Answers

Marks

1 Paul and Maria

(a) Chargeable income for the year of assessment 2014

	€	€	€	
Maria's earned income				
Salary			35,000	0·5
Fringe benefits:				
Vehicle allowance:				
Vehicle use value (17% of €20,000)	3,400			0·5
Fuel value (3% of €20,000)	600			0·5
Maintenance value (3% of €20,000)	600			0·5
	4,600			
At private use percentage (40%)		1,840		0·5
Paid vacation		2,000		0·5
Free meals at staff canteen (not taxable)		0		0·5
Provision of childcare facilities (not taxable)		0		0·5
Professional membership (not taxable)		0		0·5
Professional subscriptions and publications (not taxable)		0		0·5
Beneficial loan arrangement:				
Loan of €50,000 at 4·5% benchmark rate for financial institutions	2,250			0·5
Less: At 1·5% rate actually charged	(750)			0·5
	1,500			
Less: In-house benefit reduction	(700)			0·5
		800		
Total value of taxable fringe benefits			4,640	
Total earned income (Maria)			39,640	

	€	€	€	
Paul's earned income				
Basic salary (€24,000 x 9/12)			18,000	0·5
Fringe benefits:				
Free services (vouchers)	1,200			0·5
Less: In-house benefit reduction	(700)			0·5
		500		
Uniforms (not taxable)		0		0·5
Car cash allowance:				
€150 x 9 months	1,350			0·5
Less: 50% not taxable	(675)			0·5
		675		
Private health insurance cover		500		1·0
Total value of taxable fringe benefits			1,675	
Total earned income (Paul)			19,675	
Less: Trading tax loss brought forward from previous year of assessment			(5,000)	1·0
			14,675	

	€	€	*Marks*
Other income			
Rental income		8,000	0·5
Allowable deductions:			
Ground rent	(500)		0·5
Further deduction (20% x (€8,000 – €500)	(1,500)		1·0
		(2,000)	
		6,000	
Gross foreign dividend		2,000	0·5
Gross foreign interest		3,465	1·0
Total other income		11,465	

Deductions against Maria's income

	€	€	
Medical fees (not deductible)		0	0·5
Home for the elderly fees (capped at €2,500 x 2)		5,000	1·0
School fees			
– Kindergarten (capped at €1,300)	1,300		1·0
– Primary school (capped at €1,600)	1,600		1·0
		2,900	
Total allowable deductions against Maria's earned income		7,900	

	€	
Maria's earned income	39,640	0·5
Less: Allowable deductions	(7,900)	
	31,740	
Paul's earned income (net of tax loss absorbed)	14,675	
Other income	11,465	
Total chargeable income	57,880	
		19

(b) Tax payable for the year of assessment 2014

Separate computation using single rates

		€	€	
Maria				
€0 to €8,500	at 0%	0		
€8,501 to €14,500	at 15%	900		
€14,501 to €19,500	at 25%	1,250		
€19,501 to €43,205	at 32%	7,586		
Tax chargeable			9,736	0·5
Less: Credit for foreign tax paid on foreign source dividend (15% of €2,000)		(300)		1·0
Credit for foreign tax paid on foreign source interest (10% of €3,465)		(347)		1·0
			(647)	
Tax payable			9,089	
Paul				
€0 to €8,500	at 0%	0		
€8,501 to €14,500	at 15%	900		
€14,501 to €14,675	at 25%	44		
Tax chargeable and payable			944	0·5
Total tax payable			10,033	

Tutorial note: *Maria's earned income exceeds that of Paul. Therefore, the unearned income is allocated to her for the purposes of the separate computation.*

				Marks
Separate computation using parent rates				
		€	€	
Maria				
€0 to €9,300	at 0%	0		
€9,301 to €15,800	at 15%	975		
€15,801 to €21,200	at 25%	1,350		
€21,201 to €43,205	at 32%	7,042		
Tax chargeable			9,367	0·5
Less: Credit for foreign tax paid on foreign source income (as above)			(647)	0·5
Tax payable			8,720	
Paul				
€0 to €9,300	at 0%	0		
€9,301 to €14,675	at 15%	806		
Tax chargeable and payable			806	0·5
Total tax payable			9,526	

