Answers

1 Nowomiejska Sp.z o.o.

(a)

	PLN	PLN
Loss per accounts	851,000	
Disallow management charge (no documentation)		44,000
Disallow entertainment:		
Opening party		40,500
Entertaining councillors		16,120
Present to inspector		10,000
(advertising all allowed)		
Disallow exceptional losses:		
Lost deposit		37,000
Deszczotworca (not arising from revenue receivable)		20,000
Abandoned capital expenditure		87,500
(Small debts certified: allowed)		
Disallow equipment rentals (not an operating lease)		50,000
Claim finance charge (12,400 + 12,100)	24,500	
Depreciation:		
Kitchen equipment 300,000 x 14% x 3/12	10,500	
Office equipment 240,000 x 14% x 4/12	11,200	
Computers 96,000 x 30% x 2 x 4/12	19,200	
Fully claim small assets below 3,500	152,400	
Car: restricted to 20,000 x 3·6 = 72,000		
Allow 72,000 x 20% x 1/12	1,200	
Prepaid public liability insurance 42,000 x 7/12		24,500
Prepaid motor insurance 16,800 x 10/12		14,000
Disallow on excess over 72,000: 108/180 x (16,800 x 2/12)		1,680
Provision disallowed		9,700
Thin capital interest rules apply (over 25% held)		
Allow interest on borrowing to 3 x 1,000,000, so		
disallow on 1,000,000/4,000,000 x 60,000		15,000
Totals	1,070,000	370,000
	370,000	
Tax loss for the period	700,000	

(b) **(i)** If the tax office is not notified otherwise, the tax year will be to 31 December. If activities commence in the second half of the calendar year, the taxpayer can choose to extend his first tax year to the next 31 December after the one in the year of commencement. In the case of this company the directors may choose to have the 17 month period to 31 December 2009 as the first tax 'year'.

(ii) Notification of a chosen accounting date other than 31 December must be given to the tax office within 30 days of commencement of the business activity. In such a case the first tax year will be to the first occurrence of the chosen accounting date, even if the resulting 'year' is very short. There is no option to extend the period, unlike the situation where December is chosen and business commences in the second half-year.

(c) At present Nowomiejska Sp.z o.o. will have six tax years to the end of its loss-making phase to 31 December 2013. Since a tax loss can only be deducted from taxable income earned in the subsequent five tax years, and a maximum claim of 50% of a particular loss is permitted in any year, the company will not be able to relieve the 2008 loss, nor 50% of the 2009 loss it expects. There are several things management can do to reduce the losses that would not be recovered at present.

(i) The first tax period can be chosen to be the 17 months to 31 December 2009. In such a case there will only be five loss making periods to December 2013 and half of the 2008 loss (along with half of the 2009 loss already capable of deduction) can be claimed against the high 2014 income.

(ii) The amount of the early years' losses can be reduced significantly by not claiming the full write-down of the low value assets, but instead depreciating them normally. In particular it is likely that there will be many such asset additions as more restaurants open. These costs will still be recovered, but over a longer period, thus reducing the irrecoverable losses of 2008 and 2009.

(iii) Any taxpayer is in fact permitted to reduce (even to almost nil) allowed depreciation expenses, and to claim them later, with no loss of allowable cost. Clearly again, Nowomiejska Sp.z o.o. can take advantage of this option.

(iv) A lessor and lessee can allocate the finance charges in a finance lease however they choose. In theory Nowomiejska Sp.z o.o. could find a lessor who would agree to load the finance charge into the later part of a lease. This seems artificial and in practice it may be difficult to find a willing lessor.

(v) A simple but legitimate idea is probably the most effective, since the above plans might still leave a loss in 2008/09, only half of which can be offset, in 2014. There is no rule forbidding a company from changing its accounting date, and the first period to the new date must be extended to between 13 and 23 months, with no option of a shorter period. Thus for example, after December 2009, the directors could choose to change to November, causing the company's second tax year to run to 30 November 2011, and then have two profitable periods (to November 2014 and November 2015) to recover the 2008/09 loss (or alternatively decide to account to June, and then change back to December, causing two 18-month years to arise). These schemes will have the effect of spreading the loss-making phase of the company over a smaller number of tax years.

