Answers

1 Formtex S.A.

(a) (i)

		PLN	PLN
2004 loss			270,000
Utilised	2005 (maximum 50%)	135,000	
	2006	24,000	
	2007	66,000	
			(225,000)
Available			45,000

(ii) The rules applicable in the calendar year in which the company's accounting period commences apply for the whole financial year. The rate of tax in force at the start of the financial year applies throughout the period.

(b) The conditions for a new technology relief claim are:

– the new technology must result in the production of new or improved goods or services;
– an independent scientific body must certify that the technology has been applied for less than five years anywhere; and
– the expenditure cannot be refunded in any form.

Up to 50% of the expenditure can be claimed as a deduction from income. Payments on account made the year before it is put into use are included.

If there is insufficient income the balance can be carried forward for relief for up to three years.

The relief will be withdrawn if within three years Formtex S.A. transfers the rights, receives a refund for them or is declared insolvent or liquidated.

(c) Taxable income and tax payable for the 16 months to 30 April 2009

	PLN	PLN
Profit per draft accounts		4,260,000
General research costs	47,000	
Market research costs	103,000	
Depreciation of intangible development (W1)	1,435,000	
Gross up Japanese withholding tax (W2)		36,000
Decrease in doubtful debt provision (521,000 – 77,000)	444,000	
Stock provision increase		165,000
Directors' payment not in contracts		660,000
Interest accrual increase (4,800 – 1,300)		3,500
Disallowed penalty interest		3,900
Revenue from machinery disposal		71,600
Book value of disposed machinery (520,000 – 509,600)	10,400	
Disallowed non-employee travel		84,700
Disallowed rehabilitation fund		34,600
Disallowed environmental penalties		66,300
	2,039,400	5,385,600
		(2,039,400)
Taxable income		3,346,200
Less:		
Relief for losses brought forward (as in (a)(i))		(45,000)
New technology relief (W1)		(1,230,000)
Tax base		2,071,200
Tax at 19%		393,528
Less:		
Relief for Japanese withholding tax (W2)		(21,169)
CIT payable		372,359
Payments on account (W3)		(30,400)
Tax payable		341,959

WORKINGS:

(W1)	Cost of new technology (246,000 + 2,214,000)	2,460,000
	New technology relief 50%	(1,230,000)
	Balance	1,230,000
	Depreciation over 12 months: 7/12 x 2,460,000	1,435,000
	Depreciation cannot be over a period shorter than 12 months, and expenditure subject to new technology relief can be depreciated.	
(W2)	Gross patent income: 144,000 + (20/80 x 144,000 = 36,000)	180,000
	Japanese withholding tax	36,000
	Maximum double tax relief: 393,528 x 180,000/3,346,200	21,169
	Credit relief is limited to Polish tax applicable to the foreign income.	
(W3)	Deferred taxation entries are irrelevant.	
	Tax in declaration lodged in 2007, for 2006	nil
	Tax in declaration lodged in 2006, for 2005:	
	Income 255,000 – loss 135,000 = 120,000 x 19%	22,800
	Monthly payments in 2008/09: 22,800/12 = 1,900 x 16 months	30,400

(d) Only FOUR items required

1 The taxation rules give fixed rates of depreciation, which may differ from the realistic rates required by IAS16 to write off the depreciable amount over the expected useful life of the asset (for example one year for development expenditure).

2 A taxpayer can choose to reduce depreciation rates arbitrarily, contrary to the consistency principle.

3 The tax rules treat the cost of the asset as the depreciable amount, when in practice a business may wish to anticipate a residual value (or cost) in arriving at depreciation rates.

4 A taxpayer can apply straight-line or reducing balance method as it wishes for assets in the same category, in conflict with the principle of consistency.

5 Depreciable lives of used fixed assets are set by reference to cost for tax purposes, and not to expected useful life.

6 Relifing of an asset, when experience shows a business that existing rates are unrealistic, is not permitted under the taxation rules.

7 Revaluations as permitted or required by IFRS cannot be taken into account in setting depreciable amount for tax purposes.

