Answers

	Marks
1 Nicholas and Janet	
(a) Nicholas and Janet have moved to Malta with a view to taking up residence here on a continuing basis. Accordingly, they are considered to be ordinarily resident in Malta for tax purposes throughout the year of assessment 2013.	1
With regard to domicile, Nicholas and Janet were born and raised outside Malta, seemingly with no previous connection with Malta, which suggests that their domicile of origin is outside Malta.	1
To acquire a new domicile of choice in Malta would require a firm intention on the part of Nicholas and Janet to have moved to Malta with a view to remaining here and never leaving Malta, which is clearly not the case. Therefore, they are not considered to be domiciled in Malta for the year of assessment 2013.	1
As persons who are ordinarily resident but not domiciled in Malta, Nicholas and Janet are subject to the source and receipt/remittance basis of taxation, whereby they are taxable on income and capital gains arising in Malta, but not on foreign source income unless received in or remitted to Malta, and not on foreign source capital gains (irrespective of whether received in or remitted to Malta).	2
	5

(b) Chargeable income for the year of assessment 2013

	€	€	€	Marks
Janet				
Gross income from consultancy services		40,000		0·5
Less: Allowable deductions:				
Rental expense		(6,000)		0·5
Wear and tear allowances:				
Furniture (€2,500/10 years)	(250)			1
Computer equipment (€2,000/4 years)	(500)			1
		(750)		
Chargeable income from consultancy services			33,250	
Director's fees (excluded from part-time rules)			10,000	0·5
Total			43,250	
Nicholas				
Basic salary			35,000	0·5
Fringe benefits				
Beneficial loan arrangement				
Interest-free loan of €20,000 at 8% benchmark rate		1,600		1·5
Vehicle allowance:				
Vehicle use value (17% of €30,000)	5,100			0·5
Fuel value (fuel costs borne by employee)	nil			0·5
Maintenance value (5% of €30,000)	1,500			0·5
	6,600			
At private use percentage (50%)		3,300		0·5
Health insurance cover:				
Value of insurance cover	1,000			0·5
Less: Tax exempt portion (3 x 250, the lowest premium cover available generally to employees of FLL)	(750)			1
Taxable value of health insurance benefit		250		
Provision of business mobile phone (exempt)		0		0·5
Subscription to professional body (exempt)		0		0·5
Free clothing allowance:				
Value of free clothes	1,000			0·5
Less: In-house benefit reduction	(700)			1
Taxable value of free clothing allowance		300		
Business-specific training course (exempt)		0		0·5
Award on completion of course		500		0·5
Total value of taxable fringe benefits			5,950	
Total			40,950	
Other income				
Gross foreign source dividend (with a credit for foreign tax paid of €100)			1,000	0·5
Interest on Dutch term deposit – remitted to Malta			200	0·5
Interest on Dutch savings deposit (not remitted to Malta – not taxable)			0	0·5
Capital gain on sale of MSE-listed shares – tax exempt			0	0·5
Local dividend income (€130/0·65) (not subject to further tax due to imputation tax credit)			200	1
Foreign source capital gain on sale of former home – not taxable in Malta (irrespective of remittance to Malta)			0	0·5
Local interest income (gross) (taxed by final withholding tax at 15%, i.e. €150 in terms of the investment income provisions)			0	1
Total			1,400	
				17
Total chargeable income			85,600	

			Marks
(c) Tax payable for the year of assessment 2013			

Separate computation

		€	
Nicholas			
€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 €40,950	at 35%	7,508	
Tax chargeable and payable		9,658	1

		€	
Janet			
€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 €44,650	at 35%	8,803	
Tax chargeable		10,953	1
Less: Credit for tax at source on local IPA dividend		(70)	0·5
Less: Credit for foreign tax paid on foreign source dividend		(100)	0·5
Tax payable		10,783	
Total tax payable (exclusive of €150 final withholding tax paid on local bank interest income)		20,441	

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

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 €85,600	at 35%	19,915	
Tax chargeable		23,185	1
Less: Credit for tax at source on local IPA dividend		(70)	) 0·5
Less: Credit for foreign tax paid on foreign source dividend		(100)	)
Tax payable (exclusive of €150 final withholding tax paid on local bank interest income)		23,015	

The most beneficial method of tax computation is the separate computation, with total tax payable of €20,441 exclusive of the €150 final withholding tax paid on local bank interest income. 0·5

5

(d) Had Nicholas and Janet moved to Malta on a permanent basis with the firm intention of never leaving, they would be considered to have acquired a domicile of choice in Malta and thus be considered both ordinarily resident and domiciled in Malta for tax purposes. In this event, they would be fully subject to tax in Malta on their worldwide income and gains. 1·5

