
Answers

	Marks
1 Paul and Judy	
(a) Paul and Judy are resident and ordinarily resident but not domiciled in Malta.	1
As such, they are taxable on their local source income and chargeable gains arising in Malta and any foreign source income received in Malta.	2
They are not liable to Malta tax on foreign source capital gains, regardless of whether they are or are not received in Malta.	1
	<u>4</u>

(b) Chargeable income for the year of assessment 2012

	Paul €	Judy €	
*Profits (trading profits) from the sale of foreign securities (received in Malta)	100,000		1
*Profits (trading profits) from the sale of listed shares (taxable because the capital gains exemption does not apply to trading profits)	30,000		1
*Trading profits from dealing in mining rights (received in Malta)	450,000		1
Local bank interest received net of final withholding tax	0		1
*Foreign source pension (received in Malta)	30,000		1
*Foreign source employment income (not received in Malta)	0		1
*Professional subscription (foreign)	–		1
*Professional subscription (local)	–		1
*Tennis club subscription (local)	250		1
*Fringe benefit (fees for hairstylist, masseuse, housekeeper and cook, all availed of in Malta)	5,000		1
*Consultancy fees (local source)	3,000		0.5
*Seminar fees (local source)	2,000		0.5
*Salary (local source)		5,000	0.5
*Tuition fees (local source)		1,200	0.5
*Royalty income (received in Malta)		800	1
Total chargeable income	<u>620,250</u>	<u>7,000</u>	<u>13</u>

* indicates earned income

Tutorial note: Judy is a writer so her royalty income is considered to be trading income (earned income).

(c) Tax payable for the year of assessment 2012

Joint computation

Spouses' total income is (620,250 + 7,000) = €627,250

	€	
0 – 11,900 at 0%	0	
11,901 – 21,200 at 15%	1,395	
21,201 – 28,700 at 25%	1,875	
28,701 – 627,250 at 35%	209,492	
	<u>212,762</u>	1

Separate computation

Paul is the higher earner of earned income

	€	
Paul		
0 – 8,500 at 0%	0	
8,501 – 14,500 at 15%	900	
14,501 – 19,500 at 25%	1,250	
19,501 – 620,250 at 35%	210,262	
	<u>212,412</u>	1

Judy		
0 – 7,000 at 0%	0	0.5

Total tax due under separate computation €212,412.

Using separate computation would have been more tax efficient, as this results in a tax saving of €350.	0.5
	<u>3</u>

(d) Paul's proposed donation of shares

Sinistri Limited is a Dutch company, so any capital gain which is derived (or deemed to be derived) from a transfer of its shares is considered to be foreign source. 1.5

Therefore, there will be no Malta tax consequence from a donation of the shares, because (as stated in (a)) Paul is not domiciled in Malta and so is not subject to tax on his foreign source capital gains. 0.5
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(e) Judy's proposed transactions

The transfer of the rights over Judy's children's book is a capital transaction and the gain on the transfer is a foreign source gain, therefore as Judy is not domiciled in Malta (as stated in (a)), the gain will not be taxable in Malta. 1.5

However, the profits derived from the translation of Judy's novel are of an income nature (exploitation of rights) and as such these profits will be taxable in Malta to the extent that they are received in Malta. 1.5
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2 Malta Company Limited (MCL)

(a) Profits chargeable to income tax from Malta trading activities

	€	€	
Wholesale division			
Accounting profit	520,000		
Adjustments:			
Interest received:			
– from supplier	0		1
– from customers	0		0.5
Damaged stock	0		1
Fine for customs offence	2,000		0.5
Wages paid outside FSS	6,000		1
Impaired debts:			
– specific provision	8,500		1
– recovery of debt previously written off	0		0.5
Exchange losses:			
– realised transaction losses	0		0.5
– unrealised translation losses	6,000		1
		542,500	
Retail division			
Accounting profit	(40,000)		
Adjustments:			
Bank interest received (subject to final withholding tax)	(1,800)		0.5
Legal fees	0		1
Interest on late payment of VAT	0		1
Depreciation:			
– on building	20,000		1
– on fixtures and fittings	0		0.5
– on delivery vehicle	0		0.5
– on car (7,000 – (20% x 14,000))	4,200		1
		(17,600)	
Profit chargeable to tax (net of intra-company losses)		524,900	0.5
			13

(b) (i) Tax payable for the year of assessment 2012 and allocation to tax accounts