2 Dorota

(a) (i)

	PLN	PLN
Gross salary: 6 x 11,000		66,000
Foreign meals: 20 x 140	2,800	
Less: allowed 20 x \$40 x 2·25	(1,800)	
Taxable and charged to ZUS (flowers exempt – below PLN 380, social fund)		1,000
ZUS basis (Termination payment is exempt)		67,000
ZUS deduction 13·71% x 67,000		9,186
Salary + excess allowance (as above)		67,000
Termination payment		33,000
		100,000
Less: ZUS deduction		(9,186)
Basis for health service contributions		90,814
Less: cost allowance 111·25 x 6		(668)
Income		90,146
PIT deduction to May		
Salary 5 x 11,000		55,000
ZUS 13·71%		(7,541)
Cost allowance 111·25 x 5		(556)
Taxable at 19%		46,903
Balance: taxed at 30%: 90,146 – 46,903		43,243
		90,146

It is clear that Dorota's cumulative taxable income passes the first threshold of 44,490 in May, so her June payment of salary, excess allowance and termination payment (11,000 + 1,000 + 33,000 = 45,000 less 13·71% x 12,000 = 1,645 + 112, total 43,243) is taxed at 30%.

		PLN
Income tax:	46,903 x 19%	8,912
	43,243 x 30%	12,973
Less: 587 x 6/12		(293)
Total PIT deduction		21,592

(ii) The contract with Dziennik Wybrany S.A. does not fall into ZUS since Dorota was employed full-time in April.

	PLN
Fee	4,000
Allowed cost 20%	(800)
Taxable	3,200
PIT deduction 19%	608

(iii) The contract with Gazeta Nieprawna S.A. is subject to ZUS since Dorota had no other relevant income in August.

	PLN
Fee	10,000
ZUS 13·71%	(1,371)
HSC basis	8,629
Allowed cost 20%	(1,726)
Taxable	6,903
PIT deduction 19%	1,312

(b)

	PLN	PLN
Salary and excess allowance	67,000	
Less: ZUS	(9,186)	
HSC basis	57,814	
HSC deducted from PIT 7·75% x 57,814		4,481
Dziennik Wybrany S.A. 7·75% x 4,000		310
Gazeta Nieprawna S.A. 7·75% x 8,629		669
Total HSC to be deducted		5,460

(c) **(i)** ZUS: October and November basis salary is 2nd Quarter, December 3rd Quarter average salary.

		PLN
The rate is:		
ZUS: (18·61 – 0·10 + 13·71 – 2·45) = 29·77%		
October, November	3,080 x 60% x 29·77%	550
December	3,245 x 60% x 29·77%	580
HSC deduction from PIT		
October, November	3,080 x 75% x 7·75%	179
December	3,245 x 75% x 7·75%	189

(ii)

	October PLN	November PLN	December PLN
Cumulative revenue	3,000	10,500	20,000
Cumulative costs	(450)	(1,400)	(2,000)
Cumulative income	2,550	9,100	18,000
Cumulative ZUS (from (i))	(550)	(1,100)	(1,680)
Tax base	2,000	8,000	16,320
Tax at 19%	380	1,520	n/a
Less:	(587)	(587)	
Payable	nil	933	
Less: HSC (2 x 179)	n/a	(358)	
PIT due for month		575	
Tax payable for October (due 20 November)			nil
Tax payable for November and December (due 20 December) 2 x 575			1,150

(d) (i)

	Revenue PLN	Cost PLN	Income PLN
Employment ((a)(i))	100,000	668	99,332
Contract 1 ((a)(ii))	4,000	800	3,200
Contract 2 ((a)(iii))	10,000	1,726	8,274
Business activity ((c)(ii))	20,000	2,000	18,000
	134,000	5,194	128,806
ZUS deducted/paid			
Employment ((a)(i))		9,186	
Contract ((a)(iii))		1,371	
Business activity ((c)(ii))		1,680	
			(12,237)
Income			116,569
Relief for donations (both churches and public benefit organisation)			(1,000)
Tax base			115,569
Half tax base	57,784		
Tax on	44,490		7,866
30% on	13,294		3,988
			11,854
Total tax 11,854 x 2			23,708
Less: HSC allowed 5,460 + (179 x 2) + 189			(6,007)
			17,701
Child deduction			(1,174)
Tax liability for year			16,527
Less: paid/deducted in year			
Salary ((a)(i))		21,592	
Contract 1 ((a)(ii))		608	
Contract 2 ((a)(iii))		1,312	
Less: HSC on above (b)		(5,460)	
Business activity tax less HSC ((c)(ii))		1,150	
			(19,202)
Refund due			2,675

(ii) The refund will be received within three months of the date Dorota submits her return.

