Examiners' report

F6 Taxation (POL)
December 2008

This Polish Tax examination followed the standard format of five compulsory questions. The two long questions comprised of corporate income tax concentrating on reliefs with a simple computational element and straightforward decision on relief claims, and a relatively undemanding question on a husband and wife with salary and self employment. The VAT question worth 15 marks primarily was on input tax refunds. The fourth question covered some basic administrative/structural matters including tax arrears. The final question dealt with rules for determining an individual's tax residence together with a computation of tax liability of an individual with some foreign sources of revenue.

The examiner previously expressed concerns for candidates who failed to read and follow the question requirements. This again was apparent with misunderstandings in Question 1 parts (d) and (e). Unnecessary calculations featured in Question 2 and a failure to perform some simple calculations in Question 3(a) and 5(b). Many candidates' lost valuable time and marks here. The examiner is pleased to note that the point he made previously about disorganised layout of answers, causing many candidates to do less well, seems to concern a smaller (but still significant) proportion of candidates now. The computational elements of Question 2 in particular and also Questions 1(d), 4(c) and, surprisingly, the VAT account in 3(a) were often done poorly, making the marking task difficult. The accountant's basic ability to lay out a simple computation is thoroughly tested in tax examinations, and it appears that many candidates sorely missed their computers!

Interestingly, there were elements of the examination which only a small portion of candidates got right. These are further discussed in the question analysis below including the more common failures and comments on performance. The commentary should provide useful insight for future candidates.

Question 1

Deduction from income (or reliefs) are a very important (and in Poland a frequently changing) element of all tax legislation, so the main CIT question mainly tested knowledge of the few remaining reliefs against corporate income. Some students will recall such reliefs from the past as relief for apartment building, for employing prisoners, and of course the intricate investment reliefs that ended a few years ago, never mind the twenty or so that were available to PIT payers. Given that there are presently so few left and that they can significantly affect a final tax liability, a fairly deep understanding of them was expected and in most cases found to be seriously lacking.

Loss relief in (a) generally presented a few difficulties. However, some students stated that, "assuming full available loss relief had not been claimed in the past" 50% of the 2003 loss remained to be claimed. This would surely have lost the chief accountant of Rewolucyjna S.A his job, since 2008 is of course the last available year of claim. The examiner provided a 5 year analysis of losses/income and the inference that all available relief had been taken in the past is fairly obvious. This element required maximum relief to be computed and did not require restricting it to the PLN 240,000 given later in the question for parts (d) and (e).

Since it is considered that future economic wellbeing of nations is determined by investment and innovation, good knowledge of the new technology investment relief was expected: it has been around for over two years, so ignorance of it as "new" does not constitute an excuse for the poor standard of understanding of its conditions and application. No candidate stated that expenditure had to be incurred after 1.1.2006, nor that any costs incurred in the last year (only) can be included (despite the question providing analysis of prior year cost, correctly included by most in the computation), and only a few mentioned any of the reasons for withdrawal of relief. The basic requirement for the expenditure to result in improved output was rarely mentioned, and ignorance of rules for depreciation and unclaimed expense was common. Some candidates entered into explanation of IFRS rules concerning development expenditure, which are not relevant here. Most candidates understood the 5 year "newness" point (perhaps because it is so unusual!), the 50% limit and the 3 year carry forward, to achieve average marks of 3 out of 9, with few achieving as many as 6.

Regarding donations in (c) the majority of students did not know that relief had been extended to cover public benefit bodies elsewhere in the European Union. Candidates failed to state the details of the recipient which have to be entered in tax return. Surprisingly many confused the limit with the 6% limit for personal taxpayers, and stated that the "documented bank transfer" regulation applied to CIT payers. Interestingly a very large number did not see through the donation to local fire safety officer as a fairly transparent bribe (never mind it being disallowed as made to an individual!). Overall, easy marks were lost by many candidates. The few who pointed out the anomaly between the Tax Acts and the Act Regulating Polish State/ Roman Catholic Church relations earned a small bonus: this was not required knowledge. Again, stating that maximum relief was PLN 24,000 without answering the requirement to list which donations qualified earned no marks, except the half mark for knowledge of the limit.

