Capital Acquisition Tax – Reliefs and Exemptions

The capital acquisitions tax (CAT) regime applies to gifts and inheritances, and the number of reliefs is relatively limited. The well-known reliefs are dwelling house relief, agricultural relief and business relief. The legislation sets out the conditions for the reliefs, and the tests which must be met for relief to apply. In practice, Revenue will sometimes allow a relief to apply where the statutory conditions of the relief are not precisely met, and in other cases Revenue will take the approach of following the legislation strictly.

In many cases, where the strict conditions of a relief are not met, but there are circumstances in which a taxpayer is of the view that a relief should be allowed it can be worthwhile making a submission to Revenue asking them to apply the relief on the basis of a concession. In this context, it is worth noting that under s. 59(4) of the Capital Acquisitions Tax Consolidation Act 2003 (CATCA 2003) Revenue have the power to reduce a tax liability where *"the complication of circumstances affecting a gift or inheritance or the value of that gift or inheritance or the assessment or recovery of tax on that gift or inheritance are such as to justify them in doing so".*

It can be useful to know how Revenue generally deal with reliefs and the extent of flexibility available. This paper covers the main reliefs and Revenue's general approach in practice.

Dwelling House Relief

Dwelling house relief is probably the best known and most widely utilised CAT relief. Section 86 of CATCA 2003 provides an exemption for dwellings, which are occupied by a beneficiary as his or her only or main residence. A dwelling is *"any building or part of a building…used or suitable for use as a dwelling"*, and includes grounds of up to one acre occupied and enjoyed with the dwelling. A dwelling includes houses and apartments.

A beneficiary must have occupied the dwelling as his only or main residence throughout the 3 years prior to the gift or inheritance. If the beneficiary has moved house he must have occupied the old dwelling (owned by the disponer) and the replacement dwelling (purchased to replace the old dwelling) for 3 out of the 4 years before the gift/inheritance. Any period when a person is out of Ireland because he is working abroad can be treated as occupation provided that all the duties of the employment are performed outside Ireland.

The beneficiary must retain the dwelling house, and occupy it as a main residence for 6 years after the gift or inheritance (unless he is aged 55 or over at the date of the benefit). If the property initially received is replaced the two properties have to be occupied for six out of the seven years following the gift/inheritance. If the beneficiary leaves the house for long term medical care in a hospital, nursing home or convalescent home after he receives the benefit then he is deemed to have been occupying the property during the treatment.

The beneficiary must not be beneficially entitled to any other dwelling house at the date of the gift or inheritance. Ownership of a rental property or a holiday home in Ireland or abroad will prevent a beneficiary claiming this relief.

Special anti-avoidance rules apply to gifts. S. 86 (3A) CATCA 2003 applies to gifts taken on or after 20 February 2007 and the relevant legislation is as follows:

"(3A) For the purposes of subsection (3)(a), in the case of a gift—

(a) any period during which a donee occupied a dwelling-house that was, during that period, the disponer's only or main residence, shall be treated as not being a period during which the donee occupied the dwelling-house unless the disponer

is compelled, by reason of old age or infirmity, to depend on the services of the donee for that period,

(b) where paragraph (a)(i) of subsection (3) applies, the dwelling house referred to in that paragraph is required to be owned by the disponer during the 3 year period referred to in that paragraph, and

(c) where paragraph (a)(ii) of subsection (3) applies, either the dwelling house or the other property referred to in that paragraph is required to be owned by the disponer during the 3 year period referred to in that paragraph.".

The disponer must have owned the dwelling house throughout the 3 year period of occupation by the beneficiary and where a beneficiary receives a gift of a house from a disponer that is, at the date of the gift, the disponer's principal residence then the beneficiary must be living in the house due to the old age or infirmity of the disponer.

Old age for dwelling house relief purposes is 65 years. The beneficiary must be resident in the house for 3 years after the disponer reaches the age of 65, so the earliest point at which a beneficiary can avail of DHR on a family home based on the old age of the disponer is when the disponer reaches 68 years.

If the disponer is not 68 or older on the date of the gift the beneficiary must have been compelled to live with the disponer for the 3 year occupation period due to the disponer's infirmity. A letter from a doctor attesting the infirmity of the disponer is good evidence to support a claim for dwelling house relief in these circumstances.

