Fundamentals Level – Skills Module

Taxation (Malta)

Monday 1 June 2009

Time allowed
Reading and planning: 15 minutes
Writing: 3 hours

ALL FIVE questions are compulsory and MUST be attempted.
Tax rates and allowances are printed on pages 2–4.

Do NOT open this paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

This question paper must not be removed from the examination hall.

Paper F6 (MLA)

The Association of Chartered Certified Accountants

The Malta Institute of Accountants

SUPPLEMENTARY INSTRUCTIONS

1. Calculations and workings need only be made to the nearest €.
2. All apportionments should be made to the nearest month.
3. All workings should be shown.

TAX RATES AND ALLOWANCES

The following tax rates are to be used in answering the questions

Individual tax rates for the year of assessment 2009

Married individuals

			Rate
€		€	%
0	to	11,400	0
11,401	to	20,500	15
20,501	to	28,000	25
28,001 and over			35

Other individuals

			Rate
€		€	%
0	to	8,150	0
8,151	to	14,000	15
14,001	to	19,000	25
19,001 and over			35

Non-resident individuals

			Rate
€		€	%
0	to	700	0
701	to	3,100	20
3,101	to	7,800	30
7,801 and over			35

Corporate income tax

Company tax rate for the years of assessment 2008 and 2009	35%

Value added tax

Standard rate	18%
Reduced rate	5%

Capital allowances

Industrial buildings and structures

Initial allowance	10%
Wear and tear allowance	2%

Plant and machinery

Minimum number of years over which items of plant and machinery are to be depreciated:

Computers and electronic equipment	4
Computer software	4
Motor vehicles	5
Furniture, fixtures, fittings and soft furnishings	10
Equipment used for the construction of buildings and excavation	6
Catering equipment	6
Aircraft	12
Ships and vessels	10
Electrical and plumbing installations and sanitary fittings	15
Cable infrastructure	20
Pipeline infrastructure	20
Communication and broadcasting equipment	6
Medical equipment	6
Lifts and escalators	10
Air conditioners	6
Equipment mainly designed or used for the production of water or electricity	6
Other machinery	5
Other plant	10

Capital gains

Capital gains index of inflation:

1983	428·06	1996	549·95
1984	426·18	1997	567·95
1985	425·17	1998	580·61
1986	433·67	1999	593·00
1987	435·47	2000	607·07
1988	439·62	2001	624·85
1989	443·39	2002	638·54
1990	456·61	2003	646·84
1991	468·21	2004	664·88
1992	475·89	2005	684·88
1993	495·60	2006	703·88
1994	516·06	2007	712·68
1995	536·61	2008	720·00

Fringe benefit rates on company cars

Vehicle use	% of vehicle value
Vehicle not more than six years old	17%
Vehicle more than six years old	10%

Fuel value	
Vehicle value not exceeding €28,000	3%
Vehicle value exceeding €28,000	5%

Maintenance value	
Vehicle value not exceeding €28,000	3%
Vehicle value exceeding €28,000	5%

Private use

Car value		
From	To	
€	€	
0	16,310	30%
16,311	21,000	40%
21,001	32,620	50%
32,621	46,600	55%
46,600 and over		60%

This is a blank page.
Question 1 begins on page 6.

ALL FIVE questions are compulsory and MUST be attempted

1 Stephen and Lisa Jones moved from the United Kingdom to Malta in February 2006 and since then their tax status has been determined by the Commissioner of Inland Revenue as ordinarily resident but not domiciled in Malta. They married in September 2006 and do not yet have children.

In January 2009 Stephen and Lisa Jones appointed you as their Maltese tax advisor and provided you with the following information regarding their financial transactions during 2008:

1. On 1 April 2008, they took a bank loan of €600,000, of which they used €300,000 to finance the purchase of their new ordinary residence in Balzan; €200,000 to finance the purchase of 1,000 ordinary shares in Castello SpA, a company resident in Italy; and €100,000 to finance the purchase of a small shop in Valletta. The bank charged them interest at the rate of 8% per annum from 1 April 2008 to 31 December 2008.
2. On 1 July 2008, they rented out the Valletta shop for a period of three years at €13,000 per annum.
3. On 31 July 2008, they received in Malta the yearly interest, amounting to €11,000, on an amount of €200,000 they held in a fixed deposit account with a UK bank.
4. On 15 September 2008, they closed the UK bank account (as in item 3 above) and transferred the funds, amounting to €200,000, to Malta as they needed the money to furnish their new house.
5. On 30 September 2008, they received a dividend of €3,100 distributed out of the profits allocated to the final tax account of BG Ltd, a company whose shares are listed on the Malta Stock Exchange.
6. On 4 October 2008, Stephen Jones sold all of the 800 ordinary shares he held in Ballu Ltd, a Maltese private company, for €5,000. He had bought the shares in March 2006 for €20,000. The shares held by Stephen represented 3% of the company's issued share capital and did not entitle him to appoint or remove directors.
7. On 30 November 2008, Lisa Jones sold all of the 20,000 ordinary shares she held in Goa Properties Ltd, a company resident in India, for €60,000 and remitted all the proceeds to Malta. She had bought the shares for €20,000 in 2003.
8. On 31 December 2008, Castello SpA declared a dividend of €5,000 on the 1,000 ordinary shares that Stephen and Lisa Jones held in the company. This dividend was deposited in a savings account the couple hold with the Malta branch of an Italian bank.
9. During the whole of 2008 Stephen Jones was employed with a Maltese company under the following terms:
   (i) Annual gross basic salary of €20,000.
   (ii) Monthly disturbance allowance of €300.
   (iii) Free use of an apartment in Xlendi, Gozo, which the company had bought in 2007 for €120,000.
   (iv) Free use of a motor vehicle that the company had bought in 2000 for €30,000. However, fuel for the car had to be paid for by Stephen Jones himself.
10. During 2008 Lisa Jones ran a retail business selling souvenirs from a shop in Bugibba which she rents from an unrelated entity for €3,000 annually. She also sold souvenirs on a wholesale basis using a non-commercial motor vehicle which she bought in 2008 for €20,000. Her turnover in 2008 amounted to €27,140 inclusive of 18% value added tax (VAT). Shop expenses amounted to €4,000 whilst fuel expenses for the motor vehicle, which she used exclusively for the wholesale business, amounted to €75 per month.
11. Stephen and Lisa Jones also inform you that they moved into their new ordinary residence in Balzan in November 2008. In December 2008 they signed a promise of sale (*konvenju*) with respect to their old ordinary residence in Siggiewi and the public deed transferring the property was signed in February 2009. They had bought the Siggiewi property in 2005 for €210,000 and moved into it in 2007. The price at which they have agreed to sell the property is €360,000.

Required:

(a) **Calculate Stephen and Lisa Jones' tax liability for the year of assessment 2009, choosing the more advantageous option between joint and separate computation.** (20 marks)

(b) **Explain to Stephen and Lisa Jones whether, and if so why, the sale of their residence in Siggiewi will be subject to tax.** (2 marks)

(c) **Assuming the sale of the Siggiewi residence is subject to tax, advise Stephen and Lisa Jones on the taxing options available to them and state when they would be required to pay the relevant tax, if their marginal rate of tax in the year of assessment 2010 will be 35% and the relevant selling price of the property will be equal to the transfer value.** (8 marks)

(30 marks)

2 The directors of Patina Limited have presented you, their tax advisor, with the following draft income statement extracted from the company's management accounts for the year ended 31 December 2008:

	Notes	€	€
Gross profit on operations			120,000
Dividend income	1		14,000
Rental income	2		12,000
			146,000
Overheads and expenses			
Audit fee		2,000	
Exchange differences	3	1,400	
Depreciation	4	12,000	
Interest	5	8,000	
Bad debts	6	760	
Wages and salaries	7	23,100	
Gain on sale of fixed assets	8	(16,000)	
			31,260
Profit before taxation			114,740

Notes:

1. The dividend income is stated gross of foreign and Maltese tax withheld at source and comprises:

	€
A dividend received from the final tax account of Maltina Limited	4,800
A dividend received from the untaxed account of Spruce Limited	3,000
A dividend received from the immovable property account of Attard Limited which was taxed at 35% at the level of the distributing company	3,400
A dividend received from Barone SpA, an Italian company in which Patina Limited holds 0·05% of the shares and from which the Italian company withheld tax at 10%	2,800
	14,000

2. The rental income is derived from the lease of a small hotel to one of Patina Limited's subsidiary companies for €7,000 a year and from ground rent amounting to €5,000 a year receivable on a plot of land that the company owns in Luqa.