Under the worldwide basis of taxation, the following additional items would have been subject to tax in the hands of Nicholas and Janet for the year of assessment 2013:

	€	
Interest on Dutch savings deposit	600	0·5
Foreign-source capital gain on sale of former home	50,000	0·5
	50,600	

This would result in additional tax payable at 35% of €17,710. 0·5

3

30

					Marks

2 Medina Limited

(a) Income tax computation for the year of assessment 2013 (basis year ended 31 December 2012)

(i) **Gains/profits from a trade, business, profession or vocation**

Adjustment of profit per financial statements for tax purposes

	€	€	€	Marks
Net profit before tax as per financial statements			605,200	
Add back:				
Depreciation		30,200		0·5
Payments of a voluntary nature				
– Voluntary payment to local social club	1,000			0·5
– Charitable donations	700			0·5
		1,700		
VAT penalty (not incurred in the production of the income)		250		0·5
Expenditure relating to rental income				
– Repairs and maintenance	2,000			
– Ground rent	250			
– Licence fee	400			
– Interest	1,500			
		4,150		0·5
Realised loss on disposal of fixed asset		600		0·5
Unrealised foreign exchange losses		2,500		0·5
Provisions for doubtful debts:				
– Specific	10,000			0·5
– General	2,500			0·5
– Bad debts actually written off (allowed)	0			0·5
		12,500		
Disallowed portion of non-commercial motor vehicle lease expense ([28,000 – 14,000]/28,000 x €8,000)		4,000		1
			55,900	
Deduct:				
– Interest income		(12,000)		0·5
– Dividend income		(50,000)		0·5
– Rental income		(4,000)		0·5
			(66,000)	
Income before wear and tear allowances			595,100	
Wear and tear allowances claimed and absorbed (working 1)			(23,875)	W
Balancing allowance claimed and absorbed (working 2)			(475)	W
Group losses claimed and absorbed:				
Dingli Limited	12,000			1·5
Rabat Limited	0		(12,000)	1
Chargeable trade/business income			558,750	

(ii) **Interest income**

	€
Chargeable interest income	12,000

(iii) **Dividend income**

	€	Marks
Gross dividend income	50,000	
Less: Dividend received out of FTA profits	(36,000)	0·5
Less: Dividend received out of Untaxed account	(4,000)	0·5
Chargeable dividend income	10,000	

			Marks

(iv) **Rental income**

	€	€	
Gross rental income		4,000	
Less:			
Rent/GR/similar burden payable	(250)		0·5
Licence fee payable	(400)		0·5
Further deduction (20% of [4,000 – 250 – 400])	(670)		1
Interest expense	(1,500)		0·5
		(2,820)	
Chargeable rental income		1,180	

Workings:

(1) Wear and tear allowances

	€	
Furniture and fittings over 10 years (10% x €100,000)	10,000	0·5
Computer equipment over 4 years (25% x (€50,000 – €2,500 cost of laptop sold)	11,875	1
Air conditioners over 6 years (16·67% x €12,000)	2,000	0·5
	23,875	

(2) Balancing statement: laptop

	€	€	
Cost of acquisition		2,500	
Accumulated wear and tear allowances (4 years)			
– 2011 (full year capital allowances taken in year of acquisition)	(625)		
– 2012 (no capital allowances taken in year of disposal)	–		
		(625)	
Tax written down value		1,875	1
Proceeds on disposal		(1,400)	0·5
Balancing allowance		475	
			17

Tutorial note: *In terms of ITA Art. 16, two companies are deemed to be members of a group of companies for group relief purposes where one company is a '51% subsidiary' of the other company or both companies are the '51% subsidiary' of a third company resident in Malta. Therefore, group relief is available in respect of the trading tax losses for the year of Dingli Limited, but not Rabat Limited where the common shareholding is through individuals. Please also note that group loss relief applies to trading tax losses, but not to capital losses or unabsorbed capital allowances.*

(b) Tax charge for the year of assessment 2013

Chargeable income subject to standard corporate income tax rate

	€	
Trade/business income	558,750	
Dividend income	10,000	
Rental income	1,180	
	569,930	
Tax at 35%	199,476	1
Interest income subject to final withholding tax (FWT) at 15% (in terms of the investment income provisions)	12,000	
Tax at 15%	1,800	1
Total tax charge	201,276	
		2