Revenue's approach to dwelling house relief is generally to interpret the conditions of the relief strictly and it is not a relief that they are inclined to apply on a concessional basis where all of the conditions of the relief have not been strictly met.

Ownership of any other Dwelling House

The beneficiary must not be beneficially entitled to any other dwelling house or any interest in any other dwelling house at the date of the gift or inheritance. There is no restriction on the beneficiary owning an interest in another dwelling house before the benefit so a beneficiary may dispose of an interest in a property (such as a rental investment property or holiday home) before receiving the principal residence. A beneficiary could also consider transferring property to a company prior to receiving a benefit of a dwelling house in order to qualify for the relief, but the tax implications of any such transaction should be considered. Owning an interest in a commercial property at the date of the benefit will not affect the availability of the relief.

If a beneficiary already owns an interest in a dwelling house and receives another interest in the same property relief should still apply as the section refers to an interest in *"any other dwelling house"*.

Following an Appeal Commissioners' decision in favour of the taxpayer there was some uncertainty on whether the inheritance of another dwelling forming part of the same residue would preclude relief. This was resolved by the case of *Knapp v Revenue Commissioners AC* 191/07 Circuit Court 12 January 2010. In that case a mother left her entire estate (including a number of dwelling houses) to her 2 daughters equally. One dwelling house had been occupied continuously by the daughters, and neither of them owned any other dwelling houses, but the Court held that they were not entitled to dwelling house relief as they took other residential properties in the same inheritance.

For example if a parent dies leaving a share in a holiday home valued at €100,000 to 5 children each has a beneficial interest in a dwelling which is only worth €20,000 each, but this interest will preclude a claim for dwelling house relief on any other residential property which may otherwise qualify for the relief.

If tax planning advice is being given on a Will, and there is more than one residential property in the estate and a beneficiary can meet the terms of dwelling house relief on one property the testator may be asked to consider including a clause in the Will which provides for the sale of the other residential properties, so that the beneficiary is inheriting a cash asset (the net sales proceeds) rather than an interest in a dwelling house.

A suitable wording might be the following;-

> "*I give devise and bequeath my family home at …to my executors on trust for sale with power to postpone the sale, and I direct that the net proceeds of sale will pass into the residue of my estate".*

Ownership Requirement

As outlined above, where a beneficiary receives a gift of a dwelling house the disponer must have owned the dwelling house for the 3 year occupation period. If the disponer lives with the beneficiary during the occupation period, then the disponer must be 68 when the gift is made, or the disponer must be otherwise infirm.

In a recent case in my firm two parents were seeking to transfer the family home to a child who had lived in the house for in excess of 3 years. One of the parents (the father) was over 68 but the other parent (the mother) was under 68 and the property was held jointly. Strictly speaking, there were two disponers and both disponers needed to satisfy the old age or infirmity condition.

If the mother transferred her interest to the father, the conditions of dwelling house relief could be met but this would not have prevented an issue on the applicability of dwelling house relief as s. 8 CATCA 2003 would have deemed the transfer to the child to have been made from both the mother and the father, as the gift to the mother from the father would have been made to facilitate the gift to the child.

On further investigation it transpired that the mother suffered from a medical condition and if a letter was obtained from the mother's GP stating that the mother was infirm and dependent on her child, then this should be sufficient to show that the infirmity condition was met.

The ownership requirement would also need to be considered in a case where a house which has passed by survivorship within the 3 years prior to making a gift, is subsequently gifted on. The surviving owner would have owned as a joint tenant for longer than 3 years, so the property would have been "*owned by the disponer"* for the required 3 year period, but there is a possibility that Revenue could seek to treat only 50% of the property value as qualifying for dwelling house relief on a subsequent gift (on the basis that an interest received by survivorship under a joint tenancy is deemed to pass in the same way as a tenancy in common for CAT purposes). It could be argued that if the legislation is read strictly, any ownership interest (no matter how small) would provide a basis for relief. It would follow that if a disponer who was a tenant in common with a 1% interest for 5 years then received the remaining 99%, relief could be claimed on a gift immediately afterwards on the basis that the disponer was a 1% owner for the required 3 years. This may not be a view that Revenue endorses so the recommendation would be to write to Revenue to seek confirmation that the relief is available on 100% of the property value in all such circumstances.