3 Edukon Sp.z o.o.

(a) Taxable input proportion = 27,700,000/35,000,000 79·14%
Rounded up to the nearest full percentage point 80·00%

	PLN
Output	
Consulting (3,600,000 x 22%)	792,000
Educational (exempt)	0
Market research fee: import of services (227,273 x 22%) (self charged output tax)	50,000
	842,000
Input	
Market research fee (50,000 x 80%)	40,000
Educational direct costs (no recovery)	0
Consulting direct costs (514,000 x 22%)	113,080
Indirect costs (120,000 x 22% x 80%)	21,120
Consulting activity software (150,000 x 22%)	33,000
Educational activity equipment (no recovery)	0
Telephone switchboard – joint activity (125,000 x 22% x 80%)	22,000
Joint fixed assets below 15,000 (78,409 x 22% x 80%)	13,800
	243,000
Tax payable for July 2008	599,000

(b) (i) If the proportion of prior year taxable activity to total activity, rounded up to nearest full percentage point, exceeds 98% then full recovery is made. Thus if exempt activity in the previous year comprised less than 2·0% of the total, a company claims full input recovery during the year, but will still need to make the annual calculation at the year end, which may result in a correction.

(ii) In January 2009 Edukon Sp. z.o.o. will calculate the actual 2008 annual taxable proportion and correct the 2008 input to that proportion, paying or recovering the difference with its January 2009 VAT.

For joint activity moveable fixed assets costing over PLN 15,000 acquired in 2008 and during the previous four years the difference between the input VAT originally claimed and that resulting from the actual 2008 proportion is calculated. An adjustment of one fifth of this difference is made.

Even if the taxable proportion exceeds 98% in future years, Edukon will need to do the annual calculation while it continues to have any exempt activity, and continue to adjust for fixed assets for five years after acquisition.

(iii) Name and address of both parties.
Tax identification number (NIP) of both parties.
Date of sale, or month for continual services.
Sequential invoice number.
Name and type of service.
Unit price (if relevant) excluding VAT.
Total of each service excluding VAT.
Rate of tax.
Total value of sale, net of VAT.
Amount of tax.
Gross amount of sale, including VAT, in words and numbers.

Note: only SIX items required.

4 (a) Adrian

Adrian's sales to registered VAT payers will not alter, since they will be able to recover the VAT he charges on his revenue of PLN 30,000 (75% x 40,000).

	PLN
His PLN 10,000 invoiced to non-registered individuals must now include 22% VAT, so he will need to reduce the net values of these invoices by 22/122 of the existing amount, reducing his revenue by 22/122 x 10,000	(1,803)
He will recover input tax on his purchases of 22% x 13,000	2,860
Thus he achieves a net annual saving of	1,057
In addition, he will be able to recover input tax on his fixed asset purchases of 22% x 5,000	1,100

(b) Barbara

Currently Barbara is a highest rate taxpayer, so she pays PIT on the rental income at a marginal rate of 40%.

	PLN	PLN
Revenue (3,000 x 12)		36,000
Depreciation 1·5% x (101 x 988)	1,497	
Other costs	4,503	
		(6,000)
Taxable income		30,000
Tax at 40%		12,000
Flat rate tax on 36,000		
On first 15,072 at 8·5% =		1,281
On remaining 20,928 at 20% =		4,186
		5,467
Saving if she uses the flat rate method		6,533

(c) Cyprian

Apprentice does not affect the tax charge.

January to August (eight months): Daniel not included in determining number of skilled workers.

