Fundamentals Level – Skills Module

Taxation (Malta)

Thursday 8 June 2017

Paper F6 (MLA)

Time allowed: 3 hours 15 minutes

This question paper is divided into two sections:

Section A – ALL 15 questions are compulsory and MUST be attempted

Section B – ALL SIX questions are compulsory and MUST be attempted

Tax rates and allowances are printed on pages 2–4.

Do NOT open this question paper until instructed by the supervisor.

Do NOT record any of your answers on the question paper.
This question paper must not be removed from the examination hall.

Think Ahead

ACCA

MIA

SCIENTIA VIGILANTIA

The Association of Chartered Certified Accountants

The Malta Institute of Accountants

SUPPLEMENTARY INSTRUCTIONS

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

TAX RATES AND ALLOWANCES

The following tax rates and allowances for 2016 (year of assessment 2017) are to be used in answering the questions.

Individual income tax

Resident individual tax rates

Married couples – joint computation

€	€	Rate	Subtract – €
0	to 12,700	0%	0
12,701	to 21,200	15%	1,905
21,201	to 28,700	25%	4,025
28,701	to 60,000	25%	3,905
60,001 and over		35%	9,905

Other individuals

€	€	Rate	Subtract – €
0	to 9,100	0%	0
9,101	to 14,500	15%	1,365
14,501	to 19,500	25%	2,815
19,501	to 60,000	25%	2,725
60,001 and over		35%	8,725

Parents maintaining a child/paying maintenance

€	€	Rate	Subtract – €
0	to 10,500	0%	0
10,501	to 15,800	15%	1,575
15,801	to 21,200	25%	3,155
21,201	to 60,000	25%	3,050
60,001 and over		35%	9,050

Non-resident individuals

€	€	Rate
0	to 700	0%
701	to 3,100	20%
3,101	to 7,800	30%
7,801 and over		35%

Note: In the case of non-resident EU/EEA individuals whose worldwide income is not derived from Malta as to at least 90%, the tax liability is capped as follows:

$$\frac{\text{Malta chargeable income}}{\text{Worldwide income}} \times \text{Tax charge if worldwide income is charged at the applicable resident individual tax rates}$$

Corporate income tax

Standard rate	35%

Value added tax (VAT)

Standard rate	18%
Reduced rate – general	5%
Reduced rate – accommodation in premises required to be licensed in virtue of the Malta Travel and Tourism Services Act	7%

Capital allowances

Industrial buildings and structures

Initial allowance	10%
Wear and tear allowance	2%

Plant and machinery

Wear and tear allowance as indicated in the question where applicable

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 airframe or engine	6
Aircraft engine or airframe overhaul	6
Aircraft interiors and other parts	4
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

Capital gains index of inflation

1983	428·06	2000	607·07
1984	426·18	2001	624·85
1985	425·17	2002	638·54
1986	433·67	2003	646·84
1987	435·47	2004	664·88
1988	439·62	2005	684·88
1989	443·39	2006	703·88
1990	456·61	2007	712·68
1991	468·21	2008	743·05
1992	475·89	2009	758·58
1993	495·60	2010	770·07
1994	516·06	2011	791·02
1995	536·61	2012	810·16
1996	549·95	2013	821·34
1997	567·95	2014	823·89
1998	580·61	2015	832·95
1999	593·00	2016	838·29

Applicability of increase for inflation

$$\frac{\text{Cost of acquisition/improvements}}{1} \times \frac{\text{index(yd)} - \text{index(ya)}}{\text{index(ya)}}$$

Where:
Index(yd) is the index for the year immediately preceding that in which the transfer is made;
Index(ya) is the index for the year immediately preceding that in which the property in question had been acquired or completed, whichever is the later, or, when it relates to improvements, for the year immediately preceding that in which the cost of carrying out the improvements was incurred.

Market value percentage attributable to shares in a company

Y = (0·4 x A) + (0·2 x B) + (0·4 x C)

Where:
A is the percentage of the issued share capital represented by the nominal value of the shares;
B is the percentage of the total voting rights in the company attached to the shares;
C is the percentage of the profits available for distribution to the ordinary shareholders attributable to the holder of the shares.

