease to 'old' finance company.

Since lessee does not own old van, the trade-in is not directly reflected in the VAT returns. Old Finance company issues credit note to lessee.

Credit note

To Lessee
From Old Finance company

Old Van (sale price)	£5,000
Less: Rentals owing	<u>£2,000</u>
Balance	£3,000
Less: commission (say 5%)	<u>£150</u>
Credit Note	£2,850
VAT @ 21%	<u>£598.50</u>
Total Credit note	£3,448.50

Lessee reduces input credits by VAT per credit note.

New Finance company includes amount of credit note in new lease as an initial lease rentals and issues VAT invoice to lessee for initial lease rentals (including VAT). Lessee claims credit for VAT on initial lease rental in period in which invoice received.

Example 2 Disposal of leased asset at end of lease

A van, which had been financed by finance lease is worth £8,000 plus VAT at the end of the primary period. There are no leasing charges owing on the van. The example deals with the cases where the van is:

- ❖ Acquired by the lessee and
- ◆ Not acquired by the lessee, who leased the van under a finance lease

❖ Van acquired by lessee i.e. Indirect Disposal to lessee via LADCO

Finance company issues credit note to lessee. LADCO, which has acquired the van from the Finance company issues VAT invoice to lessee for market value of the van.

In practice, both documents are incorporated into one composite invoice/credit note, which is issued by Finance company.

Credit note

To Lessee
From Finance company

Rebate of rentals	£8,000
Less: commission (say 5%)	<u>£400</u>
Net rebate	£7,600
VAT @ 21%	<u>£1,596</u>
Total (incl VAT)	£9,196

Invoice

To Lessee
From LADCO

Van @ market value	£8,000
VAT @ 21%	<u>£1,680</u>
Total (incl VAT)	£9,680

Net Amount due (£9,680 - £9,196) £484

Lessee pays settlement amount to Finance company (£484); lessee reduces input credit by the VAT per the credit note (£1,596) and claims input credit for VAT on acquisition of van from LADCO (£1,680).

◆ Van not acquired by lessee

Lessee surrenders the van to the leasing company. Leasing company issues credit note to lessee for a rebate of rentals (reflecting the lessee's 'equity' in the asset) for market value of van less a small commission.

Credit note

To Lessee
From Finance company

Rebate of rentals	£8,000
Less: commission (say 5%)	<u>£400</u>
Net rebate	£7,600
VAT @ 21%	<u>£1,596</u>
Total (incl VAT)	£9,196

Lessee reduces input credit by the VAT per the credit note (£1,596).

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Revenue Policy on Vehicle Leasing (Statement issued in 1981)

1. Vehicle leases usually run for a specified number of years, and the rentals payable take into account an estimate of the market value of the vehicle at the end of the lease. Under contracts of this kind the vehicle is normally sold on the open market at the end of the lease and any excess or shortfall of the sale proceeds over or below the anticipated residual value on which the rentals were based leads to an adjustment of the rental payments. The tax effects of such leases normally raise no problems. By the end of the lease the lessor has been allowed tax relief for the actual depreciation he has borne, taking into account the net proceeds of the sale of the vehicle. The lessee qualifies for relief on the net rentals he has paid, taking into account any rebate he receives, or any shortfall he has to pay, on the disposal of the vehicle.
2. The leases with which this statement is specifically concerned involve some variations from the traditional provisions of vehicle leases described at 1 above. Rentals may be calculated by reference to a residual value which is lower than the expected open market value of the vehicle at the end of the lease. The vehicle, on the termination of a primary leasing period, is either then re-leased back to the lessee at very much reduced rental rates or disposed of for less than market value to a nominee of the lessee who acquires the vehicle for less than full and adequate consideration. In some cases the residual value of the vehicle used in calculating the rentals may be purely nominal or may be a conservative estimate of the market value. The lease itself may, in certain cases, provide for the sale of the vehicle to a nominee of the lessee, or the vehicle may pass through several hands before reaching the person connected with the lessee.
3. Taxation provisions not normally relevant to the leases described at 1 above may need to be considered in connection with leases of the kind referred to at 2 above. So far as the lessor is concerned, it may be appropriate to regard the transaction as a sale of stock-in-trade rather than the lease of an asset qualifying for capital allowances. If capital allowances are given, the provisions of Section 277(2) Income Tax Act 1967, may require the open market value of the vehicle to be brought into the taxation computation at the end of the lease rather than the sale proceeds. In certain circumstances the right of the lessor to claim wear and tear allowances may be in doubt, having regard to Section 241(5) Income Tax Act 1967, on the ground that the burden of the wear and tear did not fall directly on the lessor. The lessee's rental payments may be disallowed, in whole or in part, under Section 61(a) or Section 61(f) Income Tax Act 1967, as not being made wholly and exclusively for the purposes of the business or as being in part capital expenditure. The person connected with the lessee who acquires the vehicle may be liable under the provisions of Schedule E on any benefit he obtains.
4. Inspectors of Taxes will carefully examine leasing arrangements which are of the kind referred to at 2 above and will make such adjustments in assessments as may be considered necessary. Where a taxpayer cannot reach agreement with the Inspector of Taxes about his liability, the usual right of appeal will be available.

