

PUBLIC POLICY AND TAXATION REPUBLIC OF IRELAND

**Professional 2 examination
June 2004**

MARKING SCHEME

Question 1

- (a) PR-STV means proportional representation by the single transferable vote. Each constituency returns three to five candidates. The elector can vote for all of the candidates, listing them in order of preference. A quota is worked out by the following formula.

<u>Total valid poll</u>	+1
Number of seats	+1

When a candidate reaches the quota, he or she is elected. The surplus of the candidate's votes above the quota is then allocated to the other candidates, according to the preferences on the paper.

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- (b) The classic case against proportional representation, based on case studies of Weimar Germany and Italy in the 1950s, is that it leads to a proliferation of parties and thus to political instability. The canonical statement on the effects of PR has been uttered by Sartori: 'PR formulas facilitate multi-partyism and are, conversely, hardly conducive to two-partyism'. The problem is that this implicitly equates two-partyism with stability. If there is strong party discipline, as in the case of Fianna Fail, the biggest political party in Ireland, this may not be the case. Where PR-STV may contribute to political instability is through an increase in politically independent candidates on whose support minority governments may rely.

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NB: There are many other arguments that students may come up with in addition to the above. Full credit should be given for all plausible arguments, the maximum available mark is 8.

- (c) This question should be answered in three stages. First of all, the student should clarify what is it that TDs do? Their role has often been characterised as that of 'going around persecuting civil servants' in order to resolve difficulties brought to their attention by constituents. There is agreement that TDs spend much of their time engaged in work for their constituents, although there is disagreement about how effective this is.

Some believe that the lack of interest in a legislative role arises from executive pre-dominance. In line with the 'Westminster' models of government, parliament is little more than a 'glorified rubber stamp' where the government may feel obliged to justify legislation but, if assured of its majority, can treat this process in a pretty perfunctory way. The consequence is opposition members feel that they can have no real role and government backbenchers are little more than a supporting chorus for the government.

Others argue that the electoral system is often thought to be the cause and disengagement from Parliament the consequence. Whilst PR-STV increases competition, it doesn't explain why people approach their TDs in the first place. Also, this explanation would imply that changing the electoral system would reduce the demand from the public, yet the case of Belgium, with its list system shows that this is not the case. It is likely that the public demand for brokerage is as much a result of cultural forces than weak political structures.

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NB: There are many other arguments that students may come up with in addition to the above. Full credit should be given for all plausible arguments, the maximum available mark is 13.

Question 2

- (a) (i) The European Court of Justice provides an overarching framework of jurisprudence in relation to EU law. It deals with litigation both in cases referred via national courts and those that are brought directly before it. 2
- (ii) The Council of Ministers is legally one body where the appropriate national ministers meet to decide on Commission proposals that fall within their remit at national level. 2
- (iii) The European Parliament is the representative institution of the Union. It does not produce laws in the sense of a typical parliament but casts its views on legislative proposals. It is able to amend or reject draft laws and can dismiss the Commission by a 2/3 majority of its members. 2
- (b) Upon accession to the then European Economic Community, agricultural products rose 35% in price and policy lay in maximising CAP prices and support. The number of small-scale landholders remained stable, so that total disposable income increased faster than on larger farms. This counters the myth of rural immiseration and prevented an urban-rural divide. However, this developed may not have served consumers of agricultural products very well. 5

In industry many firms suffered import penetration - this resulted in the partial collapse of indigenous industry. Subsequently, in the 1980s, national debt stood at 120% of GDP, and unemployment at 17% of labour force. There is argument that industry underestimated effects of entry upon to EU but that simply exposed rather than caused weaknesses. The companies that survived were more efficient. These more efficient firms capitalised on the moves towards the single European market that were beginning to attract inward investment. The internal market also provided greater opportunities and benefited consumers through the more rigid enforcement of competition policy. 5

NB: There are many other arguments that students may come up with in addition to the above. Full credit should be given for all plausible arguments, the maximum available mark is 10.

(c) **Issues around Enlargement of the European Union**

Each response should have a maximum of three marks. 3

Agriculture: Accession countries, commonly known as Central and Eastern European Countries (CEEC), rely on agriculture to a much greater extent than the EU. Output and productivity is low, capital is lacking and standards are below the EU. Enlargement will create pressure for CAP reform, particularly in the area of price supports - will there be a levelling up or down? If it is down, will there be compensatory price supports cuts? Will there be direct payments for the CEEC? It is thought that pre-accession aid of €500m per annum may be necessary.