Long Term Medical Care in a Hospital, Nursing Home or Convalescent Home

One of the main conditions of dwelling house relief is that a beneficiary must occupy a dwelling house for three years prior to the gift or inheritance of the dwelling.

If a beneficiary moves into a hospital, nursing home or convalescent home to receive long term medical care after taking a gift or inheritance then the relief will not be clawed back. However, the legislation only allows such medical care to qualify as occupation of a dwelling to prevent a clawback and if a beneficiary moves into long term nursing home care prior to taking a gift or inheritance of a dwelling the 3 year pre-benefit occupation condition is not met.

My office has had some cases recently where beneficiaries who had lived in dwelling houses for most of their lives were precluded from the relief because they moved into a nursing home prior to taking a benefit of a dwelling, and having gone to Revenue seeking a concessional application of dwelling house relief, this was refused by Revenue.

In one case a beneficiary died having been pre-deceased by her sister who died circa 8 weeks before the beneficiary in question.

The two sisters were very close and indeed quite interdependent. The disponer had various physical issues but she was the beneficiary's main carer at home because of the beneficiary's failing memory. Each sister executed a Will to pass her estate to her sister, provided that she survived her by 30 days. Each Will, in the event that the testatrix was not survived by her sister, provided that the entire estate would pass onto an identical list of beneficiaries in identical shares.

As the beneficiary survived the disponer by circa 8 weeks her estate passed to her sister. The assets held by the disponer on her death consisted of an interest in the family home, passing to the beneficiary as the surviving joint tenant, and an amount of cash passing under the Will.

In the normal run of events the disponer would have been eligible for dwelling house relief in respect of the inheritance of the family home.

The disponer's health had deteriorated prior to her death and she required full time nursing home care. As the beneficiary could not live at home alone she had to go into a nursing home also. On that basis she was not technically eligible for dwelling house relief on the inheritance of the family home, where she had lived for her entire life with her sister. The deceased did not, in reality, survive long enough to take any benefit from the inheritance and the house would have been eligible for dwelling house relief, had it not been for the unfortunate ill health of the deceased's sister (the disponer).

Revenue refused to allow the application of dwelling house relief on a concessional basis.

In a similar case, the disponer and the beneficiary were the sole occupants of a dwelling house and the beneficiary was the principal carer of his elderly aunt (the disponer) and cooked, shopped and generally cared for the welfare of his aunt. The beneficiary was aged 67, and himself suffered from various medical complaints which required significant medical attention.

The beneficiary lived in the dwelling for well in excess of 3 years prior to the death of his elderly aunt. He did not hold an interest in any other residental property on the date he inherited the dwelling house but while the property was the beneficiary's permanent residence he was admitted to full time medical care within the year prior to receiving the benefit of the dwelling house from his aunt. The beneficiary had no other assets to fund CAT or to pay for his nursing home care.

Revenue refused to concessionally allow the application of dwelling house relief.

Clawback on Disposal

A beneficiary who receives a gift or inheritance of a dwelling house on which dwelling house relief is claimed, must not sell or dispose of property during a period of 6 years or the relief will be clawed back. There is no exception made for a married couple putting a property in the joint names of both spouses.

We advised recently on a case in which a child was to receive a gift of the family home from her parents. The 3 year occupation condition and the ownership requirement was met, and the beneficiary did not have an interest in any other residential property. The property was in the family for more than 100 years, spanning 4 generations, and the parents wanted to transfer it to the next generation.

The beneficiary had recently married and the couple lived in the property as their family home but the husband did not have 3 years' occupation. Some works were required to renovate the property, which involved taking out a mortgage secured on the property. The lending institution would not lend to the beneficiary alone, and it was a condition of the borrowing that her husband was also put on title. In order to meet the terms of her loan approval the beneficiary needed to transfer the property into joint names with her husband after receipt of a gift of the property from her parents.