Statutory Requirement for VAT Invoices

Requirements to issue VAT invoices and account for VAT due within the proper time limits - Sections 17(1) and 19(2) VAT Act 1972.

Background

Following audits carried out on a number of cases involving persons providing professional services it was discovered that VAT invoices had not been issued within the proper time limits as laid down in the VAT Acts. This resulted in VAT not being accounted for to the Revenue Commissioners at the correct time.

Where such persons are not authorised to account for VAT on the cash receipts basis but are obliged to use the invoice basis, the **date of completion of the service** and the **date of issue of the invoice** become very important. These dates determine when the VAT chargeable becomes due.

Correct Procedures

This opportunity is being taken to remind practitioners and taxpayers of the need to issue invoices and account for VAT due within the required time limits:

- ❖ Where services are supplied to customers who are registered for VAT a VAT invoice must be issued within 15 days of the end of the month in which the service is completed. In such cases VAT becomes due on the date the invoice issues or if an invoice is not issued, VAT is due on the date when the time limit for the issue of such an invoice expires.
- ❖ Where services are supplied to customers who are not registered for VAT the tax becomes due on the date the service is completed.

Where the service consists of a single transaction there is no difficulty in determining when the service is completed. A service

consisting of several connected transactions will usually be regarded as having been completed when the last of the connected transactions is carried out.

Inspectors may request evidence to show that a service is still ongoing and has not, in fact, been completed.

Where an interim payment is received on an ongoing service, VAT becomes due immediately and a VAT invoice covering such payment must be issued within the prescribed time limit.

Conclusion

Where it is established that payment of VAT correctly due in a particular accounting period was delayed or is still outstanding, then Revenue will pursue collection of the liability by reference to the correct accounting period together with interest and penalties as appropriate.

VAT Purchase Records

Background

Section 16 of the VAT Act 1972 and Regulation 9 of the VAT Regulations 1979 impose an obligation on every taxable person to keep a full and true record of all transactions which affect, or may affect, their liability to tax. This legislation is merely reinforcing Article 22 of the Sixth EU Directive.

In relation to purchases Regulation 9 requires a taxable person to keep a record of purchases made showing:

- ❖ The amount of the relevant consideration
- ❖ The corresponding tax invoiced by the supplier
- ❖ The VAT rate applying
- ❖ A cross reference to the corresponding invoice or other record of purchase available.

Invoices paid

The most common method of recording purchases is the “creditors” system which logs purchases as they are invoiced and enables the taxpayer to reclaim any VAT on such purchase invoices, despite the fact that the invoices might not be paid for some time. However, a purchases system based on “invoices paid” would be completely acceptable. The cheque payments book or other record of payment must be suitably analysed to show separately the VAT exclusively values and the VAT at the appropriate rates of all purchases for resale and not for resale. These should be cross referenced to the relevant purchase invoices. Where invoices were part paid, then only the correct proportion of the VAT included in the payment could be reclaimed.

Such system would, of course, involve a cash flow loss to the taxable person who could not reclaim VAT until it had been paid. However, it could be of interest to a small business who would be saved the trouble of keeping a VAT purchase book.

Revenue view

Revenue would have no objection to a taxable person changing their basis of reclaiming VAT to an “invoices paid” system providing it is done correctly with no duplication of VAT credit. Obviously at the time of changeover the VAT on invoices previously reclaimed under a “creditors system” could not be claimed again under a “payments system”.

