

Acquisition, disposal and enhancement costs (S.552)

Part 19-02-10

This document should be read in conjunction with section 552
of the Taxes Consolidation Act 1997

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Introduction

Section 552 of the Taxes Consolidation Act 1997 (“TCA 1997”) provides the basic rules for determining the expenditure to be allowed in computing chargeable gains. Allowable expenditure includes cost of acquisition of an asset, enhancement expenditure incurred during the period of ownership of the asset and costs incurred in disposing of the asset.

10.1 Allowable expenditure

Allowable expenditure is divided into the following categories:

- (a) Cost of acquisition, i.e., the consideration which was given wholly and exclusively for the acquisition of the asset, plus the incidental costs of acquiring the asset; or, if the disposer created the asset (e.g., copyright or the goodwill of a business), the expenditure he or she incurred in creating it.
- (b) Additional expenditure, i.e., expenditure incurred to add to the value of the asset, in so far as the expenditure is reflected in the state or nature of the asset at time of disposal; and expenditure to establish or maintain legal title to the asset, or an interest in or right over it.
- (c) Incidental costs of disposal (restricted as in **para 10.5**).

10.2 Additional expenditure

To come within the first category of (b) of **para 10.1**, expenditure must not have proved futile or have wasted away before disposal.

Example 1

In 1995/96 X buys for €30,000 (including expenses) a plot of land (not being part of a garden within Section 604) and lays out on it a tennis court at a cost of €10,000. In 1999/00 X does away with the tennis court and builds in its place a swimming pool at a cost of €20,000.

In 2020 X sells the land for €300,000 (after deduction of expenses). The €10,000 which X spent on the tennis court is not allowable because it is not reflected in the state of the land on its disposal.

The computation is as follows:

Sale price (net)				€300,000
Allowable expenditure				
Cost of land	€30,000	x	1.277 (indexation)	= €38,310
Cost of swimming pool	€20,000	x	1.193 (indexation)	= €23,860
				<u>(€62,170)</u>
Chargeable gain				€237,830

(The demolition of a tennis court is not the "entire loss, destruction, dissipation or extinction of an asset" within **section 538(1) TCA 1997** because it is not an "asset" being only part of an asset (the land); and it is not within **section 538(3) TCA 1997** (see [Tax and Duty Manual Part 19-01-09](#)) because it is not a building or a structure in the nature of a building.)

10.3 Demolition costs

It may be accepted that demolition costs are permanently reflected in the state of the land by the absence of the demolished building. In practice, the sole test of allowability is whether the purpose in incurring the expenditure was to enhance the value of the asset. Where, for example a building is erected in a garden and is subsequently removed and the garden reinstated, neither the cost of the building nor of its removal will normally be allowable. Where, however, the cost of demolition is small in relation to the cost of constructing a new building (as, for example, the cost of demolition of the tennis court in **para 10.2**), no adjustment need be made.

10.4 Expenditure and dilapidation

Expenditure incurred in repairing and putting into a fit state for letting a property acquired in a dilapidated condition is normally inadmissible as a deduction under Case V of Schedule D. For Capital Gains Tax ("CGT") purposes, however, such expenditure (including expenditure on decorations) may, in general, be regarded as allowable expenditure under **section 552(1) TCA 1997**.

10.5 Allowable incidental costs

The "incidental costs" of acquisition and disposal are defined in **section 552(2) TCA 1997**. The definition is exhaustive, i.e., no other expenditure is allowable.

Allowable "incidental costs" are limited to:

- (a) Fees, commission or remuneration paid for the professional services of any surveyor, valuer, auctioneer, accountant, agent or legal adviser so far as the expenditure is wholly and exclusively incurred for the purposes of the acquisition or disposal.
- (b) The costs of transfer or conveyance (including Stamp Duty) and the cost of advertising to find a seller or buyer.
- (c) The costs reasonably incurred in making any valuation or apportionment required for the purpose of computing the chargeable gain or allowable loss. See, however, **para 10.8** regarding the costs of appeals on questions of market value.
- (d) The costs of legal and actuarial services including Stamp Duty on transfers and ancillary expenses incurred in varying or ending a settlement (see *C.I.R. v Chubb's Trustee*, 1971 47 T.C. 353) or upon the termination of a life interest in possession. The allowable expenditure may include fees in respect of discharges, withdrawal fees and commission on transfer of assets to beneficiaries (but not insurance premiums) and, when necessary, should be apportioned between chargeable and non-chargeable assets by reference to value.