	PLN
One engineer: monthly tax per table:	450
plus administrator and Daniel: 2 x 30% = 60%	270
	720
But maximum = tax table for two, so monthly tax is	567

From September (four months), Daniel is no longer part of the taxpayer's household so he is included, hence now two engineers:

	PLN
Tax for two per table	567
Plus 20% for administrator	113
Monthly tax	680
Total = 8 x 567	4,536
4 x 680	2,720
	7,256

(d) Adrian

There are many administrative and regulatory matters for VAT payers, so requiring businesses with small volumes of activity to register

- (i) Will cause a lot of administrative effort for tax authorities, since there are many such businesses.
- (ii) Will increase costs and time spent by small traders in complying. They may need professional assistance which they cannot afford.

In addition European Union laws universally exempt small traders from a requirement to register.

Barbara

- PIT payers generally lack the knowledge of detailed rules for determining income, so this easier method was introduced as it avoids (i) computation of income, (ii) cumulation.
- The method is easy to check for tax offices, and gives less scope for manipulation by taxpayers.

Cyprian

- The tax card system is easy to operate and requires no tax law knowledge, it has existed for many years and is understood by the relevant taxpayers.
- It makes administration easy for tax offices.
- It provides continuous regular tax income even if a business makes losses.

5 Drewniana S.A.

(a) (i) If a permanent establishment is held to exist, the Polish company is deemed to have a presence in the other country and it will need to account for income taxes on profits made there, under the tax laws of that country.

(ii) The following do not result in Drewniana S.A. being regarded as operating a permanent establishment in Sweden:

(1) exhibitions of products;
(2) information gathering activities;
(3) an agent who is not able to negotiate/complete sales contracts on its behalf;
(4) holding inventory in the country; and
(5) storage and distribution facilities.

The following will constitute a permanent establishment:

(i) an agent who can take decisions on behalf of the Polish company;
(ii) a place of management; and
(iii) a branch.

(b)

	Head office PLN	Swedish branch PLN
Profit per accounts	5,014,000	320,000
Gross up dividend (W1)	35,000	
Withholding tax on interest (W2)	1,000	
Disallow Swedish depreciation		210,000
Claim 'Polish' depreciation		(124,000)
Cross-charge manager's salary	100,000	(100,000)
Disallow entertaining		44,000
	5,150,000	350,000
	350,000	
Taxable income	5,500,000	
Corporate income at 19%		1,045,000
Double tax relief:		
Norwegian tax on dividend (W1)		(23,750)
Withholding tax on interest (W2)		(1,000)
Swedish tax on income (W3)		(66,500)
Polish tax payable		953,750
Less: paid on account		(833,750)
Final CIT liability		120,000

Workings

		PLN
1.	Net Norwegian dividend received	90,000
	Gross up for withholding tax 10/90	10,000
		100,000
	Gross up for underlying income tax 20/80	25,000
	Gross income	125,000
	Norwegian tax (10,000 + 25,000)	35,000
	Maximum double tax relief 19% x 125,000	23,750
2.	Interest received from Sweden	19,000
	Gross up for withholding tax 5/95	1,000
	Gross income	20,000
	Full relief for tax paid of PLN 1,000 (less than 19% x 20,000)	
3.	Swedish income paid on profits	79,000
	Maximum relief 19% x 350,000	66,500

					Marks
1	**(a)**	Management charge			1
		Entertaining – each disallowed item 1/2, allowed remainder 1/2			2
		Exceptional items – each disallowed item 1/2, small debts allowed 1/2			2
		Lease – disallow rent 1/2, claim finance charge 1			1 1/2
		Depreciation: kitchen equipment			1
		Office equipment			1/2
		Computers – double rate			1
		Full write-down of small items			1/2
		Motor car restricted			1
		Public liability insurance prepayment			1/2
		Motor insurance prepayment			1/2
		Motor insurance restriction			1
		Provision			1
		Thin capitalisation – disallow 1/2, compute on the correct basis			1 1/2
					15
	(b)	**(i)** Automatic December year end			1
		Can extend to next December			1
					2
		(ii) Inform upon registration			1
		First period less than 12 months			1
					2
	(c)	Identify extent of potential unrelieved losses			1
		For each clearly explained point:			
		Extend first period to 17 months		2	
		No claim for small assets		1	
		Reduce depreciation charges		1	
		Delay finance charges		1	
		Change accounting dates		2	
		Any other rational ethical points (1 each)			
		Maximum			5
					6
					25