Technically, this would have been a disposal of the dwelling and would have given rise to a clawback of the relief as it would have been within the 6 year clawback period. The fact that there is no CAT applied to gifts or inheritances passing between spouses would not have prevented a clawback on the transfer. A concession was sought from Revenue on the basis that the beneficiary was simply putting the dwelling into joint names with her husband. Revenue refused to grant the relief.

In such circumstances, where a clawback cannot be avoided, it is worth investigating if bank requirements can be met by transferring a smaller interest in the property to minimise the exposure to a clawback, or by putting a mortgage in joint names without transferring legal title.

Revenue did confirm that they would not seek to apply the "gift on a gift" anti-avoidance legislation which could have deemed a gift to pass from the parents to the beneficiary's husband. Revenue indicated that the anti-avoidance would not apply on the basis that it could be demonstrated that the gift to the husband would not be connected with the gift from the parents.

Free Use of Property

If a residential property has passed to a beneficiary and dwelling house relief has been claimed, Revenue will often review the "free use of property" benefit which may have accrued during the occupation by the beneficiary prior to the gift passing.

Where a beneficiary resided in a property rent free, or otherwise had the use of an asset without paying market value consideration for it then a free use of property benefit would have arisen on 31 December for each year in which the beneficiary has the use of the asset or cash.

This benefit is measured by the value forgone by the person giving the benefit. If the asset is property which could have been rented if it was not occupied by the beneficiary, Revenue will generally measure the value of the benefit by reference to the rent foregone.

The free use value would be subject to CAT and if it was a gift the annual small gift exemption of €3,000 could be deducted if there are no other benefits received in the year. If the beneficiary occupies the property with a spouse two small gift exemptions may be available. If there is a concern that the Revenue may argue that the child is the only person receiving the gift and the spouse and any children are living there as family members rather than getting a benefit in their own right, the property can be leased to the two spouses at a nominal rent to show that both are receiving a benefit.

The free use generally erodes the beneficiary's tax free threshold and once the level of benefits reaches 80% of the relevant CAT threshold a CAT return is required. Once the threshold had been used up a CAT liability will arise.

The free use of property position should generally be reviewed prior to claiming dwelling house relief but it should be noted that Revenue have confirmed in their "Guide to the CAT Treatment of Receipts by Children from their Parents for their Support, Maintenance or Education" that no free use of property benefit will be assessed where the dwelling in question is the family home.

"The non-exclusive occupation of the family home by a child (including where relevant the child's spouse/partner) family member. Revenue's view is that this does not give rise to a gift by the owner of the property to the family member. Thus, in line with Revenue's long standing approach, there is no question of trying to attribute a value to "bed and board" provided by the owner of the house to a child (including where relevant that child's spouse/partner) of any age."

In this guide Revenue clarify that free use of property is generally assessable on a child:

A *"Parent buys a house for €1 million and allows his 30 year old daughter have the free use of the house indefinitely. The annual rental value of the house is €36,000. The free use of the house is a gift equal to the annual rental value each year (less the annual small gift exemption of €3,000). If two or more of the parent's children have the free use of the house, the value of the gift is shared. If the child ultimately inherited the house, that inheritance could be eligible for exemption from CAT under the principal private residence exemption in section 86 CATCA 2003 once the conditions governing the relief were satisfied."*

However, Revenue also indicate that if the beneficiary is a child aged 25 or under, then the free use of property benefit would be sheltered by the maintenance exemption under s. 82 CATCA 2003:

"The provision of the use of a house owned by a parent rent-free, to a child not more than 25 years of age who is attending university, to help support and maintain the child while in university, is a normal and reasonable provision and is, accordingly, exempt from tax under Section 82"

Agricultural Relief

Agricultural Relief is a valuable CAT relief which reduces the market value of agricultural property by 90% for CAT purposes. This can substantially reduce a CAT liability.

Where a gift or inheritance is taken subject to the condition that it is invested in agricultural property, and this condition is met within two years, then the benefit is deemed to have consisted of agricultural property on the date of the gift or inheritance and on the valuation date.