Joint computation

		€	€	
€0 to €11,900	at 0%	0		
€11,901 to €21,200	at 15%	1,395		
€21,201 to €28,700	at 25%	1,875		
€28,701 to €57,880	at 32%	9,338		
Tax chargeable			12,608	0·5
Less: Credit for foreign tax paid on foreign source income (as above)			(647)	0·5
Tax payable			11,961	

The most beneficial method of tax computation is the separate computation using parent rates, in terms of which the total tax payable is €9,526. 0·5

6

25

Marks

2 Karisma Operations Limited

(a) **Income tax for the year of assessment 2014 (basis year ended 30 September 2013)**

Business income

	€	€	€	
Net profit before tax as per financial statements			480,000	
Add back:				
Finance expenses (deductible against foreign interest income)		50,000		0·5
Staff costs including bonuses (fully deductible)		0		0·5
Advertising including pre-trading (fully deductible)		0		0·5
Depreciation		255,000		0·5
Payments of a voluntary nature				
– Donation to Heritage Malta (deductible)		0		0·5
– Donation to local music band (not deductible)		500		0·5
Loss on disposal of delivery lorry (deductible)		–		1·0
Disallowed portion of non-commercial motor vehicle lease expense ([60,000 – 14,000]/60,000 x €24,000)		18,400		1·0
Legal fees re proposed changes to share capital (not deductible)		10,000		0·5
Balance of legal fees per financial statements (assumed deductible)		–		
Formation expenses		5,000		0·5
Consultancy expense relating to the business plan (pre-trading expenses)		20,000		1·0
Penalty for late filing of VAT returns		2,000		0·5
Bad debts written off		0		0·5
Provisions for doubtful debts: Specific		5,500		0·5
Provisions for doubtful debts: General		9,500		0·5
Improvements to premises (Note: Capital allowances to claim, below)		40,000		0·5
Routine maintenance		0		0·5
			415,900	
Deduct:				
Financial income		(90,000)		0·5
Dividend income		(70,000)		0·5
Unrealised foreign exchange differences		(4,000)		0·5
Initial allowance: Industrial buildings (10% of (€220,000 + €40,000))		(26,000)		1·0
Wear and tear allowances:				
Industrial buildings (2% of €260,000)	(5,200)			0·5
Commercial motor vehicles over 5 years (20% of (€105,000 – €26,000) cost of disposed lorry)	(15,800)			0·5
Plant over 10 years (10% of €180,000)	(18,000)			0·5
Computer equipment over 4 years (25% of €50,000)	(12,500)			0·5
		(51,500)		
			(241,500)	
Chargeable business income for the year (MTA)			654,400	

Tutorial notes:

1. *No balancing statement is required in respect of the delivery lorry disposed of, since no wear and tear allowances were claimed given that the acquisition and disposal took place in the same year of assessment.*

2. *Legal fees relating to the proposed change in the capital structure of the company are considered to be of a capital nature and are not considered to be costs incurred in the production of the income. Hence they are not deductible for tax purposes.*

3. *The expense relating to the extension of the company's premises is considered to be of a capital nature and is not considered to be a cost incurred in the production of the income. Hence it is not deductible for tax purposes, although capital allowances may be claimed.*

	€	Marks
Foreign interest income		
Foreign interest income received (net)	65,000	
Gross up by 10% foreign tax withheld	7,222	0·5
Gross interest income	72,222	
Less: Interest expense on capital employed in acquiring the income	(50,000)	0·5
Chargeable interest income (FIA)	22,222	

	€	
Local interest income		
Net local bank interest received (FTA)	25,000	
Gross up by 15% final withholding tax (investment income provisions)	4,412	0·5
Gross interest income	29,412	

