

Fundamentals Level – Skills Module

Taxation (Malta)

Tuesday 12 June 2012



Time allowed

Reading and planning: 15 minutes

Writing: 3 hours

ALL FIVE questions are compulsory and MUST be attempted.
Tax rates and allowances are printed on pages 2–4.

Do NOT open this paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

This question paper must not be removed from the examination hall.

The Association of Chartered Certified Accountants

The Malta Institute of Accountants



Paper F6 (MLA)

SUPPLEMENTARY INSTRUCTIONS

1. Calculations and workings need only be made to the nearest Euro
2. All apportionments should be made to the nearest month unless stated otherwise
3. All workings should be shown

TAX RATES AND ALLOWANCES

The following tax rates and allowances for the year of assessment 2012 are to be used in answering the questions.

Individual income tax rates

Resident individual tax rates

Married couples – joint computation:

| € | |
|------------|-----|
| 0 – 11,900 | 0% |
| Next 9,300 | 15% |
| Next 7,500 | 25% |
| Remainder | 35% |

Other individuals:

| € | |
|------------|-----|
| 0 – 8,500 | 0% |
| Next 6,000 | 15% |
| Next 5,000 | 25% |
| Remainder | 35% |

Non-resident individuals

| € | |
|------------|-----|
| 0 – 700 | 0% |
| Next 2,400 | 20% |
| Next 4,700 | 30% |
| Remainder | 35% |

Corporate income tax

| | |
|---------------|-----|
| Standard rate | 35% |
|---------------|-----|

Value added tax (VAT)

| | |
|------------------------------|-----|
| Standard rate | 18% |
| Reduced rate | 5% |
| Reduced rate – accommodation | 7% |

Capital allowances – Income Tax Act rates

Industrial buildings and structures

| | |
|-------------------------|-----|
| Initial allowance | 10% |
| Wear and tear allowance | 2% |

Plant and machinery

Minimum number of years over which items of plant and machinery are to be depreciated:

| | |
|--|----|
| Computers and electronic equipment | 4 |
| Computer software | 4 |
| Motor vehicles | 5 |
| Furniture, fixtures, fittings and soft furnishings | 10 |
| Equipment used for the construction of buildings and excavation | 6 |
| Catering equipment | 6 |
| Aircraft | 12 |
| Ships and vessels | 10 |
| Electrical and plumbing installations and sanitary fittings | 15 |
| Cable infrastructure | 20 |
| Pipeline infrastructure | 20 |
| Communication and broadcasting equipment | 6 |
| Medical equipment | 6 |
| Lifts and escalators | 10 |
| Air conditioners | 6 |
| Equipment mainly designed or used for the production of water or electricity | 6 |
| Other machinery | 5 |
| Other plant | 10 |

Capital gains

Index of inflation

| | | | |
|------|--------|------|--------|
| 1983 | 428.06 | 1998 | 580.61 |
| 1984 | 426.18 | 1999 | 593.00 |
| 1985 | 425.17 | 2000 | 607.07 |
| 1986 | 433.67 | 2001 | 624.85 |
| 1987 | 435.47 | 2002 | 638.54 |
| 1988 | 439.62 | 2003 | 646.84 |
| 1989 | 443.39 | 2004 | 664.88 |
| 1990 | 456.61 | 2005 | 684.88 |
| 1991 | 468.21 | 2006 | 703.88 |
| 1992 | 475.89 | 2007 | 712.68 |
| 1993 | 495.60 | 2008 | 743.05 |
| 1994 | 516.06 | 2009 | 758.58 |
| 1995 | 536.61 | 2010 | 770.07 |
| 1996 | 549.95 | 2011 | 780.00 |
| 1997 | 567.95 | | |