"Agricultural Property"

Property that qualifies as agricultural property includes:-

- Agricultural land, pasture and woodland situated in the European Union;
- Crops, trees and underwood growing on such land;
- Farm buildings and dwelling houses (and the land on which they are situated) that are proportionate in size and character to the requirements of the farming activities;
- Farm machinery situated on such property;
- Livestock and bloodstock situated on such property;
- European Union 'single farm payment' entitlements.
- Milk quotas if transferred together with agricultural land (Revenue practice)

Revenue's view is that a building, without the land, is not agricultural property so a farmhouse transferred to a farmer on its own does not qualify for agricultural relief.

In addition small plots of land may not be accepted by Revenue as agricultural property. The Revenue CAT Manual notes that in February 2012 the Appeal Commissioners determined that a small parcel of land (circa 0.14 acres) was not agricultural property. In the UK case of Starke (executors of Brown deceased) v IRC [1996] 1 All ER 622 2.5 acres of land with a farmhouse and other buildings was held not to be agricultural property.

Revenue indicate in the manual that the use of the property is fundamental to agricultural relief. In Rosser v IRC (2003) sPc 368, two acres with a barn on them was regarded as agricultural while a house on the same holding was not agricultural.

The Farmer Test

A farmer is an individual who can demonstrate that not less than 80% of the market value of the property to which he is beneficially entitled in possession (following the taking of the gift or inheritance) consists of agricultural property.

An individual is deemed to be beneficially entitled in possession to an interest in expectancy, so if an individual is a remainderman following a life interest trust in favour of another person, the value of the remainder interest would be taken into account when reviewing the farmer test. However, Revenue accept that a future entitlement to a pension fund need not be included in the farmer test.

Generally, no deduction is made from the market value of property for any debts or encumbrances (such as a mortgage or other charge on property), but if an individual's principal private residence is an off-farm dwelling house which is not agricultural property, any mortgage or charge attaching to this property is deductible.

Where the agricultural property consists of trees or underwood, the beneficiary does not have to be a "farmer" for the purposes of claiming relief on the woodlands. The trees or underwood must be growing on land and cannot be cut or harvested.

From 01 January 2015 a beneficiary needs to:

- Hold a relevant farming qualification or obtain such a qualification within 4 years of the benefit and farm the land for 6 years on a commercial basis with a view to the

realisation of profits,
- Actively farm the land on a commercial basis with a view to the realisation of profits (at least 50% of normal working time test) for 6 years, or
- Lease the land to an "active farmer" for a 6 year period (at least 50% of normal working time test) and on a commercial basis with a view to the realisation of profits.

The Relief

As outlined above, agricultural relief operates so as to reduce the market value of the agricultural property by 90% when calculating the CAT liability.

In order to qualify for the relief, the following conditions must be met:-

- The benefit consists of agricultural property at the date of the gift or at the date of inheritance
- The benefit consists of agricultural property at the valuation date
- The beneficiary is a farmer on the valuation date (after taking the benefit)

Expenses and Deductions

The general CAT principle is that liabilities, costs and expenses are deductible where they are properly payable out of a benefit.

Where agricultural relief applies, the liabilities, costs and expenses relating to the agricultural property must also be reduced by 90% when taking a deduction from the market value of the agricultural property. This mirrors the 90% deduction in the market value of the agricultural property.

Where a benefit consists of a combination of agricultural and non-agricultural property, the expenses must first be apportioned between the agricultural and non-agricultural property.

The portion relating to the non-agricultural property is unaffected, but the portion relating to the agricultural property is reduced by 90% as described above.

Clawback

Any relief given may be wholly or partly clawed back within 6 years of the gift or inheritance if:-

- The agricultural land (other than crops, trees or underwood) is disposed of and not replaced within a year of the disposal by other agricultural property, or

- The agricultural land is compulsorily acquired and is not replaced within 6 years of the compulsory acquisition by other agricultural property.

Where the agricultural property has development value and is disposed of between 6 and 10 years following the date of the gift or inheritance, a clawback of the relief on the development value would also arise. It is worth noting under this provision, that there is no allowance for a continuation of the relief where the sales proceeds are reinvested in agricultural property.

From 01 January 2015 if the beneficiary does not continue to farm the land as an active or trained farmer, or lease it to an active or trained farmer for the 6 year period the relief will be withdrawn.