				Marks
2	(a)	(i)	Gross salary	$^1/_2$
			Foreign meals	1
			No ZUS on termination payment	$^1/_2$
			Flowers exempt	$^1/_2$
			ZUS calculation	$^1/_2$
			Termination payment taxable	$^1/_2$
			ZUS deduction	$^1/_2$
			Cost allowance	1
			Computation of 30% PIT basis	2
			PIT calculation	1
				8
		(ii)	No ZUS	$^1/_2$
			Allowed cost	1
			PIT deduction 19%	$^1/_2$
				2
		(iii)	ZUS – rate	$^1/_2$
			Allowed cost/basis	1
			PIT deduction 19%	$^1/_2$
				2
	(b)		Identify correct basis for each at 1 mark, total	3
	(c)	(i)	Correct ZUS rate	1
			Correct months for basis salaries	1
			ZUS 60% of basis salary	$^1/_2$
			HSC 75% of basis salary	$^1/_2$
				3
		(ii)	Correct income cumulation	1
			Deduct ZUS paid	$^1/_2$
			Tax on cumulated income	1
			Correct HSC deduction	$^1/_2$
			December PIT	1
				4
	(d)	(i)	Cumulation of all income	1
			Deduct all ZUS	1
			Correct reliefs	$1^1/_2$
			Compute tax as single parent	1
			Deduct HSC	$^1/_2$
			Child deduction	1
			Minus tax paid in year	1
				7
		(ii)	Three months after return	1
				30

			Marks
3	**(a)**	Correct taxable percentage	1
		Consulting output	$^1/_2$
		Educational (exempt)	$^1/_2$
		Market research output	$^1/_2$
		Input: market research	$^1/_2$
		Direct costs (2 x $^1/_2$)	1
		Indirect costs	$^1/_2$
		Direct fixed assets (2 x $^1/_2$)	1
		Joint fixed assets (2 x $^1/_2$)	1
		Total payable	$^1/_2$
			7
	(b)	**(i)** Exempt activity below 2%	1
		Full claim for input during year	1
			2
		(ii) Actual calculation for year	1
		One fifth for five years' fixed asset additions	1
		Continue while exempt activity exists	$^1/_2$
		Plus later adjustments for fixed assets	$^1/_2$
			3
		(iii) Each point listed $^1/_2$ (maximum 6)	3
			15
4	**(a)**	Cost of revenue reduction for individuals	1
		No change for registered taxpayers	$^1/_2$
		Cost input recovery	1
		Net annual saving	$^1/_2$
		Fixed asset recovery	1
			4
	(b)	Depreciation calculation	1
		Taxable income calculation	$^1/_2$
		Tax at 40%	$^1/_2$
		First part of revenue at $8^1/_2$%	1
		Excess at 20%	$^1/_2$
		Saving	$^1/_2$
			4
	(c)	Apprentice does not affect charge	$^1/_2$
		Daniel included as standard worker only from September	1
		First period calculation	1
		Limit to next (2) level	$^1/_2$
		Second period calculation	1
			4
	(d)	One reason for each case at 1 mark each: total	3
			15

				Marks
5	**(a)**	**(i)**	Effect: tax presence in the other country	1
			Liable to account for tax locally	1
				2
		(ii)	Not permanent establishment:	
			Exhibitions	$^1/_2$
			Information gathering	$^1/_2$
			Independent agent	$^1/_2$
			Inventories	$^1/_2$
			Storage & distribution facilities	$^1/_2$
			Permanent establishment:	
			Dependent agent	$^1/_2$
			Place of management	$^1/_2$
			Branch	$^1/_2$
				4
	(b)		Gross up dividend, including underlying tax	2
			Withholding tax on interest	$^1/_2$
			Amend depreciation	1
			Cross-charge manager	1
			Disallow entertaining	$^1/_2$
			Cumulate branch	$^1/_2$
			Tax on total income	$^1/_2$
			Deduct: Norwegian dividend tax (restricted)	1
			Tax on interest	$^1/_2$
			Swedish income tax (restricted)	1
			Polish on account tax	$^1/_2$
				9
				15