Annual market rent (tax accounting)

The annual market rent of immovable property situated in Malta owned and used by a company for the purpose of its activities (excluding property which is rented by the said company to other parties) is calculated by multiplying the aggregate surface area in square metres of all floors of such premises so owned and used by €250 per annum.

Car fringe benefit rates

Vehicle use	**Percentage of vehicle value**
Vehicle not more than six years old	17%
Vehicle more than six years old	10%
Fuel value	
Vehicle value not exceeding €28,000	3%
Vehicle value exceeding €28,000	5%
Maintenance value	
Vehicle value not exceeding €28,000	3%
Vehicle value exceeding €28,000	5%

Private use percentages

Car value

From €	**To** €	
0	16,310	30%
16,311	21,000	40%
21,001	32,620	50%
32,621	46,600	55%
46,601 and over		60%

Section B – ALL SIX questions are compulsory and MUST be attempted

Please write your answers to all parts of these questions on the lined pages within the Candidate Answer Booklet.

1 Island Insurance Limited (IIL), a company established in Malta, is engaged in providing insurance services under a licence issued in terms of the Insurance Business Act. IIL operates through a divisional structure consisting of three independent departments, which service Maltese clients, other European Union (EU) clients, and non-EU clients, respectively. IIL's turnover (insurance premium income) for the quarter ended 30 September 2016 is analysed as follows:

	Retail clients		Business clients		
	Life insurance	General insurance	Life insurance	General insurance	Total
	€	€	€	€	€
Maltese clients	5,100	7,200	1,200	3,900	17,400
EU clients outside Malta	6,600	8,900	2,500	14,900	32,900
Non-EU clients	9,200	4,600	1,900	21,700	37,400
	20,900	20,700	5,600	40,500	87,700

During the same quarter, IIL also incurred the following expenditure (exclusive of any applicable value added tax (VAT)), as supported by tax invoices where applicable:

	Maltese clients department	Other EU clients department	Non-EU clients department	Total
	€	€	€	€
Staff salaries and wages	7,100	12,400	16,200	35,700
Intra-EU acquisition of laptops	600	800	900	2,300
Importation of computer peripherals	400	600	1,100	2,100
Stationery purchased locally	90	110	210	410
Local postage stamps	50	70	130	250
Local bank charges	250	700	1,200	2,150
Consultancy fees payable to overseas group services company (note 1)	1,200	1,600	2,200	5,000
Software licensing fees payable to overseas group services company (note 1)	900	1,400	1,700	4,000
Utility bills:				
Water (supplied by the public authority)	400	700	900	2,000
Electricity	1,120	1,600	2,100	4,820
	12,110	19,980	26,640	58,730

Note

1. The overseas group services company is established outside Malta, does not have any establishment in Malta, and is not registered for VAT in Malta.

Required:

(a) **State and briefly explain the type of value added tax (VAT) registration, if any, which applies to Island Insurance Limited in Malta.** (2 marks)

(b) **For Island Insurance Limited's VAT return period for the quarter ended 30 September 2016, calculate:**

- **the output tax chargeable;**
- **the input tax creditable; and**
- **the VAT payable/excess credit for the period.**

List all of the items of expenditure referred to in the question, clearly identifying by the use of zero (0) any to which VAT does not apply or where an input credit is not deductible. (8 marks)

(10 marks)

2 James and Anne are siblings with both parents in common, and who live together. They are both ordinarily resident and domiciled in Malta, and each own 20% of the share capital of Kolonna Limited (KL). KL is a private limited liability company registered in Malta, which was incorporated on 15 April 2008, KL's balance sheet as at 31 December 2016 is as follows:

	€
Immovable property	100,000
Plant and equipment	40,000
Current assets	12,000
Current liabilities	(8,000)
	144,000
Share capital (5,000 shares of €1 each)	5,000
Distributable reserves	139,000
	144,000

Additional information:

1. The immovable property is owned and used by KL for the purpose of its business and is stated in the balance sheet at its historical cost. The market value of the property as at 31 December 2016 has been formally estimated by an architect at €240,000.
2. KL does not hold investments in any other entities.
3. All of the shares in KL confer equal voting rights and entitlement to profits. The shares were all subscribed for at cost by the shareholders, upon the incorporation of KL.
4. The profit history of KL for the last six years is as follows:

	Profit before tax	**Profit after tax**
	€	€
Financial year ended 31 December		
2016	39,800	30,900
2015	32,300	26,500
2014	22,400	19,100
2013	17,500	13,600
2012	7,300	5,700
2011	3,600	(1,300)

Prior to 2017, there had been no changes in the shareholding of KL but on 1 February 2017, James accepted an offer from an unrelated third party to purchase all of his shares in KL at a price of €45 per share. On 15 March 2017, Anne also received and accepted an offer from the same third party to purchase all of her shares in KL, at the price of €48 per share.

Required:

In respect of the disposals of shares in Kolonna Limited made by James and Anne in 2017:

(a) State, with reasons, whether or not the respective disposals constitute the transfer of a controlling interest. (3 marks)

(b) Compute the capital gain chargeable to tax, if any, for each of the disposals for the year of assessment 2018.

Notes:
1. **You should disregard any deduction for inflation allowances.**
2. **You are NOT required to calculate the tax payable.** (7 marks)

(10 marks)

3 Coffee Products Trading Limited (CPTL) is a company which was incorporated in Malta on 1 February 2016. CPTL is managed and controlled in Malta, and is fully owned by Coffee Products Holdings Limited (CPHL). CPHL was also incorporated in Malta on 1 February 2016, and is managed and controlled in Malta. The sole shareholder of CPHL is David, an individual who is neither ordinarily resident in Malta nor domiciled in Malta.

During its first financial year ended 31 December 2016, CPTL derived the following streams of income:

1. Income from local trading operations within the Maltese market. The total income chargeable to tax (computed in accordance with the Income Tax Act) amounted to €220,000.
2. Income from trading operations within a foreign country which is attributable to a permanent establishment of CPTL in that foreign country, and which suffered tax in that foreign country at the rate of 20%. The total income chargeable to tax (computed in accordance with the Income Tax Act) amounted to €140,000.
3. Income from other overseas market trading operations which is not attributable to a permanent establishment situated outside Malta. The total income chargeable to tax (computed in accordance with the Income Tax Act) amounted to €90,000. Foreign taxes of €2,000 were suffered in relation to this income, for which double taxation relief (treaty relief) is available and will be claimed.
4. Foreign source passive interest amounting to €70,000, in relation to which no relief for double taxation will be claimed.
5. Dividends amounting to €110,000 from a 51% subsidiary company registered in an offshore jurisdiction outside the European Union (EU). This subsidiary company derives its income entirely from passive royalties and is not subject to any tax whatsoever. No relief for double taxation will be claimed in relation to this income.

Where applicable, CPTL will opt to apply the participation exemption.

CPTL operates from business premises which it owns in Malta, having a total floor surface area of 315 square metres.

CPTL will distribute all of its after tax profits for the year ended 31 December 2016 by way of dividend to CPHL. CPHL has been duly registered with the Commissioner for Revenue for the purposes of making claims for tax refunds.

Required:

In respect of Coffee Products Trading Limited, for the financial year ended 31 December 2016:

- **Identify the tax account to which each of its streams of chargeable income after tax will be allocated;**
- **Calculate the tax payable in Malta; and**
- **Calculate the income tax refund claimable by Coffee Products Holdings Limited.**

(10 marks)

4 **(a)** Mark Farrugia owns the following two properties situated in Malta, which he holds as rental investments:

(1) A residential apartment situated along the seafront of a popular town
(2) A commercial office space located in a busy industrial district

Mark leases these properties to tenants, invariably on a long-term basis. His rental income and related expenditure for the year ended 31 December 2016 in relation to these properties are as follows:

	Residential property €	**Commercial property** €
Rental income	19,200	33,600
Expenditure:		
Bank loan interest (note)	6,250	–
Repairs and maintenance	250	900
Cleaning expenses	400	1,200
Ground rent	50	–
MTA licence fee	120	–
Real estate agency fees	500	1,200
Sundry expenses	180	270
	7,750	3,570
Net income	11,450	30,030

Note: The bank loan interest represents interest incurred on a bank loan taken out by Mark to finance the purchase of the residential property investment and fitting it out prior to being let.