	€	
Local dividend income		
Gross chargeable local dividend income	50,000	
Tax at source at 35%	(17,500)	0·5
Net local dividend income (IPA)	32,500	

	€	
Foreign dividend income		
Net foreign dividend received (FTA)	20,000	
Exempt dividend (participation exemption applies)	(20,000)	
Chargeable foreign dividend income	0	0·5
		17

(b) Tax charge for the year 2014

	€	
Chargeable income subject to the standard corporate income tax rate		
Business income	654,400	
Foreign interest income	22,222	
Local dividend income	50,000	
	726,622	1·0
Tax at 35%	254,318	0·5
Local interest income subject to 15% final withholding tax (FWT) (in terms of the investment income provisions)	29,412	
Tax at 15%	4,412	0·5
Total tax charged	258,730	

Tax payable for the year 2014

	€	€	
FWT paid (investment income provisions)		4,412	
Tax charged on income subject to standard corporate income tax rate	254,318		
Less: Tax at source on local dividend income	(17,500)		0·5
Credit for foreign tax suffered on foreign interest income	(7,222)		0·5
		229,596	
Total tax payable		234,008	
			3

			Marks
(c) Allocation to tax accounts			
	€	€	
Final tax account (FTA)		45,000	
– Interest subject to 15% FWT	25,000		0·5
– Exempt foreign dividends	20,000		0·5
Immovable property account (IPA)		87,500	
– IPA dividend	32,500		0·5
– Annual market rent re-allocation (€250/sqm x 220sqm)	55,000		1·0
Maltese taxed account (MTA)		370,360	
– Business income	425,360		0·5
– Annual market rent re-allocation (€250/sqm x 220sqm)	(55,000)		0·5
Foreign income account (FIA)		14,444	0·5
Untaxed account		(284,400)	0·5
Distributable profits ([€480,000 + €7,222 (foreign tax deducted)] – €254,318 [€4,412 FWT already deducted from net profit before tax as per financial statements])		232,904	1·5
			6

(d) Dividend distribution and tax refund

Dividend distribution (net)

	€	
Final tax account (FTA)	45,000	0·5
Immovable property account (IPA)	87,500	0·5
Maltese taxed account (MTA) (balance)	67,500	0·5
	200,000	

Tutorial note: *FTA and IPA profits are required to be distributed before MTA profits can be distributed. As the directors of KOL wish to avoid distributing any profits from the foreign income account (FIA) and the untaxed account, all the FTA and IPA profits will be distributed first, and the balance of the net dividend will then be distributed out of the MTA profits.*

Tax refund claimable by Karisma Holdings Limited (KHL)

No tax refunds may be claimed in respect of profits distributed out of the FTA.	0·5
No tax refunds may be claimed in respect of profits distributed out of the IPA.	0·5
KHL can claim a tax refund amounting to 6/7ths of the tax charge on the profits distributed out of the MTA.	0·5
The tax refund claimable is therefore: 6/7ths of (€67,500 x 35/65) = €31,154.	1·0
	4
	30

3 (a) Items of information required in a dividend certificate (warrant)

- The gross dividend.
- The taxed account(s) out of which the dividend is being distributed.
- The total tax chargeable on the company in respect of the distributed profits.
- The foreign tax in respect of which relief from double taxation has been given.
- The Malta tax payable after all reliefs for double taxation.
- The amount of the profits distributed from each taxed account after deducting tax.
- Any withholding tax payable on the distribution (including top-up tax).
- The net dividend.
- The net Malta rate.
- A note quoting the law conferring any exemption from tax also in the hands of the shareholder.
- A statement declaring that the company is entitled to make a tax refund claim in respect of taxed profits distributed to it by a second company, if applicable.
- An analysis by year of assessment of the profits out of which the dividend is paid.
- Any other information the Commissioner shall require.