Car fringe benefit calculation and rates

Annual value of benefit = (vehicle use + fuel value + maintenance value) x private use percentage

| | |
|-------------------------------------|-------------------------------|
| Vehicle use | % of vehicle value |
| Vehicle not more than six years old | 17% |
| Vehicle more than six years old | 10% |
| Fuel value | % of vehicle value |
| Vehicle value not exceeding €28,000 | 3% |
| Vehicle value exceeding €28,000 | 5% |
| Maintenance value | % of vehicle value |
| Vehicle value not exceeding €28,000 | 3% |
| Vehicle value exceeding €28,000 | 5% |
| Car value | Private use percentage |
| Not exceeding €16,310 | 30% |
| Exceeding €16,310 but not €21,000 | 40% |
| Exceeding €21,000 but not €32,620 | 50% |
| Exceeding €32,620 but not €46,600 | 55% |
| Exceeding €46,600 | 60% |

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Question 1 begins on page 6.**

ALL FIVE questions are compulsory and MUST be attempted

1 Catherine Earnshaw and Heathcliffe Bell are both UK nationals who were born and raised in the United Kingdom. They are in a relationship and live together but are not married. In 2008 Catherine and Heathcliffe signed a five year definite term employment contract with Bets Limited, a Maltese resident betting company, and moved to Malta. In the calendar year 2011 they spent 300 days in Malta and spent the remaining 65 days of the year on holiday in Mauritius. Catherine and Heathcliffe intend to return to the UK when their definite term contract of employment expires.

Catherine and Heathcliffe live in a villa in Kappara, Malta, which Bets Limited rents from a Maltese resident landlord for €800 per month. The market value of the villa is €350,000. Bets Limited allows Catherine and Heathcliffe to live in the villa and does not charge them any rent.

Heathcliffe's contract of employment provides for an annual salary of €50,000 and an annual bonus of €10,000. Bets Limited pays for Heathcliffe's health insurance premium of €2,000 per annum under a scheme which applies to all employees, and also pays him a disturbance allowance of €50 per month. Besides his job with Bets Limited, Heathcliffe is employed by Soft Limited, a Maltese resident company which develops computer software. Heathcliffe receives a salary of €10,000 per annum from Soft Limited. Bets Limited and Soft Limited are unrelated companies. Soft Limited retains tax from his salary at the rate of 15% (income from part-time employment) and, following Heathcliffe's instructions, deposits the salary in Heathcliffe's Swiss bank account which yields interest at the rate of 3% per annum. In 2011 Heathcliffe's Swiss bank account yielded interest of €3,000 which Heathcliffe did not receive in Malta but invested in Greek Government Bonds.

Catherine's contract of employment with Bets Limited contemplates the payment of an annual salary of €80,000 and an annual performance bonus of €40,000. Catherine's contract of employment also provides for the company's standard health insurance cover premium of €2,000 per annum and use of a company car. The car was bought by Bets Limited in 2010 for the price of €50,000 and all fuel and maintenance costs are borne by Catherine. In 2008 Catherine bought a small flat in Xemxija, Malta, which she has rented out on a short-lets fully furnished basis since 2008. In 2011 her income from the renting out of the flat amounted to €3,000. In 2011 Catherine sold the shares she held in her family's UK resident holding company to her brother and made a capital gain of €60,000. This gain was received in Catherine's Maltese bank account.

Heathcliffe incurred the following expenditure in the basis year 2011:

- (1) An interest expense of €10,000 paid in respect of a loan on the acquisition of a small shop in Sandringham, UK. Heathcliffe plans to open the shop on his return to the UK.
- (2) An alimony payment of €3,000 paid to his estranged wife who is a UK resident.
- (3) Financial assistance of €2,000 for the maintenance of his son from his marriage, who is a UK resident.
- (4) School fees for his son of €10,000. Heathcliffe's son goes to an English private school similar to a Maltese independent school.
- (5) Travel expenses of €2,000 spent in connection with Heathcliffe's employment with Soft Limited.

Catherine incurred the following expenditure in the basis year 2011:

- (i) The costs of refurbishing the villa in Kappara of €2,500.
- (ii) A donation of €2,000 to the Malta Cancer Foundation (a philanthropic institution).
- (iii) The cost of repairs to the flat in Xemxija of €1,000.
- (iv) Clothes, make-up and hairdresser costs of €4,000 spent in connection with office events including business meetings and professional seminars.

