



# Examiners' report

## F6 Taxation (POL)

June 2008

This was the second Polish Tax examination under the new syllabus. It comprised five compulsory questions, two longer ones for 25 and 30 marks on corporate and personal income tax, a 15 mark question on VAT and two further 15 mark questions concerning transfer pricing, personal income tax and social security contributions.

Most candidates attempted all questions, and clearly demonstrated a good grasp of the whole syllabus: this examination touched a few areas previously not examined in depth, so the good overall result is pleasing. There were some excellent texts, and most candidates passed fairly comfortably. However, it is important that candidates read and follow the requirements to avoid wasting time providing unnecessary calculations. An organised layout of answers will make it easier to demonstrate their ability and knowledge.

As always some common gaps in knowledge and technique were exhibited, which have been dealt with for each question below.

### Question 1

The technical part of this question concerned the tax treatment of accruals, prepayments, interest and provisions following recent change in tax law. Given that this change was significant, and the first one in this area for some years, it was surprising how few candidates had heard of it. Only a handful understood the treatment of invoices received after the year end, and many were not aware of prepayment and accrual tax treatment. However, most were able to score some easy marks on allowability of provisions and interest. The performance on this part (8 marks) was generally disappointing.

The computational part for 17 marks presented fewer difficulties. It developed concepts of accruals, interest and provisions covered earlier, and here candidates had little trouble, with one exception noted below. Also the disallowed costs in Article 16.1 are well understood.

The most common mistakes were:

- Well over half of candidates disallowed the entire closure provision of PLN 2.7 mln, when PLN 2.2 mln of it would clearly have been disallowed when created in the previous year, and only the PLN 0.5 increase becomes disallowed in present year. This mistake surprised me since most candidates had correctly answered part (a) about provisions.
- Many students correctly took depreciation on used plant at 1/36, but in addition claimed only 14%. Whereas this was the first time used plant occurred in the examination, used motor vehicles, depreciated over 30 months, have featured regularly in the past and caused no problem.
- The rent prepayment was taken at 6/12, not 5/12, and many disallowed rent entirely or claimed it fully, again contrary to answers in part (a)
- Some failures to gross up for foreign withholding tax on patent royalties, also disallowing the revenue, or adding all gross revenue when the net amount was already included.
- Some errors on exempting Polish dividends. However most students remembered to reduce final tax by both withheld foreign tax and the Polish dividend tax credit.
- A few failed to disallow the loss on abandoned plant and on the uninsured motor car.
- Overall, the computation was well done and the layout was improved, enabling the considerable majority of students to score well over half marks for the question.

### Question 2

The personal income tax (PIT) question dealt with an individual starting a business activity and needing advice on taxation of profits, including deciding which method of the several available ones to choose. The facts and requirements were straightforward, and most students scored well, with a few perfect, or near-perfect answers.

In (a), a simple ZUS computation, many ignored the instruction to use November 2007 rates for what was after all a projection into the future, and split the computation between the two rates in force during 2007. They were awarded full marks, but if they had followed the instructions they would have had more time available.

The profit calculation and basic PIT computation for 11 marks was done well. Some performed unnecessarily tedious calculations on the employee salary and ZUS cost, which were simple if done globally, and surprisingly many, having computed employee ZUS, forgot that the basic salaries, totalling PLN 80,000, were also a cost. A fair number failed to claim 100% depreciation under the new rules. Reliefs were generally properly claimed and candidates did understand and correctly apply the new tax relief for children, although a few took PLN 120, which had been amended in late 2007 to PLN 1,145, as given in the tables on the first pages of the examination paper.

For the 19% flat rate alternative, a few students claimed all reliefs or failed to note that taxpayer's own ZUS can be claimed as a cost. Virtually all stated that a disadvantage of this method was that single person taxation did not apply, not thinking that the single person taxation method exists to double the lower rate tax bands, whereas under the 19% flat rate method all income is taxed at 19% anyway. The disadvantage that almost nobody mentioned was the loss of the "free amount" (twice in the case of single parent). The obvious disadvantages are of course lack of reliefs or (at present) child deduction: pointing out these last two gave students the full marks available.