Marks

(c) Allocation of distributable profits to the tax accounts

	Brought forward	Current year allocation		Carried forward	
	€	€	€	€	
Final tax account (FTA)	125,500		46,200	171,700	
– Interest subject to 15% FWT (12,000 x 85%)		10,200			1
– Exempt dividends		36,000			0·5
Immovable property account (IPA)	200,000		7,267	207,267	
– Rental income (1,180 x 65%)		767			0·5
– IPA dividends (10,000 x 65%)		6,500			0·5
Maltese taxed account (MTA) (558,750 x 65%)	800,000		363,188	1,163,188	0·5
Foreign income Account (FIA)	–		–	–	
Untaxed account	115,000		(12,731)	102,269	0·5
Distributable profits	1,240,500		403,924*	1,644,424	0·5
					4

* 605,200 – (199,476 + 1,800) = 403,924

Tutorial note: *It is only the current year allocation which is specifically required for this question. The brought forward and carried forward balances are not being examined and are shown for illustrative purposes only.*

(d) On payment of a dividend out of the untaxed account to a 'recipient' who is not exempt from tax, the distributing company is obliged to withhold tax thereon at 15%.

Therefore, if Medina Limited pays a dividend out of its untaxed account to its shareholders, Julian Borg and Joseph Borg, it will be obliged to withhold tax therefrom at 15% and pay the tax withheld to the Commissioner of Inland Revenue within 14 days following the end of the month in which the untaxed dividend is paid. 2

25

Tutorial note: *For the purposes of the withholding tax on distributions from the untaxed account, a 'recipient' is defined so as to include, amongst others:*

– *A person (other than a company) resident in Malta; and*
– *A non-resident person who is owned and controlled by, or who acts on behalf of, an individual who is ordinarily resident and domiciled in Malta.*

3 (a) In addition to immovable property, the following assets and interests are subject to income tax on capital gains in terms of the Income Tax Act:

– securities;
– business;
– goodwill;
– business permits;
– copyrights;
– patents;
– trademarks;
– trade names;
– a beneficial interest in a trust;
– a transfer of value in securities; and
– a transfer of an interest in a partnership.

Any SIX items only required, ½ mark each, maximum 3

(b) Mediterranean Limited

1. The equity shareholding in Waffles Limited is ≥ a 10% equity shareholding, it therefore constitutes a participating holding. 1

   As such, the participation exemption applies and the chargeable income will be nil. 0·5

   Tutorial note: *The anti-abuse provisions associated with the participation exemption apply to dividends but not to capital gains.*

2. The shareholding in Roma Limited constitutes an equity holding since it confers two out of the three equity holding rights, namely the right to profits available for distribution and to assets available for distribution on a winding up. 1

Marks

As the investment cost ≥ €1,164,000 and it was held for an uninterrupted period of ≥ 183 days, it constitutes a participating holding. 1

As such, the participation exemption applies and the chargeable income will be nil. 0·5

3. Preference shares do not constitute securities for the purposes of the provisions governing income tax on capital gains. 1

   Therefore, they fall outside the scope of the charge to income tax on capital gains, such that the chargeable income will be nil. 0·5

4. As a company resident in Malta, Mediterranean Limited is chargeable to tax on its worldwide income and gains. 1

   Therefore, the disposal of the Sicily investment property will result in a capital gain as follows:

		€	Marks
Consideration		190,000	
Cost of acquisition adjusted for inflation			
Inflation index for 2008	743·05		
Inflation index for 2011	791·02		
€150,000 x 791·02/743·05		(159,684)	1
Improvements		(15,000)	0·5
Maintenance allowance (0·4% x 3 years x €150,000)		(1,800)	0·5
Chargeable capital gain		13,516	
Income tax charge on the capital gain at 35%		4,731	0·5

5. The disposal of the Malta investment property will be subject to property transfer tax; however, as Mediterranean Limited has held the property for less than seven years, it can elect to opt out of the property transfer tax system and pay income tax on the capital gain instead. 1

   Calculation of property transfer tax

	€	Marks
Consideration	350,000	0·5
Brokerage fees	(16,000)	1
Amount assessable to property transfer tax	334,000	
Property transfer tax at 12%	40,080	0·5

   Calculation of capital gain

		€	Marks
Consideration		350,000	
Cost of acquisition adjusted for inflation			
Inflation index for 2008	743·05		
Inflation index for 2011	791·02		
€285,000 x 791·02/743·05		(303,399)	0·5
Duty on documents and transfers paid on acquisition		(14,250)	0·5
Maintenance allowance (0·4% x 3 years x €285,000)		(3,420)	0·5
Other costs (less than 5% of consideration)		(16,000)	0·5
Chargeable capital gain		12,931	
Income tax charge on the capital gain at 35%		4,526	0·5

