Fundamentals Level – Skills Module

Taxation (Malta)

Tuesday 6 December 2011

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 Euro
2. All apportionments should be made to the nearest month unless stated otherwise
3. All workings should be shown

TAX RATES AND ALLOWANCES

The following tax rates and allowances for the year of assessment 2011 are to be used in answering the questions.

Individual income tax rates

Resident individual tax rates

Married couples – joint computation:

€	€	Rate
0	to 11,900	0%
11,901	to 21,200	15%
21,201	to 28,700	25%
28,701 and over		35%

Other individuals:

€	€	Rate
0	to 8,500	0%
8,501	to 14,500	15%
14,501	to 19,500	25%
19,501 and over		35%

Non-resident individuals

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

Corporate income tax

Standard rate	35%

Value added tax (VAT)

Standard rate	18%
Reduced rate	5%

Capital allowances

Industrial buildings and structures

Initial allowance	10%
Wear and tear allowance	2%

Plant and machinery

Wear and tear allowance as indicated in the question where applicable

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

Index of inflation

1983	428·06	1997	567·95
1984	426·18	1998	580·61
1985	425·17	1999	593·00
1986	433·67	2000	607·07
1987	435·47	2001	624·85
1988	439·62	2002	638·54
1989	443·39	2003	646·84
1990	456·61	2004	664·88
1991	468·21	2005	684·88
1992	475·89	2006	703·88
1993	495·60	2007	712·68
1994	516·06	2008	743·05
1995	536·61	2009	758·58
1996	549·95	2010	770·07

Fringe benefit rates on cars

Vehicle use		Percentage 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%
Car value		
From	**To**	
€	€	
0	16,310	30%
16,311	21,000	40%
21,001	32,620	50%
32,621	46,600	55%
46,601 and over		60%

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Question 1 begins on page 6.

ALL FIVE questions are compulsory and MUST be attempted

1 Peter and Jane are married and live together in a home situated in Valletta, Malta. Both Peter and Jane were born in the UK and have UK passports. Peter was born in 1944 and Jane was born in 1945. They were married in Cyprus in 1969. In 2007 Peter resigned from his post as Chief Financial Officer with a UK registered multinational, sold his flat in the UK, moved to Malta permanently and established his domicile in Malta. Neither Peter nor Jane intend to go back to the UK and their plans are to spend the rest of their life in Malta. Peter and Jane spend most of their time in Malta but Jane cannot stand Malta's summer climate and the couple spend July, August and September in their cottage in the German Alps.

Peter sits on the Board of Directors of a number of Maltese listed companies and is employed as a full-time consultant with a Government owned company named TALMALTIN Limited. Jane is a wealthy heiress and owns a number of international business interests. She is the Chairperson of a Maltese philanthropic organisation, for which she receives an annual salary from the organisation. However, Jane does not keep the salary which she receives from the organisation but donates it to Community Chest Fund.

In the basis year 2010 Peter received the following gains and profits:

1. Director's fees totalling €30,000 from a number of companies listed on the Malta Stock Exchange. One of the listed companies provided him with the right to use a company car which the company bought last year for €100,000. The company paid for the fuel costs but insurance and maintenance expenses were borne by Peter.
2. A director's annuity of €5,000 paid by a company listed on NASDAQ. The annuity was received in Peter's Swiss bank account and not remitted to Malta.
3. Bank interest from his Maltese bank account of €10,000, net of final withholding tax.
4. The sum of €20,000 from the commutation of his UK pension. This sum was received in Peter's Maltese bank account.
5. Bank interest of €3,000 from his Swiss bank account. This bank interest was not remitted to Malta but was retained in Switzerland.
6. A salary of €10,000 from TALMALTIN Limited. Peter does not serve on the board of TALMALTIN Limited. Peter's contract of employment with TALMALTIN Limited provide for the following benefits:

   – an annual business related training package worth €300;
   – a vehicle allowance of €500;
   – an annual health insurance package worth €500; and
   – free accommodation in a flat in Swieqi worth €90,000.

   Peter does not use the Swieqi flat but he allows his son, a university student, to live in it.