3. The exchange differences arose on two transactions, namely:

   (i) The purchase of a consignment of raw materials for US$12,000 on 9 November 2008, when the exchange rate between the US Dollar and the Euro was US$1·5 = €1. The amount payable to the supplier was still outstanding on 31 December 2008 and the exchange rate on this date was US$1·3333 = €1.

   (ii) The sale of a stock of hardware for £8,000 on 1 October 2008 when the exchange rate between the Pound Sterling and the Euro was £0·8 = €1. The supplier settled the amount due on 21 December 2008 when the exchange rate was £0·8333 = €1.

4. All the company's fixed assets were bought in 2006 and depreciation is charged at 20% per annum on cost with respect to all categories of assets, as follows:

	Non commercial motor vehicle	Commercial motor vehicle	Computer hardware	Total
	€	€	€	€
Cost	14,000	28,000	18,000	60,000
Depreciation for year	(2,800)	(5,600)	(3,600)	(12,000)

No depreciation was provided on the non-commercial motor vehicle that was sold during the year (see note 8).

5. The interest expense arose partly on a €100,000 loan that the company had taken out from a commercial bank in 2007, at an interest rate of 6% to finance the purchase of the hotel (as in note 2). The remaining interest expense was incurred on a bank overdraft utilised for the company's ongoing commercial operations.
6. The bad debts charge in the draft income statement comprises a debt of €500 which was written off in previous years but recovered during 2008, and with respect to current debtors, a provision of €1,260 which the company's directors deemed it prudent to make in respect of amounts the recovery of which is doubtful.
7. Wages and salaries include an entertainment allowance amounting to €50 a month to each of the company's two directors. The allowance is paid to them in cash and not reported under the Final Settlement System Rules.
8. During 2008, the company sold the following fixed assets:
   (i) A non-commercial vehicle that had been bought in 2006 for €28,000, depreciated at 20% a year for two years and sold in 2008 for €21,800.
   (ii) A decorative work of art that had been bought in 1994 for €18,000 and which was sold for €20,000. No depreciation or wear and tear allowances were ever availed of on this work of art.
   (iii) Office furniture that had been bought in 2005 for €20,000, depreciated at 10% a year for three years and sold in 2008 for €23,000.

Required:

(a) Compute the chargeable income of Patina Limited for the year of assessment 2009 by adjusting the profit before tax figure as per the draft income statement of €114,740. (18 marks)

(b) Compute the tax payable by the company for the year of assessment 2009, clearly distinguishing between the tax payable on each source of income. (7 marks)

(25 marks)

3 Mistral Enterprises Limited was incorporated in 1997 with an issued share capital of 20,000 ordinary shares of €1 each and 10,000 7% non-redeemable preference shares also of €1 each. The share capital was subscribed for by Joseph Stivala and Mario Cutajar as follows:

	Ordinary Shares	**Preference Shares**	**Total**
Joseph Stivala	15,000	4,000	19,000
Mario Cutajar	5,000	6,000	11,000
Total	20,000	10,000	30,000

In 1999 another 10,000 ordinary shares of €1 each were allotted to Joseph Stivala, at par. In 2000, the company bought a showroom for €40,000 and in 2001 it spent a further €15,000 to build another floor on the showroom.

The company's balance sheet on 31 December 2007 was as follows:

	€
ASSETS AND LIABILITIES	
Non-current assets	
Property	55,000
Plant and machinery	22,000
	77,000
Current assets	
Stocks	12,000
Debtors	18,500
	30,500
Total assets	107,500
Current liabilities	
Creditors	9,500
Accruals	2,500
Total liabilities	12,000
Net assets	95,500
EQUITY	
Share capital	40,000
Retained earnings	55,500
Total equity	95,500

The retained earnings figure, all of which, for tax purposes, is allocated to the Maltese taxed account, is made up of the following:

	€
Retained earnings brought forward on 1 January 2003	33,050
Profit in 2003 net of €3,500 tax	6,500
Profit in 2004 net of €5,250 tax	9,750
Profit in 2005 net of €6,300 tax	11,700
Loss in 2006 (no tax chargeable)	(2,400)
Loss in 2007 (no tax chargeable)	(3,100)
Retained earnings on 31 December 2007	55,500

In view of the losses incurred in 2006 and 2007, the shareholders decided to sell the business and retire. In March 2008 they received an offer from the directors of Millennium Ltd who offered to buy all the ordinary shares for €5 per share and all the preference shares for €1·2 per share.