	Maltese taxed account (MTA) €	Final tax account (FTA) €	Immovable property account (IPA) €	Foreign income account (FIA) €	
Malta trading activities (from (a))	524,900				0.5
Malta bank interest (net of withholding tax)		1,800			1*
Branch in Country L (net of local tax – 90% x 55,000)				49,500	1*
Malta rental income			74,000		1*
Less: 20% maintenance allowance			(14,800)		1
Dividend from ABC Limited		10,000			1*
Flat rate foreign tax credit (FRFTC) at 25%				12,375	1
	<u>524,900</u>	<u>11,800</u>	<u>59,200</u>	<u>61,875</u>	
Tax at 35%	183,715	0	20,720	21,656	1.5
FRFTC				(12,375)	0.5
Tax payable	<u>183,715</u>	<u>0</u>	<u>20,720</u>	<u>9,281</u>	
Profit after tax	341,185	11,800	38,480	40,219	0.5
Annual market rent (AMR) adjustment – 1,000 x €250	(250,000)		250,000		2**
	<u>91,185</u>	<u>11,800</u>	<u>288,480</u>	<u>40,219</u>	
					<u>11</u>

Notes to marking scheme for part (b)(i):

* Marks for FTA, IPA and FIA income items based on a ½ mark for the correct figure and a ½ mark for the correct tax account.

** AMR marks based on 1 mark for the correct figure and 2 x ½ mark the tax accounts adjusted.

- (ii) 1. ABC Limited is a company resident outside Malta in which MCL holds more than 10% of the equity shares. MCL can, therefore, apply the participation exemption to the dividend received and allocate it to the final tax account. 1.5

Tutorial note: As ABC Limited is resident in another EU country, the rate of corporation tax (less than 15%) is not relevant.

2. No relief is available for the capital loss suffered by LMN Limited in the year of assessment 2012. Such losses can only be offset against capital gains of LMN Limited in the year of loss and subsequent years; they cannot be group relieved. 1.5

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- (c) If each floor of the building is 800 square metres in area, the annual market rent (AMR) adjustment required becomes €400,000 (1,600 x €250). 0.5

The transfer to the immovable property account (IPA) in the year of assessment 2012 will become €381,404 as follows:

	€	
Maltese taxed account (MTA)	341,185	0.5
Foreign income account (FIA)	40,219	1
	<u>381,404</u>	

The balance of €18,596 will be carried forward and added to the AMR adjustment of the following year of assessment (2013).

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3 (a) Maltija Limited

(i) The conditions necessary for roll-over relief to apply are:

1. The asset being transferred (disposed of) must have been used in the business for a period of at least three years.
2. The asset disposed of must be replaced within one year.
3. The replacement asset must be used in the business solely for a similar purpose to the original asset.

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(ii) If roll-over relief is claimed, then Maltija Limited can both opt out of paying property transfer tax at 12% of the transfer value on the sale of the factory, and defer paying any tax on the capital gain until such time as the replacement factory is sold.

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Capital gain on the sale of the Marsa factory

		€	€	
Sale proceeds	Nov 2011		300,000	
Less:				
Cost of acquisition	1985	40,000		0.5
Cost of improvement (rebuilding)	1991	80,000		0.5
Cost of addition (extension)	2000	<u>50,000</u>		0.5
			(170,000)	
Maintenance allowance:				
On acquisition cost		0		0.5
On improvement (20 years x 0.4% x 80,000)		6,400		0.5
On addition (11 years x 0.4% x 50,000)		<u>2,200</u>		0.5
			(8,600)	
Inflation allowance				
On acquisition cost $(770.07 - 426.18/426.18 \times 40,000)$		32,276		1
On improvement $(770.07 - 456.61/456.61 \times 80,000)$		54,919		1
On addition $(770.07 - 593.0/593.0 \times 50,000)$		<u>14,930</u>		1
			(102,125)	
Capital gain			<u>19,275</u>	

Cost of acquisition of Mriehel factory for the purpose of capital gains tax

€500,000 – €19,275 = €480,725.

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(b) Julianija Limited

(1) Shares in Sussidiarja Limited

		€	
Sale proceeds	2011	25,000	
Cost of acquisition	2004	<u>(8,000)</u>	
Capital gain		<u>17,000</u>	1

(2) Shares in Barranija Limited

The shareholding is of 10% or more of the equity capital of a foreign company, therefore the capital gain is exempt from tax under the participation exemption.