Mark's marginal rate of income tax is 35%.

Required:

Calculate the total tax payable by Mark in relation to his rental investment properties for the year of assessment 2017, using the most beneficial method of tax computation. (5 marks)

(b) Carrie Vella started a marketing consultancy business on a self-employed basis on 1 January 2016. She is a parent, based in Malta, and her sole source of income during 2016 consisted of this self-employment.

Her income net of deductible expenses from the business for the year ended 31 December 2016 amounted to €69,400.

Before Carrie started the marketing consultancy business, she had incurred the following pre-trading expenses specifically in relation to the business, which have not been taken into account in calculating the net income of €69,400:

Expense	**Date incurred**	€
Cost of online advertising campaign	1 April 2014	2,200
Cost of business feasibility study	1 April 2015	1,100
Cost of print advertising campaign	1 July 2015	2,700
Support staff member's salary	1 September 2015 to 31 December 2015	5,500
Cost of support staff member's training	15 September 2015	900
Business formation expenses	1 December 2015	450

No deduction has been claimed by Carrie in relation to the pre-trading expenses.

Prior to 2016, Carrie carried on a retail business, also on a self-employed business. This business had ended by 31 December 2015, and at that date Carrie had the following unutilised balances from the retail business:

Unabsorbed wear and tear allowances	€5,500
Unutilised trading tax losses	€14,200

Required:

Calculate Carrie's chargeable income and tax charge for the year of assessment 2017. (5 marks)

(10 marks)

5 Star Merchandise Limited (SML) is a trading company registered in Malta and incorporated, managed and controlled in Malta. SML wholly owns a Maltese subsidiary, Space Travel Limited (STL).

The income statement of SML for the financial and fiscal year ended 30 June 2016 is as follows:

	Note	€	€
Turnover			4,060,700
Cost of sales			(2,380,280)
Gross profit			1,680,420
Administrative expenses	1	(406,210)	
Distribution expenses		(119,350)	
Other operating expenses	2	(35,280)	
			(560,840)
Operating profit before finance costs			1,119,580
Finance income	3	45,200	
Finance expenses	4	(323,400)	
Net finance costs			(278,200)
Operating profit			841,380
Other income:			
Gross dividends received	5	70,000	
Rental income received	6	25,600	
			95,600
Profit before tax			936,980

Notes:

1. Administrative expenses include the following:

Expenditure on advertising	€900
Other promotional expenses	€5,600
Charitable donations paid	€1,200
Depreciation of plant and equipment	€43,500
Administrative penalty levied by the VAT Department in respect of the late filing of SML's value added tax (VAT) returns	€250
Interest charged by the VAT Department on the late payment of VAT	€350
Unrealised currency exchange losses	€3,100
Bad debts written off during the year	€900
Specific allowance in respect of a potentially irrecoverable debt	€8,000
General allowance for other irrecoverable debts (calculated at 1% of the other debtors)	€3,500
Lease charges paid in respect of a non-commercial motor vehicle with an official list price of €35,000	€12,000
Repairs and maintenance incurred on the commercial property which is rented out (see (6) below)	€1,400

2. Other operating expenses includes ground rent of €500 in relation to the commercial property which is rented out (see (6) below).

3. Finance income consists of local bank interest received on which tax was withheld at source in terms of the investment income provisions.

4. Finance expenses comprise:

Interest paid on a bank loan taken out to finance the purchase of the commercial property being rented out (see (6) below)	€1,300
Interest charges in respect of the company's bank overdraft facilities	€322,100
	€323,400

5. Gross dividends received comprise the following dividends received from other companies registered in Malta:

Dividends received out of the untaxed account of Space Travel Limited, a wholly owned subsidiary of SML	€15,000
Dividends received from Circuit Limited out of profits taxed at 35% which were allocated to its immovable property account	€24,000
Dividends received from Dalefe Ltd out of tax exempt profits which remain exempt in the hands of the shareholder	€31,000
	€70,000

6. The rental income was received during the year in respect of a commercial property which SML owns and rents out to an independent third party. SML does not own any other immovable property. The directors of SML have resolved to exclude the application of the new final tax regime on rental income for the current year.