Telephone Numbers

The switchboard telephone number for the Offices of Computer Branch and Special Enquiry Branch, 3rd Floor, Setanta Centre, Nassau Street, Dublin 2 is now **(01) 671 0588.**

Correction

The article on Special Portfolio Investment Accounts in **Tax Briefing**, Issue 23 contains an error.

In the paragraph on Share Options (page 18), the last sentence reads “... *sum of money does come within...*”

It should read “... *sum of money does **not** come within...*”

Any inconvenience caused is regretted.

Payment of Tax

A substantial number of cheques in settlement of routine tax demands are being sent directly to tax offices. Practitioners are requested to remind their clients that all cheques should be sent to the Collector-General's Office unless the payment is being made following a request by a Local Collection Office or the Inspector's Office in which event the payment should be sent to the Local Collection or Inspector's Office as appropriate.

The Collector-General's address to which the cheque should be sent will be shown on the tax demand or return envelope.

Revenue Statement of Strategy 1997-1999

The Minister for Finance, Mr. Ruairi Quinn, T.D., launched Revenue's Corporate Plan for the next three years on 25 November 1996.

The Plan builds to a great extent on what has been done in the course of the first Corporate Plan, which covered the period 1994-1996.

Third Party Returns - Form 46G

Form 46G has, in recent years, issued directly to taxpayers.

The development of and use of an Agents' File for the 1996/97 bulk issue of Returns will allow the Form 46G for 1996/97 (where it is relevant) to be issued with the 1996/97 Form 11. Both forms will therefore issue directly to practitioners in April 1997.

This will allow practitioners to identify those clients who have been issued with Form 46G and to retain copies of the information submitted for future reference.

Tax Briefing Index

Copies of the **Tax Briefing** Index, containing items of current/ongoing relevance, are now available.

Car Scrappage Scheme

Mr. Ruairi Quinn T.D., Minister for Finance, announced on 22 November 1996 that the £1,000 tax refund car scrappage scheme is to be continued. The scheme will continue for a further final year until **31 December 1997**, on the same terms and conditions as currently apply. The scheme was introduced for a limited period of eighteen months and had been due to expire on 31 December 1996.

Consolidation Project - Update

Work on consolidation is well under way and the project team is making good progress. The Finance Act 1996 contained a large number of measures amending the direct taxes code in order to facilitate the consolidation process. These measures rationalised some existing provisions, corrected inconsistencies and repealed spent provisions.

The 1997 Finance Bill will contain further preconsolidation measures. The drafting of the actual Consolidation Bill started in January 1996. The drafting process is scheduled to continue into 1997.

As of November 1996, 846 sections have been distributed to the referees for review and, as of the same date, 642 sections have been sent to the Parliamentary Draftsman's Office for consideration.

Revenue Information Leaflets

Income Tax

- IT 1** Allowances, Reliefs & Tax Rates
- IT 2** Taxation of Married Persons
- IT 3** Tax Free Allowances
- IT 4** Understanding PAYE Tax Tables
- IT 5** Refund of DIRT
- IT 6** Medical Expenses Relief
- IT 7** Deed of Covenant
- IT 8** Tax Exemption and Marginal Relief
- IT 9** One-Parent Family Allowance
- IT 10** Guide to Self-Assessment for the Self-Employed
- IT 11** Employees Guide to PAYE
- IT 12** Disabled Persons & Income Tax
- IT 13** Personal Injury Compensation Payments
- IT 14** [No Leaflet Prepared]
- IT 15** The Seed Capital Scheme:
Tax Refunds for New Enterprises
- IT 16** Third-Party Returns
(Automatic Return of Certain Information)
- IT 17** Special Savings Accounts and other
Special Investment Products
- IT 18** Incapacitated Child Allowance
- IT 19** Withholding Tax
- IT 20** Benefits from Employments
- IT 21** [No Leaflet Prepared]
- IT 22** Taxation of Disability and Short-Term
Occupational Injury Benefits
- IT 23** Main Features of Income Tax Self-Assessment
- IT 24** Taxation of Unemployment Benefit
- IT 25** Employees and Contractors in the
Construction Industry
- IT 26** Urban Renewal Relief
- IT 27** Tax Relief for Service Charges
- IT 28** Tax Relief for Designated Third World Charities
- IT 29** Tax Relief for Renewal & Improvement of
Certain Resort Areas
- IT 30** Relief for Expenditure on Approved Buildings
and Gardens in the State
- IT 31** Tax Relief for Tuition Fees paid to Private Colleges
- IT 32** Revenue Audit - Guide for Small Business
- IT 33** Tax Relief for Home Alarms
- IT 35** Blind Persons - Allowances & Reliefs
- IT 45** Allowances for Over 65's
- IT 46** Dependent Relative Allowance
- IT 47** Incapacitated Person -
Allowance for Employing a Carer
- IT 48** Starting in Business
- IT 49** VAT for Small Businesses
- IT 50** PAYE/PRSI for Small Employers