In the basis year 2010 Jane received the following gains and profits:

1. A dividend of €300,000 from LuxCo, her family's Luxembourg resident company. The dividend was exempt from tax in Luxembourg.
2. A dividend of €15,000 from a partnership *en commandite* with capital divided into shares (Pcom) resident in a high tax jurisdiction. Jane owns 90% of the equity shares in the company. The dividend was received net of witholding tax at the rate of 15%. Pcom was liable to tax in the high tax jurisdiction and paid tax at the rate of 25%.
3. A net profit of €30,000 derived from the sale of the coin collection which she had inherited from her father in 1992.
4. A salary of €10,000 from the philanthropic organisation, which she donated to the Community Chest Fund. Jane's employment contract with the organisation provides that she is entitled to

   – ten free opera tickets, worth €100 each; and
   – the right to attend an annual seminar on corporate governance at her employer's expense at a cost €200.

   Jane used all of her opera tickets but asked her Chief Financial Officer to attend the seminar in her place.

Required:

(a) Calculate the chargeable income of Peter and Jane for the year of assessment 2011.

Note: you should list all of the items of gains and profits referred to in the question, indicating by the use of '0' any items which are not chargeable to tax. (14 marks)

(b) Calculate, the tax payable by Peter and Jane under joint computation for the year of assessment 2011 and determine whether the separate method of computation would have been more tax efficient. (4 marks)

(c) Jane is considering the transfer of a property situated in Barbados, which she inherited from her parents in 1992. The property was Jane's parents' matrimonial home and they had owned and occupied the property for over 40 years. When Jane inherited the Barbados property she declared the value of the property at €1,500,000. Now she is considering donating the property to the Government of Barbados. The deed of donation will bind the Government of Barbados to use the property as a home for the elderly. The current market value of the property is €2,000,000.

Required:

Advise Jane of the Maltese tax consequences of the proposed transfer of the Barbados property and calculate the tax payable (if any) by Jane. (4 marks)

(d) Jane is considering selling her shares in LuxCo to her step-brother. Jane owns 50% of the equity shares in LuxCo and has held the shares uninterruptedly for over 30 years. Jane would sell the shares to her step-brother for a total consideration of €5,000,000.

LuxCo's assets consist wholly or mainly of immovable properties situated in Tuscany. According to LuxCo's latest financial statements, its net asset value is €50,000,000 and its goodwill, based on twice the average profits before tax for the last five years, is €500,000. The net asset value of LuxCo based on its last audited accounts filed with the CIR by the 18 December 1992 was €40,000,000.

Required:

Advise Jane of the Maltese tax consequences of the proposed sale and calculate the tax payable (if any) by Jane. (5 marks)

(e) Jane is considering making a number of generous gifts.

Jane's aunt lives in a home for the elderly in Surrey, England but she can no longer afford to pay the €3,000 annual fees. Jane is considering paying the fees on her aunt's behalf.

Jane would like to provide sponsorship to five children from the orphanage down her road. The sponsorship will consist of full season packages at a Maltese football nursery, which runs activities approved by Kunsill Malti tal-Isport. The packages will cost €100 per child.

Jane supports immigrants and intends to donate the sum of €15,000 to provide for the subsistence of a meritorious immigrant to attend a full time course at the University of Malta.

Required:

Advise Jane as to whether each of the three proposed gifts can be claimed by way of a tax deduction. (3 marks)

(30 marks)

2 **(a)** MINMALTA Ltd (ML) is a company which is registered in the UK and which is listed on an exchange recognised under the Financial Markets Act. ML is effectively managed and controlled in Malta. The shareholders of ML are two individuals who are neither ordinarily resident nor domiciled in Malta and who derive no other income from Malta. Each shareholder owns 50% of the equity shares in ML.

The following profits (after tax) have been allocated to ML's tax accounts in 2010.

Final tax account (FTA)	Immovable property account (IPA)	Foreign income account (FIA)	Maltese tax account (MTA)	Untaxed account (UA)
€	€	€	€	€
100,000	15,000	5,000,000	10,000	(30,000)

Notes:

1. 50% of the profits allocated to the FTA consist of profits after tax derived from the transfer of property chargeable to property transfer tax. The remaining 50% was derived from profits after tax resulting from income which has been charged to tax under the investment income provisions.
2. Profits allocated to the IPA consist of profits derived from the disposal of shares in companies which own immovable property situated in Malta.
3. Profits allocated to the FIA consist of dividends received from fully owned subsidiaries resident in a number of tax havens outside the EU where the effective rate of tax was less than 5%. The flat rate foreign tax credit (FRFTC) has been used in relation to these profits.
4. Profits allocated to the MTA consist of interest from a Maltese bank account received gross.