8 The limit of PLN 3,500 for small assets which can be expensed may conflict with the principle of materiality: for small companies such assets may be material, and for a large company the limit may be too small.

9 The effect of new technology relief (and previously investment relief) causes a large write off early in the life of the asset, contrary to the matching principle, with no regard to the useful life of the asset. Also the relief may be arbitrarily continued for three years, depending on income, not on the actual life of the asset.

10 Since new technology relief is claimed as well as full depreciation charges, the taxpayer is able to charge more than the actual cost of the asset.

11 The increases in tax depreciation for 'heavy use' or bad conditions are arbitrary and may not reflect the actual experience of the business.

12 The Euro 20,000 restriction on depreciable cost for passenger cars means that the whole cost will not be depreciated.

13 The Euro 50,000 immediate writing off for new businesses conflicts with the principle of consistency.

2 Kazimierz, Ludwika and Maria

(a) Taxable income for the year ended 31 December 2008

	PLN	PLN
Profit per accounts		240,196
Revenue not yet earned	17,000	
Interest receivable accrual	680	
Private pension contribution disallowed		10,426
Hotels VAT (8,200 x 7%)		574
Excess meal allowance (29 x (100 – 24))		2,204
Excess kilometre rate (12,400 x 1·20)		14,880
Entertaining		1,200
Subscriptions, texts, papers – all allowed		–
	17,680	269,480
		(17,680)
Taxable income of partnership		251,800
Apportioned: Kazimierz 50%	125,900	
Ludwika, Maria 25% each	62,950	

(b) Tax payable 2008

	PLN	PLN
Kazimierz		
Income	125,900	
Tax on	85,528	20,178
40% on	40,372	16,149
Total payable by Kazimierz		36,327
Ludwika		
Income	62,950	
Relief for internet	(760)	
Tax base	62,190	
Half tax base (joint taxation)	31,095	
19% x 31,095		5,908
Less		(587)
		5,321
Total payable by Ludwika 5,321 x 2		10,642
Maria		
Income		62,950
Rehabilitation relief:		
Motor travel allowance	2,280	
Medicines (necessary) (2,930 – 1,200 lower limit)	1,730	
Staying in rehabilitation centre	5,160	
Maria's holiday – not allowed	–	
Home nursing	3,350	
Rehabilitation equipment	480	
		(13,000)
Tax base (no joint taxation)		49,950
Tax on	44,490	7,866
30% on	5,460	1,638
		9,504
Less child deduction: 1,174 x 4/12		(391)
Total payable		9,113

(c) Alternative PIT calculations for 2008

	Kazimierz PLN	Ludwika PLN	Maria PLN
Income	125,900	62,950	62,950
Tax at 19%	23,921	11,961	11,961
PIT (normal rules)	36,327	10,642	9,113
Tax saving/(additional tax)	12,406	(1,319)	(2,848)

(d) (i) The social insurance (ZUS) costs of a taxpayer registered for business activity can be treated as a relief from his/her income if it has not been included in business costs. Thus this plan is acceptable, if the partners agree.

The effect will be that the partners will have their own ZUS contributions allowed as a relief, rather than the total cost of 46,250 being in effect apportioned in the profit sharing ratio. Kazimierz will save a lot of tax (but not as much as under the 19% method), and his partners will suffer more PIT, but not sufficiently much to prefer the 19% method instead.

(ii) Change in Tax Liabilities

	Kazimierz PLN	Ludwika PLN	Maria PLN
PLN 46,250 cost not allowed	(23,125)	(11,563)	(11,562)
Relief claim	31,250	7,500	7,500
Reduction/(increase) in tax base	8,125	(4,063)	(4,062)
Marginal tax rate	40%	19%	30%
Tax saving/(additional tax)	3,250	(772)	(1,219)