If the costs of transfer, etc., have been borne by the person to whom the property is transferred, he or she may either be allowed a deduction for these costs or he or she may forego a claim and permit the trustees to treat these costs as an allowable deduction in computing their chargeable gain arising from the deemed disposal.

- (e) Any part of a liquidator's expenditure which has been wholly and exclusively incurred in disposing of a company's assets. A liquidator is normally a professional person e.g. an accountant, and in his or her capacity as liquidator may pay himself or herself fees for professional services. Insofar as it can be shown that such fees (or part thereof) have been wholly and exclusively incurred in disposing of a company's assets, such fees may be included in the part of the liquidator's expenditure ranking as an allowable deduction. Where the actual expenditure on specific assets cannot be identified, a reasonable apportionment may be made.

10.6 Professional advisers

Fees paid to a professional adviser are allowable only to the extent that they are directly referable to the cost of acquiring or disposing of each particular investment. To the extent that the fees are referable to advice about the general state of markets or the prospects of particular forms of investment or the management of a portfolio, they are not allowable.

Amounts in respect of subscriptions for periodicals or for publications by analysts, stockbrokers or other professional advisers, whether for public or private circulation, or other similar types of expenditure, are not allowable.

Accountants' fees are allowable only to the extent that they refer to the ascertainment of market value of the assets or to any apportionment for the purposes of the computation. Otherwise, fees for the computation of liability are not allowable. It follows that, in the case of quoted securities, allowable accountancy fees will usually be very small.

10.7 Interest and companies

Where a company finances building work out of borrowed money, and charges the interest on that money to capital, then, except in so far as such interest has been taken into account for the purposes of relief under the Income Tax ("IT") Acts, or could have been so taken into account but for an insufficiency of income or profits or gains, the expenditure qualifying for allowance under **section 552 TCA 1997** is to include any such interest in respect of the time up to the disposal.

10.8 Costs of appeals

The costs of appeals (or contributions thereto) on questions of market value should not be treated as allowable expenditure.

10.9 Mortgage arrangement fees

Fees of building societies, solicitors and valuers and any other costs of arranging a mortgage or other loan in connection with the acquisition of an asset should not be treated as allowable expenditure.

10.10 Insurance premiums

Premiums paid under a policy of insurance against risk of damage to or depreciation of the asset are not allowable expenditure.

10.11 Expenditure reimbursed out of public money

Under **section 565 TCA 1997**, no allowance should be given for any expenditure otherwise allowable which is met by the State or by any government, by any board established by statute or by any public or local authority, whether in the State or elsewhere.

10.12 Foreign Tax

Foreign tax on the disposal of an asset is allowable expenditure to the extent that the tax does not qualify for double taxation relief (see **section 828 TCA 1997**).

10.13 CGT and Value Added Tax (“VAT”)

Where a chargeable asset is acquired otherwise than as an asset of a trade, the cost for CGT purposes should be the cost inclusive of any VAT borne on the purchase. Where, however, the asset is acquired as an asset of a trade and the VAT borne on it is part of the trader's deductible "input tax", the cost, where relevant for capital gains purposes, should be the cost exclusive of VAT.

10.14 CGT and Capital Acquisitions Tax (“CAT”)

Neither Inheritance Tax nor Gift Tax (both components of CAT) is an allowable deduction in arriving at a chargeable gain. In an appeal before the Circuit Court in November 2008, the taxpayer's grounds of appeal were that Inheritance Tax was –

- Part of the incidental costs of acquiring the asset,
- Expenditure wholly and exclusively incurred in establishing the person's title to the asset,
- Costs incidental to the making of the disposal.

The decision upheld Revenue's long-standing view that CAT (Inheritance Tax) is not a deductible cost for CGT.

The same treatment should be given to Gift Tax.

10.15 Foreign currency

The cost of an asset acquired in a foreign currency is to be translated into the currency of the State, at the rate in place at the time of acquisition, for the purposes of the computation of CGT liability on its subsequent disposal.

10.16 Assets are deemed to have been sold and reacquired

Where, for the purpose of computing chargeable gains, assets are deemed to have been sold and immediately reacquired (e.g., where liability is based upon market value at 6 April 1974) no incidental notional expenditure, such as would have been incurred in actual transactions (e.g., transfer fees), should be allowed.