Six items only required, ½ mark each, maximum 3

Marks

(b) Charles Borg

Chargeable capital gains and tax payable

1. No chargeable capital gain and hence no tax charge.
   Reason: Bonds do not constitute securities chargeable to income tax on capital gains. 1·0

2. No chargeable capital gain and hence no tax charge.
   Reason: Preference shares with a fixed rate of return do not constitute securities chargeable to income tax on capital gains. 1·0

3. The disposal constitutes a transfer of a controlling interest.

   Calculation of market value:

	€	€	Marks
Net asset value		450,000	
Add: Goodwill adjustment (2/5 of past 5 years' profits = €25,000 x 2)		50,000	1·0
Market value of immovable property	220,000		
Book value of immovable property	(180,000)		
		40,000	1·0
Market value		540,000	
Market value of portion pertaining to Charles's shareholding (50%)		270,000	0·5
Since the consideration is lower than the market value, the market value will be taken for the purposes of the capital gains computation.			0·5
Cost of acquisition (50% of €100,000 ordinary share capital)		(50,000)	0·5
Chargeable capital gain		220,000	
Income tax charge on capital gain at 35%		77,000	0·5

4. No chargeable capital gain and hence no tax charge.
   Reason: Gains on transfers of shares in companies listed on the Malta stock exchange are specifically exempt from tax. 1·0

5. No chargeable capital gain and hence no tax charge.
   Reason: Paintings fall outside the scope of the charge to income tax on capital gains. 1·0

6. Amount chargeable to property transfers tax = €125,000 – €3,000 = €122,000 0·5
   Property transfers tax charge = 12% x €122,000 = €14,640 0·5

   It is possible to opt out of property transfers tax since less than seven years have elapsed since the date of acquisition of the property.

		€	Marks
Consideration		125,000	
Cost of acquisition adjusted for inflation			
Inflation index for 2008	743·05		
Inflation index for 2012	810·16		
€90,000 x 810·16/743·05		(98,129)	1·0
Improvements adjusted for inflation			
Inflation index for 2009	758·58		
Inflation index for 2012	810·16		
€10,000 x 810·16/758·58		(10,680)	1·0
Maintenance allowance			
(0·4% x 4 years x €90,000)		(1,440)	1·0
Brokerage fees (less than 5% of consideration)		(3,000)	0·5
Chargeable capital gain		11,751	
Income tax charge at 35%		4,113	0·5

   The capital gains option is more beneficial as it results in less tax being paid than the property transfer tax option. Therefore, the taxpayer will elect to pay income tax on the capital gain. 0·5

			Marks
7.		€	
Consideration		590,000	
Cost of acquisition		(520,000)	
Inflation allowance:			
Inflation index for 2007	712.68		
Inflation index for 2012	810.16		
€520,000 x 810·16 – 712·68/712·68: €71,125			1·0
Limitation on inflation allowance:			
(€590,000 – €520,000 – €10,400 – €17,000)		(42,600)	1·0
Maintenance allowance			
(0·4% x 5 years x €520,000)		(10,400)	1·0
Other expenses of transfer (less than 5% of consideration)		(17,000)	0·5
Chargeable capital gain		Nil	
Income tax charge		Nil	
			17
			20

Tutorial note: *Property transfers tax does not apply since the property is situated outside Malta.*

4 (a) David Vella

	Marks
The transaction constitutes an importation of goods into Malta by David Vella.	1·0
The importation is deemed to take place in Malta.	0·5
The person liable to account for and pay the VAT is David Vella (being the importer).	1·0
The applicable rate of Maltese VAT is the standard rate of 18%.	0·5
	3

(b) Melita Health Limited (MHL)

	Marks
The transaction constitutes an intra-EU acquisition of goods in Malta by MHL.	1·0
The acquisition is deemed to take place in Malta.	1·0
The person liable to account for and pay the VAT is MHL (being the acquirer).	1·0
No VAT is payable as pharmaceutical goods constitute an exempt with credit supply for Maltese VAT purposes.	1·0
	4