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

6. A trademark is an asset which falls within the scope of the charge to income tax on capital gains and so the disposal will result in a chargeable gain as follows: 0·5

	€	Marks
Consideration	25,000	
Cost of acquisition	(10,000)	0·5
Legal and other fees incurred in the production of the income	(8,500)	0·5
Chargeable capital gain	6,500	
Income tax charge on the capital gain at 35%	2,275	0·5
		17
		20

			Marks
4	**International Trading (Malta) Limited**		
1.	**Malta trading income**		
	Allocated to the Malta tax account (MTA)		0·5
	Chargeable income	€150,000	
	Tax chargeable and payable at 35%	€52,500	0·5
	Tax refundable to International Holdings (Malta) Limited (IHML) on a dividend distribution (6/7ths of €52,500)	€45,000	1
2.	**Foreign trading income attributable to a permanent establishment (PE)**		
	Allocated to the foreign income account (FIA)		0·5
		€	
	Chargeable income	200,000	
	Tax chargeable at 35%	70,000	0·5
	Less: Double taxation relief (22%)	(44,000)	0·5
	Tax payable in Malta	26,000	
	Tax refundable to IHML on a dividend distribution (2/3rds of €70,000)	€46,667	0·5
	Limited to tax paid in Malta	€26,000	1
3.	**Foreign trading income not attributable to a PE**		
	Allocated to the MTA		0·5
		€	
	Chargeable income	75,000	
	Tax chargeable at 35%	26,250	0·5
	Less: Double taxation relief	(1,000)	0·5
	Tax payable in Malta	25,250	
	Tax refundable to IHML on a dividend distribution (6/7ths of €26,250)	€22,500	1
4.	**Foreign source investment income (not passive royalties)**		
	Allocated to the FIA		0·5
		€	
	Foreign income received in Malta	50,000	
	Add: Flat rate foreign tax credit FRFTC (25%)	12,500	0·5
	Grossed-up income	62,500	
	Tax chargeable at 35%	21,875	0·5
	Less: FRFTC	(12,500)	0·5
	Tax payable in Malta	9,375	
	Tax refundable to IHML on a dividend distribution (2/3rds of €9,375)	€6,250	1
5.	**Foreign source dividend**		
	Allocated to the FIA		0·5
		€	
	Chargeable income	70,000	
	Tax chargeable at 35%	24,500	0·5
	Less: Double taxation relief (3·5%)	(2,450)	0·5
	Tax payable in Malta	22,050	
	Tax refundable to IHML on a dividend distribution (2/3rds of €24,500)	€16,333	1

		Marks
6. **Foreign source passive royalties**		
Allocated to the FIA		0·5
Chargeable income	€35,000	
Tax chargeable and payable at 35%	€12,250	0·5
Tax refundable to IHML on a dividend distribution (5/7ths of €12,250)	€8,750	1
		15

5 Value added tax (VAT)

		Marks
(a)	A supply of goods is defined as the transfer of the right to dispose of tangible property as owner.	1
(b)	A supply of services is defined as a supply which is not a supply of goods.	1
(c)	A supply of goods which are transported takes place where the goods are at the time when the transport of those goods begins.	1
(d)	A supply of goods which are not transported takes place where the goods are situated at the time when they are placed at the disposal of the person acquiring those goods.	1
(e)	A supply of goods which are installed or assembled by or on behalf of the supplier takes place where the goods are installed or assembled.	1
(f)	The place of supply of services to a taxable person acting as such shall be the place where the customer is established.	1
	However, if those services are provided to a fixed establishment of the taxable person located in a place other than the place where he has established his business, the place of supply of those services shall be the place where that fixed establishment is located. (In the absence of such a place of establishment or fixed establishment, the place of supply of the services shall be the place where the taxable person who receives such services has his permanent address or usually resides.)	1
		2
(g)	The place of supply of services to a non-taxable person shall be the place where the supplier is established.	1
	However, if those services are provided from a fixed establishment of the supplier located in a place other than the place where he has established his business, the place of supply of those services shall be the place where that fixed establishment is located. (In the absence of such a place of establishment or fixed establishment, the place of supply of the services shall be the place where the supplier has his permanent address or usually resides.)	1
		2
(h)	No Maltese VAT is chargeable where a Malta taxable person supplies accountancy services to a non-taxable person who is established outside the EU, as the place of supply in such circumstances is where the customer is established.	1
		10