A considerable number of students failed to read/understand the requirement in (d) which asked for separate computation of taxable revenues and tax allowed costs. Whereas previous examinations have asked candidates to demonstrate knowledge of exemptions/disallowables etc by adjusting a draft accounting profit to arrive at taxable income, the identical result is achieved by computing the ALLOWED/TAXABLE items. This is indeed what most company accountants do in practice. Students who went about it the correct way scored well, with full marks achieved often. Those who started with a fictional "accounting profit" and then "adjusted" up or down had clearly not followed the instruction and should have been awarded nil marks out of 8, but the markers went to great lengths to discover if the answer demonstrated understanding of the basic allowable/disallowable items in order to award marks. This was not easy, since it was often unclear whether the "pluses/minuses" displayed by candidates were meant to be for items allowed, disallowed, grossed up, or to be ignored.

Of the intelligible answers a common mistake was ignoring the depreciated value of the disposed fixed asset and the cost of the disposed investment. Candidates who netted these values off against revenue were awarded full marks, although technically of course the gross revenue is taxable revenue and the "book value" is an allowable cost.

The last part of the question involved consideration of which of the available reliefs to claim in the case of this company, which had more reliefs than income. The taxable income was not required to be computed, and clearly given both in note (6) and in Requirement (e): by this means the examiner had attempted to avoid the situation where a student might lose marks by miscomputing income and then designing an inappropriate strategy for reliefs. It was disappointing to see many candidates began with a completely incorrect income figure, usually arising from the misunderstanding of requirement (d) above, and scored poorly.

Five marks were available, so well prepared candidates should have realised that there was a little bit of thinking time offered and a bit of explaining required. Most got the point that donations needed claiming this year since there is no carry forward, and that this is the last year to utilise the remainder of the 2003 loss, to score 2 easy marks. Very few went on to appreciate that, although 3 years remain to recover the (very high) 2006 loss the company has achieved relatively low income in two of the last three years, and of course a loss in the third. Hence there is no certainty of high future profit. Thus it is important to offset as much of the 2006 loss as possible before the 5 year period runs out. The new technology relief can be omitted this year, since if there is a lot of income next year it will be recovered, and 12 month depreciation will also do the trick. Nobody made all of these points lucidly.

Candidates are advised to apply a little analytical thinking, explanation and simple planning of the syllabus. A true professional is not simply a filler in of returns, but is able to use understanding of a situation to achieve strategic successes (not only of course in tax!).

Generally this challenging question was not answered satisfactorily, with many candidates struggling to achieve even half marks.

Question 2
This question was based on a couple, one employed, one self employed and their social security and PIT computations. The facts and requirements were straightforward, and most students scored over 50%, with some excellent answers. Poor tabulation and unnecessary individual tax computation often occurred.

Part (a) asked for the year's ZUS and Health Service Contribution costs for each party. Most appreciated the difference in bases between employment and self-employment and the structure of the computation and earned the full 6 marks and even with a few errors of understanding over half marks were achieved by almost all.

Common errors were:
- Charging the entire relocation compensation to ZUS, instead of reducing by the 2 month salary exemption: ZUS is rarely charged on a higher basis than PIT; or exempting it (some taxable items are exempt from ZUS, but this is not one of them).
- Unnecessarily computing Piotr's employer's ZUS contribution, or the 1.25% HSC "cost", when only the 7.75% limit for reduction from PIT is eventually required.
- Charging Olga 30% of the average wage under the new business reduction available: congratulations for knowing of the reduction, but it is 30% of the Minimum Wage, which was not given and if required the examiner would have asked for this minimum charge to be presented.
- Unnecessarily computing monthly costs, or charging Olga 12 months, when she was in business for only 8.
- Losing the answer to (a) messy calculations for (b), making it difficult to find and mark. The question is split into separate requirements to make life easier for candidate and marker, so a clearly labelled answer to each section is expected.