(c) Valletta Advisory

(i) **Services to Verona SpA**

	Marks
The transaction constitutes a supply of services by Valletta Advisory.	0·5
The supply is deemed to take place in Italy (where the VAT registered business customer is established).	1·0
The person liable to account for and pay the VAT is the business customer (Italian VAT would be accounted for by the business customer in Italy).	0·5
No Maltese VAT is payable as the transaction falls outside the scope of Maltese VAT.	0·5

(ii) **Services to a Maltese public authority**

	Marks
The transaction constitutes a supply of services by Valletta Advisory (as above).	
The supply is deemed to take place in Malta (where the supplier is established).	0·5
The person liable to account for and pay the VAT is Valletta Advisory (being the supplier).	0·5
The applicable rate of Maltese VAT is the standard rate of 18%.	0·5

(iii) **Services to Turisti Limited**

	Marks
The transaction constitutes a supply of services by Valletta Advisory (as above).	
The supply is deemed to take place in Malta (where the VAT registered business customer is established).	0·5
The person liable to account for and pay the VAT is Valletta Advisory (being the supplier).	0·5
The applicable rate of Maltese VAT is the standard rate of 18% (as above).	
	5

	Marks
(d) Grand Harbour Hotel Limited (GHHL)	
The transaction constitutes a supply of services by GHHL to the individual tourist.	0·5
The supply is deemed to take place in Malta (where the hotel is physically situated).	1·0
The person liable to account for and pay the VAT is GHHL (the supplier).	0·5
The applicable rate of Maltese VAT is 7%.	1·0
	3
	15

5 Alpha Limited group

(a) Membership of the loss relief group for the year of assessment 2014

Both Beta Limited and Gamma Limited are eligible to surrender/claim group losses since they have been respectively liquidated and incorporated part-way during the financial year and thus fall within the exceptions to the general rule that the claimant and surrendering companies must have identical financial period start and end dates. 2·0

Delta Limited was acquired part-way during the year and hence did not form part of the group throughout the whole year. Therefore, it cannot surrender/claim group losses in respect of the year of assessment 2014. 1·0

3

Tutorial note: *Other things being equal, Delta Limited should form part of the group and be able to surrender/claim group losses with effect from the year of assessment 2015.*

(b) (i) Tax losses which may be surrendered and potential offsetting profits for group relief

	Alpha Limited 1 January to 31 December 2013	Beta Limited 1 January to 30 September 2013	Gamma Limited 1 April to 31 December 2013	
	€	€	€	
Profit/(loss) before tax as per financial statements	20,000	45,000	(25,000)	
Add back:				
Depreciation of property, plant and equipment	40,000	20,000	3,000	0·5
Accounting loss on sale of securities	15,000	–	–	0·5
Deduct:				
Accounting gain on sale of securities	–	–	(10,000)	0·5
Income/(loss) before wear and tear allowances	75,000	65,000	(32,000)	
Wear and tear allowances carried forward from previous year of assessment absorbed	(4,000)	(3,000)	0	0·5
Wear and tear allowances for the year absorbed	(24,000)	(30,000)	0	1·0
Income/(loss) after wear and tear allowances	47,000	32,000	(32,000)	
Chargeable capital gain	0	–	5,000	0·5
	47,000	32,000	(27,000)	
Trading tax losses carried forward from previous year of assessment absorbed	(1,000)	–	–	1·0
	46,000	32,000	(27,000)	

Therefore, the losses which can be surrendered intra-group are the €27,000 trading tax losses for the current year pertaining to Gamma Limited, which can be claimed in whole or part against the profits of Alpha Limited and/or Beta Limited. 0·5

5

Tutorial note: *Unabsorbed trading tax losses for prior years, as well as any unabsorbed capital losses and any unabsorbed wear and tear allowances (whether for the current year or prior years), cannot be surrendered intra-group.*

(ii) Unabsorbed amounts carried forward

	Alpha Limited €	Beta Limited €	Gamma Limited €	
Unabsorbed capital losses carried forward to the year of assessment 2015	23,000	2,000	Nil	1·0
Unabsorbed wear and tear allowances carried forward to next year of assessment	Nil	Nil	1,500	1·0
				2
				10