Revenue Approach to Agricultural Relief

Revenue's approach to the agricultural relief legislation can be a little more lenient than the approach to other legislation, although this is generally restricted to the changes made by Finance Act 2014, which brought in the active farmer requirements.

Revenue updated the CAT Manual following Finance Act 2014 and many of the examples contained in the manual clarify the active farmer rules.

The intention of the legislation is to encourage the active use of farmland and the general recommendation would be to make a submission to Revenue if the application of the legislation is unclear or a literal reading of the legislation is such that it is in contradiction to the general intention of the legislation.

Outside of the active farmer provisions, Revenue tend to interpret the agricultural legislation quite strictly.

My office recently dealt with Revenue in a case where a deceased had held an interest in farmland.

The land passed to the deceased's children and the 80% financial farmer test was met. The date of the inheritance was prior to 01 January 2015 so the active farmer requirements were not relevant. The property was agricultural property on the date of the inheritance.

To meet the strict conditions of agricultural relief, the property needed to be agricultural property on both the date of the inheritance (the date of death) and the CAT valuation date (generally the date of grant of probate).

The only practical way to distribute the Estate was to sell the farmland, and two of the beneficiaries wanted to reinvest the sales proceeds in agricultural property after they were distributed from the Estate. The beneficiaries did not want the Inland Revenue Affidavit (IRA) to be lodged until they knew what the sale proceeds would be, so as to limit any CGT payable on the disposal. If the date of grant of probate was the CAT valuation date the property would not have been agricultural property on the valuation date, as the asset would have been a right to the sales proceeds.

The CAT issue arose because of the timing of the sale. If the beneficiaries received the property, then sold it and reinvested sales proceeds the clawback on sale would not arise because of the reinvestment. However because the contract for sale would be signed in this case before the valuation date, and the reinvestment would occur after, the issue was that technically the beneficiaries would not qualify for the relief. On the basis that the beneficiaries would be investing in agricultural property, a concession was sought from Revenue asking them to allow agricultural relief. Revenue refused, as the strict terms of the relief were not met.

In order to accelerate the valuation date to a date prior to the sale of the land, without lodging the IRA, the beneficiaries took possession of the land so that the property was agricultural property on the valuation date.

Business Relief

CAT business relief enables the donee/successor to reduce the value of a relevant gift/inheritance by 90% of its taxable value.

The operation of the relief can be complex and the following questions need to be considered:

1. Is the asset "**relevant business property**"?	*If not there will be no relief.*
2. Do **investments** make up more than 50% of the value of the asset	*If so there will be no relief, if not any investment value will need to be excluded from the relief.*
3. Was the asset held for the required **period of ownership** before the benefit?	*If not there will be no relief.*
4. Does any part of the value come from **excepted assets**?	*If so the value will need to be excluded from the relief.*
5. Does any part of the value come from **excluded assets**?	*If so the value will need to be excluded from the relief.*
6. Will the beneficiary **retain the asset** for the required 6 – 10 years to avoid clawback?	*If not the relief will be clawed back.*
7. Will the asset remain **"relevant business property"** as defined?	*If not the relief will be clawed back.*

Relevant Business Property

In order for assets to qualify for business relief they must constitute relevant business property. There are 6 categories of qualifying property:

1. A business or interest in a business (note that a single asset will not qualify).

2. Unquoted shares in a company if the beneficiary controls 25% of the votes after taking the benefit.

3. Unquoted shares in a company if the beneficiary has 10% of the nominal value after taking the benefit, and has been a full time officer or employee of the company for 5 years.

4. Unquoted shares in a company controlled by the donee/successor within the meaning of S 27 CATCA 2003 (effectively a company controlled by the donee's family and in this context 50% ownership may give control).

5. Any land building plant/machinery which immediately prior to the gift/inheritance was used wholly or mainly by a company controlled by the donor (in this context a majority of votes test) or a partnership in which the donor was a partner, provided that the asset passes with the shares or interest in the partnership business and the shares or interest qualifies as relevant business property.

6. Quoted shares in or securities of a company which would fall within the categories listed above but for the fact that they are quoted, which were in the beneficial

ownership of the disponer immediately prior to the disposition and were unquoted at the date the disponer acquired them or at 23 May 1994, whichever is later.