3 (a) Walgron S.A. – Value added tax for the month of June 2008

		Input PLN	Output PLN
(1)	The customs office will charge input VAT on the customs value increased by the customs duties: ((120,000 x 3·1) + 29,760 = 401,760 x 22%)	88,387	
(2)	Not a passenger car, recover input tax (85,400 x 22/122)	15,400	
(3)	Self charge output VAT and claim for a similar input: (20,000 x 3·45 x 22%)	15,180	15,180
(4)	Input restricted to lower of 60% and PLN 6,000: (42,000 x 22% x 60%)	5,544	
(5)	Entertaining disallowed: no input recovery	–	
(6)	Such tickets satisfy the documentation requirements: (8,132 x 7/107)	532	
(7)	Samples are allowed: since the product is taken from stock, the relevant input tax has been claimed, and there is no output charge. Packaging etc input is (35,000 x 22%)	7,700	
(8)	Gifts to individuals in excess of PLN 100 per individual are taxable: (50 x 120 = 6,000 x 22%)		1,320
	Gifts below PLN 100 are allowed.		
	Gifts to staff are taxable (20 x 40 x 22%)		176
(9)	Input tax of (4,000 x 22% x 60%) = PLN 528, but the total for the car of PLN 6,000 is exceeded (see (4)): recover only (6,000 – 5,544)	456	
(10)	The conditions for bad debt VAT relief are satisfied. Correct the output tax for the relief (30,300 x 22%)		(6,666)
		133,199	10,010

(b) (1) The documents were received in time for the July declaration of 25 August. The export date is the tax point, and the sale (at 0% tax) will be included in the July return.

(2) Date of receipt, output tax PLN 1,803 (10,000 x 22/122).

(3) The date the goods were shipped out of the EU (Rotterdam).

(4) For the invoiced customer, within seven days of delivery; for the non-invoiced goods, upon delivery.

(5) The 15th day of month following delivery, or the invoice date if earlier.

4 (a) (i) Social Security contributions (ZUS) are required for income from employment, self employed business activity, and assignment contracts (‘*umowy zlecenia*’).

ZUS is always required for income from employment. If a taxpayer has both an employment for at least the minimum wage and business activity he generally will not need to pay ZUS on the business activity. For assignment contracts, ZUS is due, unless the taxpayer is already satisfying the ZUS obligation by employment (or business activity, although in such a case an assignment contract is unusual). However, assignment contracts for the employer of the taxpayer are treated as employment and subject to ZUS.

(ii) The disability pension contribution is only paid up to a maximum ‘upper earnings limit’ which is set before each year commences.

The accident benefit contribution rate for those employing more than ten workers will differ, depending on the particular industry of the employer. For assignment contracts performed off premises (not in the employer’s premises) the contribution is not due.

The guaranteed workers’ benefit contribution does not apply to registered business activity taxpayers, and also for some classes of employer, in particularly the State (and state railways, airports).

(b) Grzegorz

(i) Grzegorz is resident in Poland because his ‘centre of interests’ is now clearly in Poland, with his intent to stay and with his permanent employment in Poland.

(ii) Personal income tax for 2008

	PLN	PLN
Polish salary (7 x 4,000)	28,000	
Less: ZUS deducted 13·71%	(3,839)	
Less: allowed cost (7 x 111·25)	(779)	
Income from Polish source		23,382
South African salary	40,000	
Less: allowed cost (3 x 111·25)	(334)	
Less: overnight allowance (110 x 30% = 33 x 60)	(1,980)	
Income from South Africa		37,686
‘World’ income		61,068
Polish tax on	44,490	7,866
30% on	16,578	4,973
Total		12,839
Effective rate (12,839/61,068)		21·02%
Tax on Polish sources (only) (21·02% x 23,382)		4,915
Tax deducted by Polish employer 23,382 x 19%	4,443	
Less: (586·85/12 x 7 months)	(342)	
		4,101
Additional tax to be paid		814

5 (a) (i) (1) **Nieplynna Sp. z.o.o.**

The purpose of the plan is to avoid the ‘thin capitalisation’ rules in Poland, which disallow the interest expense on borrowings from parent and direct sister companies which exceed three times the Polish subsidiary company’s capital.