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				Marks
(3) Office block (fully furnished)				
		€	€	
Sales proceeds	2011		340,000	0·5
Less:				
Cost of acquisition	2008	300,000		0·5
Cost of furniture and fittings	2008	<u>50,000</u>		0·5
			(350,000)	
Maintenance allowance (350,000 x 0·4% x 3 years)			(4,200)	0·5
Inflation allowance (none available)			<u>0</u>	1
Capital loss			<u>(14,200)</u>	
Tutorial note: <i>The inflation allowance is capped to the selling price after deducting the cost and maintenance allowance.</i>				
(4) Emphyteusis (for 40 years)				
Assignments of an <i>emphyteusis</i> for 50 years or less are exempt from tax.				0·5
(5) Business permit				
			€	
Sales consideration			20,000	
Less:				
Cost (fees paid)			<u>(1,500)</u>	
Capital gain			<u>18,500</u>	1
Summary of gains and losses for the year 2011				
			€	
(1) Shares in Sussidiarja Limited			17,000	
(3) Office block			(14,200)	1
(5) Business permit			<u>18,500</u>	
			<u>21,300</u>	
Tax thereon at 35%			<u>7,455</u>	0·5
				<u>8</u>
				<u>20</u>

- 4 (a)** Value added tax (VAT) must be charged whenever a supply is made in the course of an economic activity; however, the VAT Act prescribes that activities by employees acting as such are outside the scope of VAT. 1·5
- For this purpose, the definition of an 'employee' in the VAT Act (article 5 (5)) includes 'the holder of an office', therefore services supplied by directors are outside the scope of VAT. 1·5
- 3

(b) Lettings Limited**(i) Value added tax (VAT) payable for the quarter ended 30 September 2011**

	€	
Supplies/output VAT		
Rents from residential apartments (exempt without credit supply)	0	1
Rents from apartments licensed under the Malta Travel & Tourism Services Act €48,000 x 7%	3,360	1
Rents from office premises €20,000 x 18%	3,600	0.5
Rents from parking spaces €4,000 x 18%	720	0.5
Purchase of furniture from Italy €7,000 x 18% (reverse charge mechanism applies)	1,260	1
	<u>8,940</u>	
Purchases/input VAT		
Electricity €1,200 x 5%	60	1
Insurance (exempt without credit supply)	0	1
Wages of cleaner (not a taxable supply)	0	1
Cleaning materials €300 x 18%	54	0.5
Furniture from Italy	1,260	1
	<u>1,374</u>	
VAT payable	<u>7,566</u>	0.5
		<u>9</u>

- (ii)** The VAT return for the quarter to 30 September 2011 should have been submitted and the VAT paid by 15 November 2011.

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- (c)** An excess VAT credit will be refunded by no later than five months from the expiry of the time allowed for the submission of the VAT return for the tax period or, if later, from the date on which the return was submitted.

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- 5 (a)** Tax avoidance refers to the legal means of reducing a person's tax burden by taking advantage of available reliefs within the tax legislation.

2

Tax evasion refers to seeking to pay less tax than is legally due by means of intentional misbehaviour or misrepresentation, such as the non-disclosure of information or income, providing deliberately false information or claiming a deduction when there is knowledge that such a deduction is not due.

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- (b)** The Income Tax Act contemplates three mechanisms for the elimination of double taxation:

(1) Treaty relief

Treaty relief applies where a double taxation arrangement/agreement is in force by Ministerial order between Malta and the relevant foreign territory. The relief is given in accordance with the terms of the treaty arrangement where the tax paid abroad is either income tax or any tax of a similar character imposed by the laws of the other territory.

2

The person entitled to the income must be a resident in Malta for the year immediately preceding the year of assessment and be in possession of evidence of the tax paid abroad.

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(2) Unilateral relief

Unilateral relief is given on a similar basis as treaty relief but in cases where the income received comes from a foreign territory with which Malta does not have a double taxation arrangement.

1

(3) Flat rate foreign tax credit (FRFTC) relief

FRFTC relief is only available to companies registered in Malta with an empowerment clause and for the income which such companies allocated to their foreign income account (FIA).

1

Unlike either treaty relief or unilateral relief, the tax credit is imputed at the fixed rate of 25% of the net amount received regardless of the actual tax rate suffered (deducted).

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Tutorial note: There is a fourth mechanism for double tax relief: Commonwealth relief, but this is not examinable.