In April 2008, they were approached by the directors of another company Spiral Ltd who offered to buy the property from the company for €120,000, which was considered to be the property's market value at the time.

The shareholders are undecided whether to sell their shares or sell the property and liquidate the company. They have appointed you as their tax consultant to advise them on which of the two offers will maximise their net of tax income from the transaction. They inform you that their marginal tax rate for the year of assessment 2009 will be 35%.

Required:

(a) Compute the net of tax income that Joseph Stivala and Mario Cutajar would receive should they decide to sell their shares in the company. (14 marks)

(b) Compute the net of tax income that Joseph Stivala and Mario Cutajar would receive if the company were to sell the property for €120,000 and be liquidated. You should assume that on liquidation the realisable value of the assets and liabilities will be the same as that indicated in the 31 December 2007 balance sheet; and clearly distinguish between the return of capital on liquidation and the final dividends payable from the Maltese taxed account and the final tax account. (6 marks)

(20 marks)

4 L Limited is a fully owned subsidiary company of H Limited. Both companies are resident in Malta for tax purposes.

The two companies' income and related expenses during the financial year ended on 31 December 2007 were as follows:

L Limited

	Rent (Note 1)	**Interest (Note 2)**	**Trading (Note 3)**
	€	€	€
Gross income/turnover	4,000	1,500	28,000
Expenses			
Interest	(300)	(800)	(6,000)
Ground rent	(600)	0	0
Other expenses	0	0	(29,000)
Net income/ (loss)	3,100	700	(7,000)

H Limited

	Dividend (Note 4)	**Dividend (Note 5)**	**Trading (Note 6)**
	€	€	€
Gross income/turnover	8,000	10,000	35,000
Expenses			
Interest	0	(2,000)	(4,200)
Other expenses	0	0	(21,000)
Net income	8,000	8,000	9,800

Notes:

1. Rental income of €4,000 consists of income from the rent of a showroom in Valletta to an unrelated company.
2. The gross interest income of €1,500 was received on a fixed deposit account held with a Maltese bank, out of which the bank withheld 15% final withholding tax. The interest expense consists of interest on funds borrowed from a related party, which funds were deposited in the fixed deposit account.
3. The net loss of €7,000 arose from the operation of a retail outlet in Sliema.
4. The gross dividend income of €8,000 consists of a dividend received from a Turkish company in which H Limited holds 1% of the issued share capital, which it had bought in 2007 for €100,000. The Turkish company deducted 23% withholding tax from the gross dividend.
5. The gross dividend income of €10,000 was received from a Maltese company's immovable property account, which was taxed at 35% at the level of the distributing company. The interest was payable on a loan taken out to finance the purchase of the ordinary shares from which the dividend was derived.
6. The net income of €9,800 arose on the operation of a business consisting of the buying and selling of giftware by wholesale.

Required:

(a) Calculate the chargeable income, tax charge and tax payable by L Limited for the year of assessment 2008 and allocate the income to the company's taxed accounts.

Note: you should ignore group loss relief/surrender. (8 marks)

(b) Calculate the chargeable income, tax charge and tax payable by H Limited for the year of assessment 2008 and allocate the income to the company's taxed accounts.

Note: you should ignore group loss relief/surrender. (5 marks)

(c) Briefly explain the restrictions contained in the group loss relief provisions regarding the surrender of losses which, had they been a profit, would have been allocated to the foreign income account, immovable property account or Maltese taxed account. (2 marks)

(15 marks)

5 The Value Added Tax Act makes provisions obliging certain categories of persons to register for value added tax (VAT) and granting other categories of persons an option to register.

Required:

(a) **Explain the provisions of article 10 of the Value Added Tax Act with regard to the registration of persons for VAT, clearly distinguishing between the registration obligations of persons established in Malta and of persons not established in Malta and indicating the period within which registration is to be effected.** (6 marks)

(b) **Explain the provisions regulating the registration of taxable persons not registered under article 10 and other persons under article 12 of the Value Added Tax Act, 'Registration of persons who make intra-community acquisitions'.** (4 marks)

(10 marks)

End of Question Paper