In either case (i.e. whether the plan is adopted or not) Nieplynna Sp. z.o.o. will pay annual interest of 5% x PLN 8 mln = PLN 400,000.

If the loan is advanced by parent company:

Interest is allowed on 3 x PLN 1 mln = PLN 3 mln.
Disallowed interest = 5% x PLN 5 mln = PLN 250,000.

If the loan is from the bank the entire interest is allowed.
Thus, Polish CIT saved is 19% x 250,000 = PLN 47,500.
However, the group will suffer a cost of 0·5% on the PLN 8 mln deposited with the bank at 4·5% which the bank will lend at 5%.

Annual cost to group is 0·5% x 8 mln = PLN 40,000
Resulting in a net annual saving of PLN 7,500
In addition the arrangement fee will cost PLN 20,000.
It seems that there is a saving only if the loan lasts over three years, and not a big one at that for the trouble involved.

(ii) (2) **Zyskowna Sp. z.o.o.**
This scheme is attempting to transfer profits from Poland, where they are taxed at 19%, to the Netherlands, where the profit will be taxed at only 12%. This is done by overcharging costs from the Netherlands to Poland by PLN (15 – 10) = 5 mln.

	PLN
Saving of Polish tax = PLN 5 mln x 19%	950,000
Additional Dutch tax borne = PLN 5 mln x 12%	600,000
Saving for group = PLN 5 mln x 7%	350,000

However, Zyskowna Sp. z o.o. and company XB are connected, since both are controlled by the Dutch company. Therefore, the Polish transfer pricing rules should be applied, and an investigation may result in this saving not in fact being made, with the additional risk of penalties.

(iii) (3) **Helena**
Helena is attempting to have her PLN 10,000 bonus transferred into 2009, where it will be subject to 18% PIT, whilst at present it will be taxed at her marginal rate of 30% (since her taxable pay is about PLN 73,000 before the bonus).

However, due to her earlier bonus, she is above the upper earnings limit in 2008, so the ZUS cost for her will be at a marginal rate of only 2·45% if the bonus is paid in 2008:

	PLN
Gross pay to date in 2008:	
12 x 5,500	66,000
June bonus	20,000
Gross pay before ZUS of 11,710 and cost of 1,335	86,000
This is above the upper earnings limit for ZUS of	85,290
In 2009, her earnings before bonus are only	66,000

So if the bonus is paid in 2009 it will be subject to her retirement and disability contributions, since the PLN 76,000 total is below UEL.

	2008 PLN	2009 PLN
Bonus	10,000	10,000
Employee ZUS (2·45%/13·71%)	(245)	(1,371)
	9,755	8,629
Tax (30%/18%)	(2,927)	(1,553)
'Take home' pay	6,828	7,076
		(6,828)
Saving for Helena		248
However Dobra S.A. will be reluctant to agree to defer the bonus, since in 2009 it will cost the company an additional employer's contribution of (9·76% + 4·50%) = 14·26% x 10,000 =		1,426
Overall Helena's plan will result in an additional cost of		1,178

(b) (1) In the case of the 'back to back' agreement with the bank there is some commercial sense in the transactions, other than the avoidance of tax. The bank is not a connected body. It seems that the plan is acceptable.

(2) The transfer pricing arrangement is clearly artificial, and deception is necessary for it to succeed. As such it is unethical, and the advisor should have nothing to do with it.

(3) Employer and employee can make whatever arrangement between each other that is convenient to them. There is nothing unethical about paying the bonus at a time which saves some tax, provided this does not conflict with legal documentation, for example a monthly salary required to be paid in the relevant month, or a contractual bonus due at a particular moment.