Social policy and labour markets: Concerns that disparities in wealth will create pressures for internal migration. Yet similar concerns were expressed when Spain and Portugal joined, but rising living standards pre-empted large scale migration. CEEC will be concerned that upgrading health & safety and social legislation will render them uncompetitive but not readjusting could be perceived as social dumping.

Migration: Currently the accession countries are acting as a buffer zone, leaving Europe less insulated from unwanted migration. Access to regular immigration channels to EU will remain limited. Asylum is one of the few viable options for immigrants and refugees alike. Urgent need to standardize procedures. The question is will they be minimalist?

Economic: There is a fear that enlargement threatens to reduce the scale of foreign direct investment into Ireland. There may be some loss of employment, especially in labour-intensive industries. But Ireland is attempting to move away from these sectors anyway. However, the candidate countries have a combined population of over 100 million, making an expanded EU the largest developed market in the world.

NB: There are many other arguments that students may come up with in addition to the above. Full credit should be given for all plausible arguments, the maximum available mark is 9.

Question 3

- (a) This is said to be made up of three areas:
1. Governance- the manner in which parliament exercises oversight in relation to public service 2
 2. Policy-making – the manner in which ministers develop policy in a resource-constrained environment 2
 3. Public management – the manner in which civil servants implement the policy concerns of ministers 1
- (b) A problem with the SMI is that it takes policy as a given and focuses on how best to achieve the ends of this policy, an essentially technical question. This is a common feature of public sector reforms, the reduction of the political to the technical. It neglects how policy objectives are formulated and decided upon, how these objectives are translated into action by civil servants, and how these arrangements are supervised in the public interest. The result of this neglect is that political intent, the wishes of the government, and strategic delivery, the work of civil servants are divorced from each other. Consequently, civil servants believe themselves to be working with an ambiguous policy direction. Furthermore, the level of detail required to assess the performance of civil servants – the governance factor - is not always present. PA consulting found that such assessment was dependant on 'a certain definition and clarity' about outputs that was not always present. 10
- (c) Greater evidence of planning on the part of the executive so that political intent could be matched with departmental strategy. 2 ½
- Greater connection of departmental strategy and resources through multi-annual budgeting. 2 ½
- Greater delegation of authority to Secretary Generals to manage staff. 2 ½
- Greater emphasis on outcomes the attainment of which will be assessed by Parliament. This would signify a move away from the traditional approach of measuring outputs. 2 ½

Question 4

(a) Industrial Buildings Allowance

Industrial buildings capital allowances => 4%
 Different rates for tax incentive areas

1/10/02 purchase buildings	180
purchase land	<u>120</u>
Total	300

Previous owner cash allowances

1//E 97 – 01 => 5 years
 annual allowance 160,000 x 4% => 6,400 x 5 => 32,000

	In €
Sales proceeds	180,000
TWDV	128,000
B. Charge	52,000
Restricted to	32,000

Residue (TWDV + BC) => 128,000 + 32,000 => 160,000
 Useful life remaining => 20 years
 Annual CAs => 160 / 20 => €8,000

Schedule D Case 1 Loss (initial)	258,320
l B. Capital allowance	<u>8,000</u>
Adjusted Case 1 Loss	266,320

(b) Chargeable Gain

Part Disposal

		€
2003	Sales Proceeds	20,000
96/97	Cost	
	$17,500 \times \frac{20}{20 + 30} = 7,000$	
	Index Factor 1.251	<u>8,757</u>
	Gain	11,243
	Capital Loss b/forward	<u>12,758</u>
	Assessed Gain	0
	Capital Loss c/forward	1,515

(c) Schedule D Case IV

02 Receivable 21,150 – 4,430 + 3,980 => 20,700 / 80% => 25,825
 03 Receivable 16,680 – 3,980 => 12,700 / 80% => 15,875
 Standard Rate D.I.R.T => 20%
 (assuming not incentive accounts)

Dividends not assessed

Dividend withholding tax

Charitable Donation treated as an allowance trading charges.

	y/e 31/3/02	y/e 31/3/03
	€	€
Schedule D Case I	1,230,300	nil
Schedule D Case III	25,875	15,875
Chargeable gains	<u>1,256,175</u>	<u>15,875</u>
Less: Charges	1,000	1,000
Taxable Income	<u>1,255,175</u>	<u>14,875</u>
	nil	
Profits	<u>1,255,175</u>	<u>14,875</u>
	y/e 31/3/02	y/e 31/3/03
	€	€
254,000 @ 12,5 %	31,750	
25,875 @ 25 %	6,769	
975,300 @ 16 %	156,048	
14,875 @ 25 %		3,719
Corporation tax liability	<u>194,267</u>	<u>3,719</u>