10.17 Unapproved Share Option Schemes

For CGT purposes, the allowable cost of shares that have been issued to an individual under an unapproved share option scheme has been, under current interpretation, the sum of the following:

- (a) The cost (if any) of the option [**section 540(4) TCA 1997**] – see **Note 1**
- (b) The price paid for shares on exercise of the option [**section 552(1) TCA 1997**] – see **Note 2**, and
- (c) The amount charged to IT on the exercise of the option (**section 128 TCA 1997**).

The decision of the UK Court of Appeal in the case of *Mansworth v Jelley* ([2003] STC 53) has raised doubts about our current interpretation.

Note 1: Whereas, in practice, both the cost of an option and its market value at the time it was acquired are usually nil, strictly speaking, it is the market value of the option that should be taken into account since the option is acquired in consideration for or in recognition of the individual's services in an office or employment - see **section 547(1)(c)(iii) TCA 1997**.

Note 2: By virtue of **section 547(3) TCA 1997** the market value rules in **section 547(1) TCA 1997** do not apply where there is no corresponding disposal and the acquisition is at less than market value. This is generally the case where shares are issued on the exercise of a share option.

The *Mansworth v Jelley* case was concerned with the allowable cost for CGT purposes of shares acquired on the exercise of an option that had been granted to the taxpayer concerned by reason of his employment. The option was granted when the taxpayer was not UK resident and exercised when the taxpayer was UK resident. The shares in question were shares already in existence i.e. they were not newly issued shares. On acquiring the shares, the taxpayer immediately sold them on.

HM Revenue and Customs raised capital gains assessments on the taxpayer on the basis that the allowable cost of the shares was the sum of:

- (a) The market value of the option at the time of grant; and
- (b) The price paid for the shares on exercise of the option.

Under UK practice, the taxpayer was not liable to an IT charge on exercise of the option since it had been granted at a time when he was not resident. Since it was agreed that the option was granted in consideration of the taxpayer's services in his employment the market value of the option replaced its actual cost under the UK equivalent of our **section 547(1)(c)(iii) TCA 1997**. In any event, in this case both the cost of the option and its market value were nil.

However, the UK Court of Appeal determined that the allowable cost of the shares to be used in the computation of gain on their disposal was their market value at their time of acquisition - the value (if any) of the acquisition of the option was irrelevant. This meant that the taxpayer had no gain on disposal of the shares since the shares were disposed of immediately after their acquisition on exercise of the option. In brief, the Court's reasoning was that the transaction under which the taxpayer had acquired the shares was a single transaction comprising both the acquisition of the option and its exercise and that that single transaction was an acquisition by reason of the taxpayer's employment. Therefore, the market value rule applied since as the shares were not newly issued shares the equivalent of our **section 547(3) TCA 1997** was not relevant.

Having considered *Mansworth v Jelley*, **Revenue does not propose to treat the amount charged to IT as part of the cost of acquiring the shares**. The base cost, for CGT purposes, of shares acquired on the exercise of an option under an unapproved share scheme should be calculated as follows:

Where the shares are issued on the exercise of the option:

Regardless of when the options were exercised, the cost of acquisition is the sum of the following:

- (a) The cost (if any) of the option,
- (b) The price paid for shares on exercise of the option and
- (c) The amount charged to income tax on the exercise of the option.

Where the shares are already in existence at the time of exercise of the option:

For options exercised before 12/12/2002, the cost of acquisition is the sum of the following:

- (a) The cost (if any) of the option,
- (b) The price paid for shares on exercise of the option, and
- (c) The amount charged to IT on the exercise of the option.

For options exercised on or after 12 December 2002, the cost of acquisition is the market value of the shares at the time of exercise of the option.

Example 2

An individual, by virtue of his or her employment, is granted share options under an unapproved share option scheme. The value of the options at time of grant is nil. A few years later the individual pays €10,000 in exercise of the options and acquires shares worth €15,000. The individual immediately sells on the shares for €15,000.

Shares issued on the exercise of the option or already in existence and option exercised before 12 December 2002:

Disposal proceeds		€15,000
Less		
Costs of acquisition:		
Cost of shares at time of acquisition	€10,000	
Amount charged to IT	€5,000	
	<u> </u>	€15,000
Capital gain		NIL

Shares in existence and option exercised on or after 12 December 2002:

Disposal proceeds		€15,000
Less		
Costs of acquisition:		
Market Value of shares at time of acquisition:	€15,000	
Capital gain		<u> </u> NIL