The following businesses are excluded from the relief

1. Dealing in currencies, securities, stocks or shares, land or buildings
2. Making or holding investments.

In addition the relief is not available if the value of the asset is derived "wholly or mainly" from investments so if the majority of the value of a business (over 50%) consists of the investment assets listed above the relief will not be available.

The assets must have been owned by the disponer for a period of 2 years before an inheritance or 5 years before a gift.

Excepted and Excluded Assets

An asset which has not been used wholly or mainly for the purposes of the business throughout the two years to the date of the gift or inheritance (or for the entire period of ownership if it has been owned for less than 2 years) is an excepted asset and the value of the asset will not qualify for relief. Any asset used for the personal benefit of a company director will be excepted as it is used personally and not for the business.

If the benefit consists of shares and the company owns assets which are not excluded as investment assets, but which would not have qualified as relevant business property, the value of those assets will need to be deducted when calculating the relief.

Clawback Period - Disposal

The relief will be withdrawn if the relevant business property is disposed of within 6 years of the date of gift/inheritance and not replaced within a period of one year from the date of disposal. If part of the relevant business property is development land then the clawback period is extended to 10 years.

Clawback Period – Relevant Business Property

The relief shall be withdrawn if the asset ceases to qualify as relevant business property during the 6 years after the date of gift/inheritance, and does not come back into the category of relevant business property within a year. This could occur if the trade in a company is scaled down and a trading property is rented so that it falls into the category of investments and as a result the investments held make up more than 50% of the value of the company.

Groups

If the shares passing are in a group company, and the business of any company which is a member of the group is largely an investment business, then unless the investments are land and buildings occupied wholly or mainly by other companies whose activities do qualify for relief, the value of the investment company is excluded from relief.

Revenue Verification

Revenue may look at the following to verify that a business was carried on by a disponer, and continues to be carried on by a beneficiary:

- Income tax returns of a disponer and a beneficiary to ascertain if trading income has been included in the income tax returns
- In the case of a deceased's estate, Revenue may look to see if estate income tax returns have been filed to include trading income
- In the case of an estate, Revenue may look to the IRA to confirm the occupation of the deceased (i.e. if the deceased is indicated as retired in the IRA) Revenue may argue no business was being carried on
- Revenue may seek trading accounts

Control

In the context of the control test, it is worth noting that the control test is a point in time test and does not look back, so if the ownership conditions are met and the control test can be met by transferring voting rights or shares between shareholders, it may be possible to give the disponer/beneficiary control so that a gift or inheritance would qualify for the relief.

This would be particularly relevant if the disponer held 50% of the voting rights, as the disponer would only need to acquire an additional 1% of the voting rights for the control test to be met.

Gift of Subsidiary

If a disponer gifts a subsidiary company to a beneficiary, the transfer would not qualify for relief, as the disponer has not held the subsidiary company directly so the ownership conditions have not been met.

Agricultural Relief and Business Relief – Time of Disposal and Acquisition

If agricultural property or relevant business property is sold, the timing of the sale or disposal can be important in the context of the clawback on sale if the disposal occurs within 6 years of the date of the gift or inheritance (10 years in the case of land with development value) and the following should be considered:

1. Is the timing of the sale within the 6 or 10 year clawback period?
2. If the sale occurs within 6 years is the subsequent purchase of replacement property occurring within the permitted year, to continue the relief and prevent the clawback?

The agricultural relief legislation refers to a "*disposal or compulsory acquisition*" and the business relief legislation refers to a "*sale, redemption or compulsory acquisition*". Both reliefs allow for a continuation of the relief if the sale occurs in the 6 years after the benefit and the proceeds are reinvested in other agricultural or relevant business property within a year of the sale.

It should be noted that if the clawback relates to development land and occurs in the years between the sixth and tenth anniversary of the benefit there is no option to reinvest the sales proceeds to recapture the relief.

There are two schools of thought in relation to the timing of a sale/disposal for CAT purposes.