Required:

- (a) **State, giving reasons, whether Heathcliffe and Catherine will be considered as ordinarily resident and/or domiciled in Malta for tax purposes.** (3 marks)
- (b) **Assuming that Heathcliffe and Catherine are considered to be tax resident in Malta, calculate the chargeable income and tax payable by each of them for the year of assessment 2012.** (19 marks)

- (c) In January 2011 Mrs Bell (Heathcliffe's elderly mother) visited Heathcliffe. She stayed in Malta for three months and lived in the Kappara villa with Heathcliffe and Catherine. During her stay, Heathcliffe introduced Mrs Bell to his Maltese bank manager who convinced her to channel some of her investments to Malta. Mrs Bell opened a bank account in Malta and transferred all her savings to the Maltese bank account. In 2011 the Maltese bank account yielded interest of €10,000.

Mrs Bell's other sources of income are:

- (1) Her pension from the British Government of €800 per month. Mrs Bell continued to receive this pension during her stay in Malta but no funds were received in Malta in 2011 because Mrs Bell used the money to buy some stocks and shares listed on the London Stock Exchange.
- (2) Royalties received from her late husband's publishing house. In 2011 Mrs Bell was entitled to royalties amounting to €10,000 but instead of receiving this sum, she decided to re-invest these funds in a third edition of her husband's last book. None of these royalties were received in Malta in 2011.
- (3) Rents of €2,500 from a flat she owns in Yorkshire and rents out. For 2011 Mrs Bell agreed with her tenant that all rental payments would be made directly to her bank account in Malta.

Required:

(i) **State, giving reasons, Mrs Bell's tax status in Malta for the basis year 2011;** (2 marks)

(ii) **In respect of each item of Mrs Bell's income, state, giving reasons, whether it will be taxable in Malta for the year of assessment 2012.**

Note: you are not required to make any calculations for this part. (6 marks)

(30 marks)

- 2 Malta Holdings Limited ('MHL') is a company which was incorporated in Malta in 2001. The shareholders of MHL are Barranija Limited ('BL'), a non-resident company which holds 50% of the shares in MHL, and Frustiera Limited ('FL'), a Malta resident company which holds the remaining 50%. The shareholders of both FL and BL are two individuals who are neither domiciled nor ordinarily resident in Malta.

MHL's income for the year 2011 was as follows:

Trading income

- (1) Profits of €300,000 attributable to activities performed in MHL's head office in Malta. The head office trades in securities which are listed on the Malta Stock Exchange, there are no expenses directly relating to this activity. MHL rents its head office (which measures 500 square metres) from an unrelated party for €15,000 per annum.
- (2) Profits of €100,000 attributable to the branch (Branch X) which MHL has established in a tax haven where the branch is exempt from tax. The branch is involved in trading in securities.
- (3) An unrealised foreign exchange gain of €10,000 attributable to Branch X in the tax haven jurisdiction.

Non-trading income

- (i) A dividend from A Ltd of €50,000, net of foreign tax at the rate of 10%. MHL owns 100% of the equity shares in A Ltd, which is resident in another EU state.
- (ii) A dividend from Investments Limited ('IL') of €50,000, net of withholding tax at the rate of 15%. IL is a company resident in a non-EU state which pays corporate tax in its home jurisdiction at the rate of 25%. MHL is an equity shareholder in IL and has held 1% of the company's equity shares for an uninterrupted period of 100 days. The total investment value of the equity shares in IL is €2,500,000. MHL has proof of the tax paid as withholding tax on the dividend and proof of the tax paid by IL as corporate tax.
- (iii) A net dividend of €30,000 from B Ltd, a Maltese resident company. MHL owns 100% of the equity shares of B Ltd.
- (iv) A capital gain of €30,000 derived from the transfer of equity shares in C Ltd, a Maltese resident company.
- (v) A net dividend of €25,000 from D Ltd, a Maltese property company. MHL owns 100% of the equity shares of D Ltd.
- (vi) Rental income of €120,000 from the renting out by MHL of its warehouse in Dubrovnik.