(d) Losses utilised against profits before charges

Total Loss to utilise	€ 266,320
Set off y/e 2003	<u>15,875</u>
	€ 250,445

	y/e 31/3/02	y/e 31/3/03
	€	€
Schedule D Case I	1,230,300	nil
Schedule D Case III	25,875	15,875
Chargeable gains	<u>1,256,175</u>	<u>15,875</u>
		15,875
Loss Relief	250,445	
	<u>1,005,730</u>	-
Less: Charges	1,000	-
Profits	<u>1004,730</u>	
Corporation tax		
254,000 @ 12,5 %	31,750	
25,875 @ 25%	6,469	
<u>724,855 @ 16%</u>	<u>115,977</u>	
Corporation tax liability	<u>154,196</u>	-

Year/end	2002	Original CT Liability	194,267
		Revised CT Liability	<u>154,196</u>
		Reduction	40,071

- (e) In the year to 31 March 2002, the loss claim reduces the corporation tax liability by €40,071.

In the year to 31 March 2003, claim of € 15,875 saves tax of € 3,719.

Although the rate of relief in the year to 31 March 2003 is disappointing, the overall position is that losses of € 266,320 have saved tax of € 43,790. There are also charges unutilised c/f to 2004.

The only alternative would have been to carry forward the trading loss to the year to 31 March 2004 to the same trade, in which the company seems likely to pay tax at 12,5% . Saving tax at 12,5% (and having to wait a year before this benefit is obtained) is clearly worse than saving tax at 20.6%, so the company's decision was the right one.

Question 5

(a) Non-taxable employment income:

- employer's contribution to occupational pension scheme
- mileage allowance within agreed rates (cap 79,7c with 32c clearly below)
- parking space
- mobile telephone – necessary for business
- staff party

Non-taxable income from other sources:

- interest on SSIA
- premium bond prize
- rent from lodger (subject to €5,000 thresholds)

(b) The donations are deemed to be made net of 20% income tax. Charities are not liable to income tax so the charities concerned recover a further €127 (€507 x 20/80) from Revenue, making the donations worth €634 in total.

This has the effect of moving €634 of income from the higher rate to the basic rate, resulting in a tax saving of €139 (22% x 634).

(c)

		€
Schedule E:		
Gross salary		42,500
Less: Pension contributions (6%)	2,550	
Car allowance deficit:	756	
Professional subscription	114	3,420
		39,080
Add: BIK – Loan		612
Long service award		400
		40,092
Schedule D Case III		190
Schedule F (€4,860 + €1,215)		6,075
		46,357
Taxable income		46,357

	€
Taxable Income	46,357
Gross tax	
32,000 x 20%	6,400
14,357 x 42%	6,030
	12,430
Charity Donation	(139)
Tax Credits	
Single 1,520	
PAYE 800	2,320
	9,971
Tax paid	
DWT	1,215
DIRT	38
Payable	8,718

(d)

	Amount
E'ER 10,75% x 40,350 = 4,338	42,500
E'EE 4% x 40,350	- 2,550
2% x <u>40,350</u>	+ 400
Total	40,350

Income for PRSI is income after superannuation and excludes BIK.

(e) Tests which are used to distinguish employment from self-employment:

- Control
- Financial risk
- Provision of equipment
- Work performance and correction
- Holidays and sickness
- Exclusivity

If Howard persuaded the organisation to treat him as a self-employed consultant, it appears that he would continue to work exclusively for them and that his work would still be under their control. Presumably he would still be required to perform the work personally, would undertake no financial risk and would provide no equipment of his own. It is uncertain whether he would continue to receive holiday pay and sick pay but (apart from this) the majority of the tests outlined above clearly indicate employment. Therefore his attempt to claim self-employment status would almost certainly fail.

(f) The provision of personal services via an intermediary company is caught by the anti-avoidance legislation. This legislation applies to "relevant engagements" whereby a worker provides services through an intermediary in circumstances such that the income arising from the engagement would have been treated as income from employment if it had not been for the presence of the intermediary.

In Howard's case, therefore, the income derived from his work would continue to be taxed as if he were an employee, regardless of the fact that this income would be paid to his private company rather than to him directly.