The PIT computations were often messy, but generally done well, with the following common weaknesses:

For Piotr:
- Relocation exemption omitted.
- Antique car sale omitted as beyond 6 months, when 6 months from end of month of acquisition is relevant.
- Allowing him motor travel to work, when available is only the flat rate allowance, generally computed excellently with the 25% (not 50%) increase for 3 months of living in a different place to workplace.

For Olga:
- Some difficulty with room depreciation or omission. Many thousands of small self employed people working from home will want to claim every cost that is available.
- Confusion on hotel stay: it is an allowed cost, and since the VAT is disallowed it becomes an additional PIT cost, spotted by very few: 7% was acceptable although lower rate or exempt items will always be given in the question.
- Varieties of incorrect interpretations of meal and overnight allowances. The flat rate cost for meals is allowed in place of the disallowed restaurant bills, and Olga gets this allowance for both her hotel stay and the nights when she stayed privately: for those nights of course she also gets 1.5 times this allowance in lieu of hotel cost. Extremely few candidates got these elements correct.
- Limiting the internet cost to the PIT relief limit, where here the full cost is a bona fide business expense.
- A few questioned the allowability of the professional subscription: since she is in practice as an architect the fee would be a legitimate business expense, as would be other costs related to her profession, such as periodicals, courses, textbooks.
- It was stated that she did not want to claim accelerated depreciation, but candidates claiming the full writing off of new business assets were generously awarded the mark: some depreciation computations missed the fact that she was not in business for the full year.

Computation and joint taxation conditions:

- Individual PIT computations were not requested, but done by many, who often then failed to do the required joint tax computation.
- The question asked for the final liability, so required the HSC allowable to be deducted, which many failed to do, although those who had done so in the (unnecessary) individual computations were awarded a mark if they had taken the correct amount from each taxpayer.
- The conditions for joint taxation were well known, and a half mark was awarded to any who stated that flat rate taxation by one party prevented the joint tax calculation, although nothing in part (b) had suggested any such thing.
- Almost all correctly stated why joint taxation was favourable in this case.
- Computation of the saving was not required, and those who went to the trouble of calculating it wasted time and invariably got it wrong.

Generally this question performed well, with most students earning more marks out of 25 than they had scored out of 30 in the CIT question.

Question 3

The first part of this VAT question was concerned with excess input tax and refund claims. The basic VAT account for each month seemed a straightforward requirement and surprisingly many performed poorly. A few combined the two months! The arrival at excess VAT for a period is of course the first stage in a refund claim. Early refund was available for fixed asset VAT, but many did not notice or understand that refund is only of the excess input, which was less than total VAT on fixed assets, and claimed the entire fixed assets VAT.

Most knew of the "lower rate" input reason for refund in the second month, but about half restricted it to the 22% equivalent of 7% sales, forgetting that it applies to all lower rate activity, including zero rated exports. One candidate restricted that element to 15%, which logically should be the limit, but which is of course not the case. Time limits for the early refund were generally well remembered.

Two expected sensible answers for a company declining to claim early refund were usually provided. The joy of greeting a VAT inspection seems to reflect happy experience! Not requiring the cash as a justification is not worth a mark.

The special mechanism for on account refund of VAT for major capital expenditure incurred before the commencement of taxable activity has been around from the very beginning of VAT in Poland, and is useful since no other means of recovery are available. It has featured in examinations occasionally. Candidates either knew it well or not at all.

Many candidates exhibited very poor knowledge of these VAT matters, but most did well, with some excellent answers.

Question 4

Taxpayer, remitter and circumstances of tax liability arising were not always well defined, but were usually well explained. Copious examples of each were not requested in part (a), and at most earned half a mark in lieu of proper explanation of responsibilities. Only one candidate explained Tax Office Decision as a source of tax obligation.

Examples of remitter required in part (b) were usually correct, except that a company is a taxpayer, not a CIT remitter.