Additional information:

(i) For the purposes of calculating the claim for wear and tear allowances for the year, the following information relates to the fixed assets of SML, eligible for allowances as at 30 June 2016:

	Historic cost	Net book value	Tax written down value
Lift	€60,000	€45,000	€42,000
Furniture and fittings	€40,000	€30,000	€32,000
Computer software	€12,000	€9,000	€6,000

(ii) SML's subsidiary, Space Travel Limited (STL), incurred losses during the financial year ended 30 June 2016. STL's tax computation showed a trading loss for tax purposes for the year amounting to €4,000, and unabsorbed capital allowances for the year amounting to €7,500. The directors of SML would like to avail themselves of any tax benefits which SML may derive from any possible transfers of the losses suffered by STL. SML would not pay any consideration in relation to the transfer of such losses.

Required:

Prepare the computation of chargeable income of Star Merchandise Limited for the year of assessment 2017.

Notes:
1 You should commence your computation with the profit before tax figure and include all of the items referred to in notes (1) to (6), indicating by the use of zero (0) any items for which no adjustment is required.
2 You are NOT required to calculate the tax charge for the year.

(15 marks)

6 Dana and Julia are two individuals who were born and raised outside Malta. They moved to Malta together during 2014 to take up residence in Malta for a few years. During 2015, Dana and Julia formally registered their relationship as a civil union under the applicable Maltese law. They live together in a traditional house of character which they rented for €1,500 per month on moving to Malta.

Dana is an experienced graphic designer and is employed on a full-time basis with a leading digital games producer in Malta. Her remuneration package for the year ended 31 December 2016 consisted of the following:

(1) A basic gross salary of €55,000 per annum.

(2) The use of a brand new company car valued at €35,000. Fuel, maintenance and all other vehicle-related costs are covered by her employer.

(3) A housing allowance of €700 per month, which Dana used to contribute towards the cost of the couple's monthly rent.

(4) A business mobile phone contract costing €85 per month and an internet subscription for business purposes costing €30 per month, both paid for by her employer.

Dana did not have any other income in the year 2016.

Julia does not have a full-time occupation in Malta; however, she does hold the position of non-executive director of a local private educational services company, Edu Limited (EL), for which she receives an annual director's fee of €12,000. EL also provides Julia with an insurance policy costing €600 per annum (paid by EL) which provides director indemnity cover against any potential liability which may arise from her office.

In addition to the above, Julia received the following income and gains during 2016:

(i) Interest of €450 on a savings deposit account which she has with a UK bank. No foreign tax was suffered on this interest income. The interest was credited to the same savings deposit account, and was not remitted to Malta.

(ii) Interest of €1,100 on the maturity of a fixed-term deposit of €35,000 which she held with a Swiss bank. No foreign tax was suffered on this interest income. The full amount of €36,100 representing the principal and interest was transferred to Julia's bank account in Malta.

(iii) Gross royalty income of €5,200 which she received from a UK publisher arising from sales of a book which Julia had written and published. The full royalty was remitted to Malta after deduction of foreign withholding tax at the rate of 15%.

(iv) A capital gain of €500 arising on the sale of a holding of 5% preference shares which she held in a Maltese private limited liability company.

During the year, Julia also transferred the sum of €20,000, originally received from a recent inheritance, from her current account with a UK bank to a new savings deposit account with a Maltese bank. On 31 December 2016, Julia was credited with gross interest of €200 in respect of this deposit, from which the bank withheld tax at source in terms of the investment income provisions.

Dana is designated as the responsible spouse for tax purposes.

Required:

(a) State, giving reasons, whether Dana and Julia will be considered to be ordinarily resident and/or domiciled in Malta for tax purposes during the year of assessment 2017. (3 marks)

(b) Calculate the total chargeable income of Dana and Julia for the year of assessment 2017.

Note: You should list all of the items of income and gains referred to in the question, indicating by the use of zero (0) any items which are exempt from tax or not taxable in Malta. (9 marks)

(c) Calculate the total tax payable by Dana and Julia for the year of assessment 2017, giving a brief explanation of the method used. (3 marks)

(15 marks)

End of Question Paper