				Marks
1	(a)	(i)	Utilisation in 2005	1
			Utilisation in 2006	$^1/_2$
			Utilisation in 2007	$^1/_2$
				2
		(ii)	Rules and tax rate at start of period apply	1
	(b)		New/improved goods/services	1
			Certified as under five years old by institution	1
			Not refunded	1
			Include prepayments from prior year	1
			Claim 50% off income	1
			Carry forward up to three years	1
			Each reason for withdrawal $^1/_2$ mark, maximum	1
				7
	(c)		General research costs	$^1/_2$
			Market research costs	$^1/_2$
			Depreciation on intangible	1
			Gross up patent income	1
			Doubtful debt decrease	$^1/_2$
			Stock provision	$^1/_2$
			Supervisory board payment	$^1/_2$
			Interest accrual	$^1/_2$
			Penalty interest	$^1/_2$
			Fixed asset disposal: revenue	$^1/_2$
			book value	$^1/_2$
			Non-employee travel	$^1/_2$
			Rehabilitation fund	$^1/_2$
			Environmental penalties	$^1/_2$
			Loss relief	$^1/_2$
			New technology relief	1
			Tax calculation	$^1/_2$
			Deferred tax irrelevant	$^1/_2$
			Withholding tax, including limit	$1^1/_2$
			Payments on account: basis year, base, 16 months	2
				14
	(d)		Each valid point $1^1/_2$ marks, maximum	6
				30

			Marks
2	**(a)**	Revenue not earned	$^1/_2$
		Interest accrual	$^1/_2$
		Claim all ZUS	$^1/_2$
		Private pension disallowed	1
		Hotel VAT	1
		Excess meals	1
		Excess kilometres	1
		Entertaining disallowed	$^1/_2$
		Professional subscription, texts, newspapers – all allowed	1
		Apportion income	1
			8
	(b)	Kazimierz: computation of tax payable	1
		Ludwika:	
		Internet (limited)	1
		Computation on joint tax basis	1
		Computation of tax payable	1
		Maria:	
		Rehabilitation relief: motor car	1
		Medicines (less lower limit)	1
		Rehabilitation centre stay	$^1/_2$
		Holiday stay for Maria – not allowable	$^1/_2$
		Home nursing	$^1/_2$
		Equipment	$^1/_2$
		Computation of tax payable	1
		Child deduction	1
			10
	(c)	Tax at 19% on correct basis	1
		Compute saving	1
			2
	(d)	**(i)** Proposal is acceptable	$^1/_2$
		Effects of proposal	$1^1/_2$
			2
		(ii) Change in tax base	$1^1/_2$
		Correct marginal tax rate	$1^1/_2$
			3
			25
3	**(a)**	Items (1),(8) $1^1/_2$ marks	3
		Items (5),(6) $^1/_2$ mark	1
		Remainder 1 mark	6
			10
	(b)	Each item 1 mark	5
			15

				Marks
4	**(a)**	**(i)**	Identify the three sources	1
			Employment always due ZUS	$^1/_2$
			Self employment exempt if employed	$^1/_2$
			Contracts exempt if employed	$^1/_2$
			Except if for employer	$^1/_2$
				3
		(ii)	Upper earnings limit for disability	1
			Accident: variable rates, depending on industry	$^1/_2$
			Accident: none for off-premises contracts	$^1/_2$
			No guaranteed workers' benefit for 'self employed'	$^1/_2$
			State bodies exempt from guaranteed workers' benefit	$^1/_2$
				3
	(b)	**(i)**	Centre of interests	1
		(ii)	Polish salary less ZUS	1
			Cost allowance	1
			South Africa allowed cost	1
			Overnight allowance	1
			Cumulate both sources	1
			Calculate and apply effective rate	2
			Correct tax deduction during year	1
				8
				15
5	**(a)**	(1)	Explain thin capitalisation rules	1
			Compute disallowed interest	1
			Polish tax saving	$^1/_2$
			Group interest cost	$^1/_2$
			Arrangement fee cost	$^1/_2$
			Saving/conclusion	$^1/_2$
				4
		(2)	Identify transfer pricing issue	1
			Overall tax saving	1
			Possible risk of challenge/investigation and penalty	1
				3
		(3)	Utilisation of 18% rate	1
			Extra ZUS cost, over UEL	1
			Compute 2008 net bonus	1
			Compute 2009 net bonus, saving	1
			Extra cost to company	1
				5
	(b)		Each point explained correctly 1 mark	3
				15