Part (c), requested computation of tax liabilities at relevant dates and to explain procedures resulting from a failure to pay tax on due date. This caused universal grief, with some fairly poor answers, despite considerable computational effort in some cases.

Whilst nearly all knew the due dates for monthly CIT payments, many failed to realise that the tax is computed on a cumulative basis during the year, and so charged tax on the full April "profit", when it would in effect be reduced by the March loss, which lowers the cumulative tax base. Another error frequently made was to "carry back" the March loss to reduce the cumulative base at February. In both income tax laws no "overpayments" are recognised till the year end declaration is made.

The penalty tax rate was almost universally taken as the National Bank of Poland Lombard rate, when twice that rate is applied.

Some computed interest by arriving at a rounded daily interest rate of 0.1% (= 3.66% annually), which showed a lack of numerical analysis. The relevant annual rate (in this case 10%) should be applied to days of arrears (the examiner even gave the number of days in the year as a clue).

The days of arrears were generally counted fairly accurately, but many took calendar months, or counted from month end dates or from 1st January, or occasionally incomprehensibly.

The allocation of the payment against tax and interest was done incorrectly. Candidates primarily allocated either fully against interest, or against the January interest arrears, or not at all. No candidates allocated proportionately against the tax/interest due at the time. The Tax Ordinance brought in this absolutely "fair" allocation method when introduced many years ago. It does give rise to complex calculation (especially when an underpayment has a "knock-on" effect on many future months of liabilities) but has the fairness and wisdom of Solomon.

Many missed the occurrence of continuing interest charges from the first payment, which did not extinguish the arrears, until the final settlement.

The final payment computation (if done) was difficult to understand.

This question was answered poorly, with most candidates who attempted the question achieved below half marks. Candidates most frequently omitted this question.

Question 5

Rules on determining fiscal residence in Poland were generally well known, and many candidates knew the double tax treaty tests for determining in which of two countries a taxpayer is resident, including even the order of test. The only point is not to repeat the residence definitions in the double tax treaty rules, which are applied when the basic criteria do not determine residence status.

Reasons for Edward being deemed resident in Poland stemmed from the basic centre of interests definition, and no marks were earned for such statements as:

- Staying (or "probably" staying) in Poland over 183 days (he probably did not);
- Not earning income while in South America;
- Being in Sweden only 100 days.

The computation was simple, but many errors were made. Apart from layout and calculation errors:

- Whichever relief method is applied it is crucial to arrive at the separate income from each source. Few candidates did, and those who did at least get to the Peruvian income after cost allowance rarely named it correctly.

- The daily "cost of living" allowance is a generous relief in Polish tax law against earnings from foreign employment, but those who remembered usually forgot that it is presently restricted to 30% of the daily foreign meals allowance for the particular country;
- Almost all failed to realise that the monthly "getting to place of work" flat rate cost, which is a holy entitlement for Polish employment contracts, applies also if working abroad. A few claimed it for the whole year when the question stated that Edward worked in Sweden during 4 months only.
- Tax on total ("World") income was occasionally computed at 19%, with no "free amount" of PLN 587 deduction.
- On credit for foreign tax, most failed to test whether the foreign tax deducted was less than equivalent proportion of Polish tax on INCOME.
- Having failed to compute the taxable income from Sweden, those who did the test compared the Swedish tax deducted to Polish tax on gross revenue.
- Almost all candidates doing the maximum credit test compared to 19% of the relevant income (or incorrectly revenue, as mentioned). The test is for proportional tax. The law states that this is done by taking total Polish tax times the proportion of the foreign income to total income, but equally acceptable is computing the effective rate and applying that to each foreign income.
- No information was given in the question about double tax treaty relief, so credit relief, as stated in the tax law, should have been applied. In the event, Poland surprisingly does not have a treaty with Peru (so credit relief applies) and the Swedish treaty envisages credit relief. Nonetheless, candidates who attempted exclusion relief adequately were awarded equivalent marks in this instance.

The computational part of the question was generally done poorly and often untidily, pulling the average mark for the question down to about 50%.