1. The timing of a sale links in with the date of signing of a contract to transfer property
2. The timing of a sale links in with the date of completion of a transaction

The link into the signing of a contract is largely based on the CGT definition of a disposal and there is a strong argument that in general terms a disposal or sale does not take place until a contract is completed. However, it is understood that the Revenue view is such that the date of signing of a contract is treated as the date of disposal/sale from a CAT perspective also, even though there is nothing in the legislation detailing this. The Revenue view would be open to challenge.

Where possible it is best to treat a disposal or sale as occurring on the signing of a contract and an acquisition as occurring on the completion of a contract. In practice, this could reduce the one year period available for replacement but it would leave little scope for Revenue challenge.

Life Interests

S. 54 CATCA 03 provides for the payment of CAT by instalments (for a maximum period of 5 years) with interest charged on the tax due.

Under S. 54 (5) CATCA 03, where an interest is a life interest, and the life interest ceases before all of the instalments have fallen due, the balance of the instalments are no longer payable. If a taxpayer pays the tax up front on a life interest, but the life interest ceases within a 5 year period, a refund equal to the amount of instalments which would not yet have fallen due if an instalment arrangement had been entered into, is available.

In cases where a life tenant dies shortly after receiving a life interest, the practical result is that no tax will be due even though the life tenant has taken an inheritance. As this is a legislative provision there is no requirement to obtain Revenue agreement, but Revenue will generally seek a CAT return and allow a credit for the tax due.

Favourite Nephew Relief

This relief provides that a nephew or niece is deemed to be a child of the disponer for the purpose of computing tax on a gift or inheritance of business assets provided the following conditions can be met:

1. The donee or successor must be a child (including an adopted child or a stepchild) of a brother or a sister of the disponer, or have a similar relationship by reason of a civil partnership.

2. The nephew or niece must have worked substantially on a full-time basis for the disponer in the five years ending on the date of the gift or the date of the inheritance (or on the date the disponer ceases to have a beneficial interest in possession in the business assets). Reasonable periods of annual or sick leave may be included in calculating the period of five years.

3. He must have assisted in carrying on the trade, business, or profession of the disponer.

4. The benefit must consist of property which was used in connection with that trade, business or profession. If the donee has worked substantially on a full-time basis for a company the gift or inheritance must consist of shares in that company.

If the above conditions are met the nephew or niece is entitled to claim a group (a) threshold, instead of the group (b) threshold, in relation to the business assets. It should be noted that this relief is not available where the benefit is taken from a discretionary trust.

Meaning of "Substantially on a Full-time Basis"

Where the benefit is property used in connection with the disponer's business etc, the nephew or niece must have worked substantially on a full-time basis in the business and Para 7(3) Sch 2 provides that the nephew or niece must work:

- more than 24 hours a week for the disponer at a place where the business is carried on; or
- more than 15 hours a week for the disponer at a place where the business is carried on and such business is carried on exclusively by the disponer, any spouse (or civil partner) of the disponer and the nephew/niece.

Where the benefit consists of shares in a company, the nephew or niece must have worked:

- more than 24 hours a week for the company at a place where the business is carried on; or
- more than 15 hours a week for the company at a place where the business is carried on if such business is carried on exclusively by the disponer, any spouse (or civil partner) of the disponer and the nephew/niece.

Mixed Assets

It should be noted that if a beneficiary who is eligible for this relief also receives non-business assets the other assets fall to be taxed as a group (b) benefit so a beneficiary may be entitled to claim two different tax free thresholds (group (a) and group (b) thresholds). This could put a favourite nephew in a better position than a child receiving the same benefit.

Example

Gerry Murphy inherits the estate of his Uncle Harry. The inheritance consists of

- *Agricultural Assets €500,000 (business)*
- *Non-agricultural Assets €100,000 (non-business)*

Gerry qualifies for favourite nephew relief in respect of the agricultural assets valued at €500,000 so they will be a group (a) benefit and will not aggregate with the group (b) non-business assets (€100,000).

If the group (b) threshold is available and the group (a) threshold has been used up the disponer could consider using a discretionary trust to pass some assets to the beneficiary, as assets passing through a discretionary trust fall outside of the terms of the relief, allowing the beneficiary to use the group (b) threshold as well as the group (a) threshold which applies to the business assets passing directly.