Capital Gains Tax

- CGT 1** Guide to Capital Gains Tax
- CGT 2** CGT - Self Assessment
- CGT 3** Roll-over Relief for Individuals on disposal of
certain shares

VAT

- IT 49** VAT for Small Businesses
Guide To Value-Added Tax
VAT Treatment of Second-Hand Goods

Capital Acquisitions Tax

- CAT 1** Gift Tax
- CAT 2** Inheritance Tax
- CAT 3** Probate Tax
- CAT 4** Capital Acquisitions Tax Business Relief
- CAT 5** Agricultural Relief - 1995 Finance Act
- CAT 6** Review and appeal procedures
- CAT 7** Elderly Brother/Sister Residence Relief
- CAT 8** Heritage Property Relief
- CAT 9** Tax Reliefs for Business

Residential Property Tax

- RP 1** Residential Property Tax Self-Assessment Return
- RP 2** Notes on Residential Property Tax
- RP 3** Residential Property Tax Help Leaflet
- RP 4** Review and Appeal Procedures
- RP 5** Residential Property Tax Certificate of Clearance

Stamp Duty

- SD 1** Stamp Duty
- SD 2** Stamp Duty Relief on Transfers of Land to
Young Trained Farmers
- SD 3** Review and Appeal Procedures

Customs & Excise

- C&E 2** Persons Transferring Residence to Ireland
- C&E 3** Customs and the Single Market
- C&E 4** Customs Information for Travellers
- C&E 5** Appeal Procedure relating to Customs Matters
- C&E 6** Appeal Procedure relating to Payment of Excise Duty
- C&E 7** Paperless Declaration (Customs AEP System)

Vehicle Registration Tax

- VRT** Vehicle Registration Tax - £1,000 Repayment
- VRT 1** Vehicle Registration Tax
- VRT 2** Vehicle Registration Tax - Temporary Exemption
- TCU 1** Binding Tariff Information (BT1)

Charities/Residence

- RES 1** Explanatory leaflet on the legislative provisions
relating to the residence in Ireland of individuals
for tax purposes
- CHY 1** Applying for Relief from Tax on the Income &
Property of Charities
- CHY 2** Applying for Relief from Income Tax &
Corporation Tax for Certain Sporting Bodies
- CHY 3** Tax Relief for Covenantors
(for teaching the Natural Sciences)
- CHY 4** Tax Relief for Covenantees
(for teaching the Natural Sciences)
- CHY 5** Tax Relief for Covenantors
(for the Conduct of Research)
- CHY 6** Tax Relief for Covenantees
(for the Conduct of Research)
- CHY 7** Trading by Charities - Exemption from Tax

Collector-General

- CG 1** Tax Clearance Scheme
- CG 2** Due Dates Payments and Returns
- CG 3** Payments to the Collector-General
- CG 4** Change of Address
- CG 5** Vat Claims and Payments
- CG 6** P35 - End of Year Returns

Direct Debit VAT
Direct Debit PAYE/PRSI
Direct Debit Preliminary Tax - Income Tax

Other Leaflets/Guides

- HET 1** Relief for Donations of Heritage Items

Artists' Exemption

Employer's Guide to PAYE (Edition 7 - March 1994)

- IT 50** PAYE/PRSI for Small Employers

Supplies

Supplies of all leaflets may be obtained from the
Revenue Forms & Leaflets Service at (01) 878 0100