ML pursues a policy of distributing all of its retained earnings to shareholders on an annual basis.

Required:

(i) **Calculate the tax paid by MINMALTA Ltd in respect of each of its tax accounts for the year of assessment 2011.** (5 marks)

(ii) **Determine the tax refunds (if any) due to each of MINMALTA Ltd's shareholders in respect of the distribution made from each of the company's tax accounts assuming they file tax returns in Malta for the year of assessment 2011.** (3 marks)

(iii) ML intends to relocate all of its back-office operations to Malta. In order to do so ML proposes to acquire the perpetual emphyteusis of an office block, which measures 500 square metres.

Assuming that in the year following the acquisition of the office block, MINMALTA Ltd will receive the same income as it received in 2010, determine the annual market rent profits allocation, the effect on the net dividend receivable by each of the company's shareholder's (other than from the untaxed account) and the tax refunds (if any) due to them as a result of the acquisition. (6 marks)

(b) GGANT Holdings Ltd (GL) owns 100% of the equity shares in NANU Ltd (NL). NL owns 60% of the equity shares in SUSS 1 Ltd (SL1) and 80% of the equity shares in SUSS 2 Ltd (SL2).

The income tax computations (before any group relief) of each of the four companies for the year ended 31 December 2010 are as follows:

Company	GL	NL	SL1	SL2
	€	€	€	€
Accounting profit/(loss)	180,500	70,000	(90,000)	(150,000)
Add depreciation	–	–	40,000	20,000
	180,500	70,000	(50,000)	(130,000)
Less capital allowances	–	–	(50,000)	(20,000)
	180,500	70,000	(100,000)	(150,000)

Additional information:

1. All four companies are resident in Malta and are not resident in another jurisdiction.
2. All four companies have accounting reference dates which begin and end on the same date.
3. All the chargeable income of NL, SL1 and SL2 is allocated to the Maltese tax account.
4. GL's income includes:
   - a royalty of €80,000 received from a foreign country which charged withholding tax of 20% but GL has lost all evidence of the tax paid abroad on this income; and
   - a dividend of €500 which was exempt from tax in terms of the participation exemption.

Required:

(i) Prepare the income tax computations of all four group companies assuming that the group policy is to minimise the tax liability of the group as a whole, and calculate the final income tax liability of GGANT Holdings Ltd for the year of assessment 2011. Clearly identify any unrelieved amounts carried forward.
(8 marks)

(ii) State the definition of an equity holding and explain the relevance of this definition for tax purposes.
(3 marks)

(25 marks)

3 (a) List the circumstances in which a taxpayer can opt out of property transfer tax and pay capital gains tax in respect of a transfer of property. (5 marks)

(b) Timothy Borg has decided to emigrate and is considering the sale of the following properties he owns in Malta:

1. A flat in Sliema, which he had inherited from his father in 2007. The deed of transmission recorded the value of the flat at €300,000. Timothy has lived in the house as his primary residence since he was a child. Timothy intends to sell this flat for €250,000.
2. The family's house in Tarxien, which Timothy had also inherited from his father in 2007. The house in Tarxien, which has been in the family for over 300 years, is very run down and in need of renovation. The deed of transmission recorded the value of the house at €1,500,000. Timothy intends to sell this house for €1,000,000, its current market value.
3. A summer residence in Saint Julians. The residence is in a designated area. Timothy bought this residence in 1996 for €650,000. Timothy has found a foreign buyer who is prepared to pay €1,200,000 for the property. Legal fees relating to the execution of the deed will amount to €1,000.
4. 500 shares in a company listed on the Malta Stock exchange. Timothy bought these shares for €100 each and intends to sell then at €120 each.
5. 500 Maltese government bonds of €50 each which he intends to sell at €100 each.
6. 500 shares which are subject to a fixed return. Timothy bought these shares for €100 each and intends to sell them at €110 each.
7. 50% of the share capital of his family's company which has an issued share capital of 50,000 ordinary shares of €1 each. Timothy had acquired these shares by title of donation in 2004. At the time of the donation, the shares were valued at €0·50 each. The net asset value of the company as at 31 December 2010 was of €60,000 and the company's two years' average profits for the five financial years immediately preceding the year in which the sale is to be made is €5,000. The transfer shall be made at a consideration of €25,000.

Timothy pays income tax at the marginal rate of 35%.