Workings

2003 Salary €42,500

Car Expenses

p. service rates up to 4000 miles => € 79,76

Preferential Loan

Home Loan 7,5 %
Other Loan 11,0%

8,000 @ 9 % (11-2) => € 720	Average
5,600 @ 9 % (11-2) => € 504	
	612

Car Capital Allowances

Travel to or from work and private - not allowable

$$\frac{2,500}{12,000} = > 21\%$$

Excluding Depreciation (Assumption) => Balance € 2,000

$$2,000 \times 21\% = > € 420$$

Assumption C Alls equivalent to Depreciation

$$1,600 \times 21\% = > € 336$$

Revised Cost 420 + 336 => € 756

Alternative

Agreed rate	29,7 x 2,500 => 1,993
Allowed	32,0 x 2,500 => <u>800</u>
Discrepancy	1,193

Prudent approach claim revised cost € 756

Question 6

(a) (i) Annual Accounting for VAT

Section 58, Finance Act, 1989 enables the Collector General to authorise persons to make an annual VAT Return and pay their VAT on an annual basis. The features of this provision are as follows:

- a) The Collector General may determine that Returns be submitted for any number of taxable periods not exceeding 6.
- b) The taxable person may continue to operate VAT on a two-monthly basis if he so wishes.
- c) The period covered by the authorisation is defined as the accounting period.
- d) VAT Returns and payment must be submitted between the 10th and 19th day of the month following the end of the accounting period.
- e) The Collector General must consider certain factors before authorisation, and the authorisation may be issued conditionally or unconditionally.
- f) The Collector General may terminate the authorisation, having taken account of certain factors.
- g) The taxable person has the option to align the date of his annual VAT Return with his commercial accounting period.
- h) There are provisions for a deemed termination of authorisation on cessation of trading, or liquidation, bankruptcy or death of the taxable person as appropriate.
- i) Where the deemed termination arises on the death of a taxable person, his personal representative is deemed to be the taxable person.
- j) A taxable person who operates on an annual basis may be required to pay their VAT by monthly direct debit.

(ii) Cash Basis

With effect from 1 July 1994 the following have the option to account for VAT on the basis of cash received in a taxable period rather than on the basis of sales.

- a) A person who satisfies the Revenue Commissioners that taking one period with another, not less than 90% of his turnover is derived from taxable sales to unregistered persons.
- b) A person who satisfies the Revenue Commissioners that the total consideration which he is entitled to receive in respect of his taxable supplies has not exceeded and is not likely to exceed €635,000 in any continuous period of twelve months.

(iii) In general, it is not possible to recover input tax incurred in connection with non-business activities. However, a special scheme permits persons (and certain other statutory bodies) to recover input tax on taxable supplies.

The business activities of a local authority (or other statutory body) for example is likely to involve the making of both taxable supplies and exempt supplies. Such a body will therefore be partially exempt but the usual partial exemption rules do not apply. Local authorities and similar bodies are able

to recover input tax incurred in connection with their business activities as follows:

- Input tax which is attributable to taxable supplies is recovered in full.
- Input tax on overheads are recoverable based on agreed apportionments

(iv) Intra-Community Acquisitions – Unregistered Persons

Public bodies who make an intra-Community acquisitions are not registered for VAT in Ireland because the annual value of their intra-Community acquisitions remains below €41,000 threshold. The result is that VAT is instead payable in the Member State where the goods were purchased at the VAT rate applicable there. Where a non-taxable entity or exempt business exceeds the intra-Community acquisition threshold, it must register for VAT and is liable to tax in Ireland on its intra-Community acquisitions and must self-account for the tax payable. The threshold applies to a rolling 12 months basis.

- (v) Interest, penalties, VAT and cross tax head audit may result. The interest charges on late payment is .0322% per day or part thereof. It may also have consequences for registration and the scheme operated by the organisation

(vi) “Fourth Schedule” Services

These include advertising services, consultancy, legal and accounting services, data processing services, banking, financial and insurance services, the provision of staff, transfers and assignments of copyright patents, licences, trade marks and similar rights, hiring out of movable goods (other than means of transport), telecommunication services, radio and television broadcasting services and electronically supplied services. There are complicated provisions determining the place of supply of these services and this will vary according to the place of residence or establishment of the customer and according as to whether or not the services are supplied for business purposes.

- (b) The main features of the Self Assessment system which should be outlined are:

- The role of the annual tax return with supplementary pages and optional electronic filing via ROS System
- The optional tax calculation section of the return
- The deadlines for submission of the tax return
- The procedure with regard to enquiries and audit procedures in accordance with recent Finance Acts
- The appeals procedure
- Record-keeping requirements.
- Revenue audit arrangements