Required:

- (a) For the basis year 2011, allocate Malta Holdings Limited's (MHL) profits to the relevant tax accounts and calculate the tax charge of MHL, after claiming the most advantageous reliefs available.**

Note: you should present your answer in a columnar format, clearly identifying both the applicable tax account and, where relevant, distinguishing between participating and non-participating holdings. (20 marks)

- (b) Calculate the maximum tax refunds due to MHL's shareholders out of each of MHL's tax accounts for the basis year 2011.** (5 marks)

(25 marks)

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Question 3 begins on page 10.**

3 Anthony Borg is the sole heir of an estate which comprises assets and properties situated in Italy, Malta and the United Kingdom. Mr Borg has decided to transfer some of his assets to a holding company he will establish in Malta, named Borg Estates Limited ('BEL'), and some other assets to his only child, Pablo (Pablo is 26 years old). BEL will be wholly owned by Mr Borg. Mr Borg wishes to minimise the tax liability arising from the asset transfers wherever possible.

The relevant contracts are described below and will all be executed in 2012.

1. Villa in Wardija, Malta

Mr Borg will transfer a villa in Wardija valued at €600,000 to BEL. The property will be transferred by title of donation (nil consideration but the property will be given a sales value equivalent to its acquisition value). Mr Borg had inherited this property from his parents in 1990, since when he has occupied it as his family home. The value declared in the deed of inheritance was €100,000. (2 marks)

2. Arable land in Pembroke, Malta

Mr Borg will transfer a piece of arable land in Pembroke valued at €100,000 to Pablo. The property will be transferred by title of donation (nil consideration but the property will be given a sales value equivalent to the acquisition value). Mr Borg had also inherited this property from his parents in 1990, when the value declared in the deed of inheritance was €10,000. (2 marks)

3. Summer residence in Florence, Italy

Mr Borg will transfer his summer residence in Florence to BEL. The property will be transferred at a consideration of €1,300,000. Mr Borg had also inherited this property from his parents in 1990, when the value declared in the deed of inheritance was €400,000. (2 marks)

4. Lease (kera) in Malta

Mr Borg intends to transfer his right to occupy a palace in Valletta by title of rent to BEL. The transfer will be made at nil consideration but a *laudemium (rigal)* of €35,000 will be paid to the landlord. The market value of the palace is €250,000. (2 marks)

5. Family business in Malta

Mr Borg will transfer the family business to Pablo. The consideration for the transfer of the business will be paid by way of an annuity equal to 10% of the business's chargeable income. (2 marks)

6. Intellectual property rights registered in Malta

Mr Borg will transfer the patents and trademarks which he had inherited from his parents to Pablo. The patents will be transferred at a consideration of €50,000. The market value of the patents is €100,000. The trademarks will be transferred at a consideration of €75,000. The market value of the trademarks is €70,000. (3 marks)

7. Shareholding held in Shares Limited

Mr Borg will transfer 500 shares in Shares Limited, a Maltese incorporated company, to Pablo. The shares being transferred represent 50% of the total share capital of the company. The issued share capital is 1,000 ordinary shares of €1 each. Mr Borg became the sole shareholder of Shares Limited when he incorporated the company in 2005; at the time of incorporation the shares had a nominal value of €1 each. The net asset value of Shares Limited as at 31 December 2011 was €100,000 and the company's two years' average profits for the five financial years immediately preceding the year in which the transfer is to be made are €15,000. (4 marks)

8. Rights in Dividends Limited

Mr Borg has agreed to enter into an agreement with Pablo, wherein Mr Borg will cede in favour of Pablo his right to receive dividends from Dividends Limited. No consideration will be charged for the cession of rights. Dividends Limited was incorporated in Malta in 1999. The shareholders of Dividends Limited are Mr Borg who holds 9,999 shares of €1 each and Pablo who holds one share of €1. Mr Borg became a shareholder of Dividends Limited when he incorporated the company. The shares have always had a nominal value of €1 each. (1 mark)