Required:

Calculate the tax payable in respect of each of the above sales transactions on the basis that Timothy's policy is to minimise his overall tax liability for the year. Clearly identify and give the reason for any transaction which is exempt from tax or on which no tax is payable. (12 marks)

(c) List the assets, other than immovable property, to which capital gains tax applies. (3 marks)

(20 marks)

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Question 4 begins on page 12.

4 Sally and Matthew have been living together for three years and intend to get married in 2013. They are both domiciled and ordinarily resident in Malta.

In 2005, Sally and Matthew established a partnership collectif, named SALMAT, to operate a small clothes shop in Sliema, Malta. SALMAT's deed of constitution provides that the profits and losses must be shared equally between Sally and Matthew. The financial results of SALMAT for the year ended 31 December 2010 are as follows:

	Note	€
Turnover		150,000
Cost of sales	1	(20,000)
Overheads	2	(50,000)
		80,000
Other income	3	20,000
Net profit		100,000

Notes:

1. Cost of sales includes the following:
   - a €1,400 VAT penalty for failing to provide a customer with a valid fiscal receipt; and
   - a fine of €100 for displaying clothes on the pavement outside the shop.
2. Overheads were made up of the following:

	Note	€
Depreciation	a	3,250
Wages and salaries	b	45,000
Professional fees	c	1,250
Impaired (bad) debts	d	500
		50,000

(a) The depreciation charge was arrived at as follows:

	€
Electronic equipment – 25% of €1,000	250
Commercial van – 20% of €10,000	2,000
Company car – 20% of €5,000	1,000
	3,250

The company car is used solely for business purposes.

(b) Wages and salaries comprise:

	€
Partners' salaries of €20,000 each per annum	40,000
Annual salary paid to the partnership's part-time sales girl	5,000
	45,000

The part-time salesgirl does not have a work permit and is not registered for FSS purposes.

(c) Professional fees are made up of the following:

	€
Accountancy and audit fees	500
Legal fees – litigation expenses related to SALMAT's application to open a shop-window overlooking the street	750
	1,250

(d) The impaired (bad) debts figure is made up of the following:

	€
General provision	300
Specific provision	100
Debt written off	100
	500

3. Sally's father has given her and Matthew the sum of €20,000 to help them out with their business.

Other information:

Matthew is studying at a recognised Maltese tertiary education institution and must pay annual fees of €5,000. He used to be married to a foreign lady but they separated in 2009. Matthew's deed of separation binds him to pay his estranged wife the sum of €2,000 per annum.

Sally is a single mother and maintains her and Matthew's two-year-old baby, at a cost of €5,000 per annum. She receives the children's allowance and also gets help from her parents.

In addition to their income from SALMAT, in 2011:

– Sally received interest of €30,000 (net of final withholding tax); and
– Matthew received rents of €20,000.

Required:

(a) Prepare a computation of taxable income for SALMAT Partnership Collectif for the year of assessment 2011. (6 marks)

(b) Calculate the chargeable income and tax liability of Sally and Matthew for the year of assessment 2011. (6 marks)

(c) Matthew and Sally are thinking of converting SALMAT into a limited liability company, SALMAT Limited, by converting their partnership quotas into shareholding quotas in the equivalent ratio (50:50).

Advise Sally and Matthew whether:

(i) there will be a tax charge when the partnership is converted into a limited company; and
(ii) they will be able to surrender future trade losses suffered by the limited company against their personal incomes for tax purposes. (3 marks)

(15 marks)

5 IVA Limited is a company established in Malta which supplies goods and services to non-taxable persons. The following information relates to IVA Limited's first value added tax (VAT) return. All figures are stated inclusive of VAT where applicable.

	Note	€
Local sales	1	30,000
Local purchases		3,000
Expenses	2	5,000
Capital expenditure	3	100,000

Notes:

1. Sales are all at the standard rate of VAT and net of a 5% discount for early payment.
2. Expenses include €500 in respect of tobacco and alcohol bought to entertain clients, and a commission of €600 paid to a sales manager. The sales manager did not issue a fiscal receipt.
3. 10% of the capital expenditure was spent on the acquisition of furniture and fittings and the remaining 90% on the acquisition of immovable property.

Required:

(a) Calculate the amount of value added tax (VAT) payable/refundable to IVA Limited for the relevant quarter. Indicate by the use of '0' any item for which VAT is not payable/deductible and state why. (6 marks)

(b) Define the concept of 'economic activity' and explain its relevance for the purposes of VAT. (4 marks)

(10 marks)

End of Question Paper