There were few problems with the flat rate method, although prior year turnover limit (or current year as some incorrectly stated) is not a condition in year of commencement. Again quite a few students failed to claim the PIT reliefs as a deduction from revenue. Similarly the tax card option was explained very well. The final choice was answered well but full marks were only awarded to those who explained the effect on taxable profit of there being no further depreciation cost for some time. Other reasons, such as possible remarriage or children coming of age were not awarded marks, since the children were stated to be young, and no romantic implications were provided in the text.

Overall, students impressed with their overall grasp of Poland's unique and varied taxation methods for businesswomen and men.

### Question 3

The VAT question concerned the basic VAT account mechanism. It was answered poorly, with the lowest average mark of the whole examination.

The most common errors included:

- Charging output tax at 22% on intra EU sales (and occasionally also on extra EU exports).
- Failure to add import duties to arrive at taxable customs value.
- Failure to self-charge output tax on intra EU imports, or to claim identical input: also for services imported.
- Failing to claim, or claiming too much input on passenger motor car.
- Virtually all failed to restrict lease instalment VAT on passenger motor car to 60%.
- Some errors on passenger motor car fuel (disallowed) as opposed to fuel for "business" vehicles (allowed).
- Correctly stating that hotel stays are taxed at 7%, which is irrelevant, and incorrectly claiming input tax.
- Incorrect treatment of donated inventory (where input tax must have been claimed on production/purchase) which needs to have output tax paid for with no further input claim, and presents bought, where no input recovery is allowed since item was bought for non-business purposes. In the latter case students who claimed input and charged output were awarded the mark.

Poor layout of the VAT account by some students did not help clarity: a two column layout is best, where it can easily be seen where input is claimed/output payable, and the self-charging and claiming mechanism is immediately apparent. A phrase of explanation is also appropriate against each point.

Relatively few candidates performed well on this question.

#### **Question 4**

The question dealt with definition of connected persons, determination of fair price, and creation of arguments to justify apparently not fair prices within a group. It was expected to be challenging; however candidates demonstrated a good grasp of the topic and ability to justify transaction prices with intelligence.

The circumstances in which transfer pricing rules are applied were not always familiar: the situation concerned groups with foreign bodies, so family connections are less relevant, and of course rules are only applied if the Polish body reduces its local tax by the various mechanisms.

The three methods of fair price determination were reasonably well explained, but for two marks each a full definition and explanation of application was required. It was clear that some candidates had studied the topic well, as they pointed out that the “non-controlled” price was rarely available.

The justifications for low intra-group prices in the case study were universally spotted and well explained.

Many students scored well on this question, with several perfect answers.

#### **Question 5**

The first part of this question invited candidates to discuss effects of fiscal policy, a rarely examined area of the syllabus, and most rose to the challenge excellently. However, one point is that the employee rate decrease in July 2007 does not reduce employment costs, whereas the later employer contribution drop does. Many correctly linked the reduction with additional VAT collection from increase in consumption, and income taxes from the lowering of the PIT base, and further employment increase, and the danger of inflationary pressure (as is indeed occurring) was picked up often. Reduction of the grey economy seems also to be a fairly frequently suggested effect, which earned a mark.

On the other hand, the simple net pay calculation for Magda the statistician caused universal grief, with only a minority performing the take home pay calculation for 4 marks correctly. The most common errors were reducing her cash pay by the flat rate cost allowance used to arrive at income, and confusion over the health service contribution, taking it off tax base, or computing it twice, when for the purposes of the requirement only the additional 1.25% cost was of interest to Magda. A surprising number of candidates spent time computing June pay, which was not requested, and had they not done so more time would have been available to spend elsewhere on the paper.

As mentioned in the last examiner’s report clear thinking and tabulation of sometimes complicated calculations are skills expected of candidates. In part (b) a little planning of lay-out of answer would have enabled the computational element to have been done efficiently.

In part (c) candidates did well, with only a handful struggling, and some giving credit for dividend tax or cumulating interest income. Students are reminded that the interest tax is an income tax (not a Belka tax, as many named it), and the incidence and rate were expected to be known.

It was pleasing that most explained exclusion with cumulation well, with only a few claiming credit relief, or failing to understand the method.

The majority of candidates scored well on this question.