9. Shares in a company in which the Government of Malta has an interest

In 1980 Mr Borg had incorporated a Netherlands company named Gvern Limited. Gvern Limited has an issued share capital of 1,000 shares with a nominal value of €1 each. The Government of Malta holds 80% of the share capital of Gvern Limited and Mr Borg holds the remaining 20% of the share capital. Mr Borg will sell his 200 shares in Gvern Limited to BEL for a consideration of €100,000. (2 marks)

Required:

For each of the transactions (1) to (9), briefly explain whether or not it will be subject to tax, and, if taxable, the applicable rate(s) of tax and basis of computation that will be used.

Note: you are not required to calculate the tax payable. The mark allocation is shown against each of the transactions above.

(20 marks)

- 4 (a) In 2005 Andre and Josef formed a partnership *en collectif* which they named the Andef Partnership (Andef). Andef trades in securities and commercially exploits property (property leasing, construction and development). The partnership agreement provides that profits and losses will be shared equally.

In the year ended 31 December 2011 Andef received the following:

1. Rent of €60,000 from the ten tenants of a block of flats situated in Msida, Malta.
2. Rent of €155,000 from the five firms that occupy offices situated in Swatar, Malta.
3. Gross bank interest of €5,000 from Andef's bank account held in Switzerland. This bank interest was exempt from tax in Switzerland.
4. A consideration of €150,000 from the sale of a flat in Gzira, Malta. Andef had bought the flat in 2009 for a consideration of €100,000. Andef had refurbished the flat in the year of re-sale, at a cost of €30,000. On the execution of the deed of sale, Andef had opted out of property transfer tax.

The figures above were calculated before charging partners' salaries of €35,000 per partner, interest of €150,000 paid on monies borrowed on capital employed in acquiring income, and capital allowances for the year amounting to €30,000. There were no capital allowances brought forward from previous years.

Required:

- (i) **Calculate the Andef Partnership's taxable profits for year of assessment 2012, showing the division of profits between the partners.** (7 marks)
- (ii) **Briefly explain the treatment of the partners' salaries.** (2 marks)

- (b) In 2011 a sole trader sold the following assets:

- (1) A commercial van for the sum of €35,000. He had bought the van in 2004 for €50,000.
- (2) A second-hand non-commercial vehicle for the sum of €10,000. He had bought the vehicle in 2009 for €15,000.

Both assets had been booked as 'plant and machinery' and capital allowances had been claimed.

Required:

- Prepare a balancing statement for each of the assets and calculate the balance charge or allowance (if any).** (6 marks)

(15 marks)

- 5** Finanziaria Limited ('Fin') is a Maltese resident company, established in Malta for value added tax (VAT) purposes. Fin is a licensed company and it will supply the following services:
- (1) The provision of a safe deposit box to a non-taxable person for a consideration of €1,000. The deposit box will be situated in Malta.
 - (2) The provision of investment advice to a Maltese taxable person for a consideration of €50,000.
 - (3) The provision of investment advice to a non-taxable person who is established outside the EU for a consideration of €1,000.
 - (4) The provision of payment services to a Maltese taxable person for a consideration of €13,000.
 - (5) The provision of investment advice to a taxable person established in another EU member state for a consideration of €10,000.
 - (6) The provision of investment advice to a Maltese non-taxable person for a consideration of €50,000.
 - (7) The supply of traveller's cheques to a foreign individual for a consideration of €60,000.
 - (8) The supply of accountancy services to a taxable person established in Malta for a consideration of €5,000.
 - (9) The sub-letting of office space to a Maltese resident company registered for VAT purposes under article 10 for a consideration of €1,000 a month.
 - (10) The sale of furniture belonging to Fin on which VAT had originally been recovered, to a Maltese individual who is a non-taxable person, for a consideration of €100.

Required:

Calculate the value added tax (VAT) that must be charged on each of the supplies (1) to (10) above, if any. If you conclude that no VAT is chargeable, state the reason.

(10 marks)

End of Question Paper