Fundamentals Level – Skills Module

Taxation (Malta)

Tuesday 4 June 2013

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 3–5.

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.

Paper F6 (MLA)

The Association of Chartered Certified Accountants

The Malta Institute of Accountants

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The question paper begins on page 3.

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 2013 are to be used in answering the questions.

Individual income tax rates

Resident individual tax rates

Married couples – joint computation

€	€	Rate
0	to 11,900	0%
11,901	to 21,200	15%
21,201	to 28,700	25%
28,701 and over		35%

Other individuals

€	€	Rate
0	to 8,500	0%
8,501	to 14,500	15%
14,501	to 19,500	25%
19,501 and over		35%

Parent maintaining a child/paying maintenance

€	€	Rate
0	to 9,300	0%
9,301	to 15,800	15%
15,801	to 22,300	25%
22,301 and over		35%

Non-resident individuals

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

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 by the Malta Tourism Authority	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	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

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	791·02
1997	567·95	2012	810·16

Fringe benefit rates on cars

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%

ALL FIVE questions are compulsory and MUST be attempted

1 (a) Peter was born to Maltese parents in 1973. He does not own a house in Malta and his principal home worldwide is his parents' house in Valletta. Peter is an airline pilot and is employed full-time with Arab Aviations Limited ('AAL'), an airline company which is resident in the United Arab Emirates. Peter's job designation in his contract of employment provides that he must serve as first officer on long-haul flights from Dubai to Beijing. Any stand-by time must be spent in Dubai. Peter rents an apartment in Dubai and spends around 320 days per annum outside Malta but spends the rest of his time in Malta because he always returns to Malta for his holidays.

Before he became a pilot, Peter was an estate agent and he has remained in touch with the property business. In Malta, he has a good contact with a small local airline company and finds rental properties for its employees. He is also very close to a Maltese property developer, for which he acts as broker. Peter owns a number of flats in Malta which he rents to tourists (short lets of fully furnished holiday accommodation).

Peter is also a self-employed flying instructor, spending some of his time teaching people to fly light aircraft, which he hires for the purpose from local airfields. He is also a shareholder in Taghna Limited, a company incorporated in Malta which produces plastics.

In the basis year 2012 Peter received the following gains and profits:

1. A salary of €150,000 from AAL. Peter's contract of employment provides that AAL must pay the rent of Peter's apartment in Dubai of €20,000 per annum, and all water and electricity bills amounting to €2,500 per annum. AAL provides Peter with free meals on all flights at a cost of €1,000 per annum. AAL also pays for Peter's aircraft type rating exams (qualification exams for pilots) at a cost of €2,500 per annum, and provides Peter with four uniforms per year at cost of €200 each. Peter keeps all payments received from AAL in his bank account in Dubai.

2. A brokerage fee of €15,000 earned by Peter in connection with the transfer of two apartments in Malta. The brokerage fee was received in cash and was not recorded in the deed of transfer. Peter incurred the following expenses in connection with the brokerage fee:

	€
Telephone costs (Malta/Dubai)	300
Promotional expenses	300
Business related travel	1,500
Service fee (note)	1,000

Note: When Peter received the brokerage fee, he made a gift to his sister Maria of €1,000 for showing the apartments to his clients.

3. The following is an extract from Peter's profit and loss account from his rental business:

	€
Rents received	15,000
Less	
Emphyteusis paid	(500)
Water and electricity bills (not reimbursed by clients)	(2,500)
Fees paid to a cleaner	(700)
Cost of furniture	(5,000)
Interest paid on a loan used to refurbish the premises	(5,000)
Profit	1,300

For the purposes of his rental activity, Peter does not engage any employees, and is registered for value added tax (VAT), so VAT is not a cost to him. All the expenses above are stated exclusive of VAT.

4. The following is an extract from Peter's profit and loss account from his business as a flying instructor:

	€
Fees received	5,000
Hire of light aircraft, including fuel	(6,000)
Insurance	(1,000)
Loss	(2,000)

5. Peter received a dividend of €50,000 from Taghna Limited. 50% of the dividend was received from Taghna Limited's final tax account and the remaining 50% from Taghna Limited's untaxed account.

In 2012, Peter incurred the following expenditure:

	€
Financial assistance for the maintenance of his son from a relationship with a non-Maltese resident air hostess	6,000
Fees paid in respect of his grandmother's home for the elderly	4,000

Required:

(i) In relation to each of Peter's sources of income, state the basis on which it will be taxed and calculate the income (if any) chargeable to tax for the year of assessment 2013;

Note: You should list all of the items of gains and profits referred to in the question, indicating by the use of '0' any items which are not chargeable to tax. (18 marks)

(ii) Calculate the total tax payable by Peter on submission of his tax return for the year of assessment 2013. (4 marks)

(b) Mr Vella is an individual whose tax status has been determined as that of a person who is both ordinarily resident and domiciled in Malta. He used to work with the Government of Malta but retired four years ago. Since 2010 he has provided services as a night watchman on a freelance basis.

In 2012 Mr Vella received income as follows:

Pension of €10,000 inclusive of all bonuses
Local bank interest (gross) of €300
Fees for services as a night watchman of €3,000

Required:

(i) State, giving reasons, what returns Mr Vella must file with the Inland Revenue Department. (1 mark)

(ii) Calculate Mr Vella's total tax charge for the year of assessment 2013. (3 marks)

(c) Patricia is married to Hugh, an employee of the Government of Malta. Her tax status has been determined as being that of a person who is both ordinarily resident and domiciled in Malta. Patricia is a housewife but trained as a seamstress and in her spare time sews made-to-measure children's clothes. For the year of assessment 2013, Patricia's chargeable income from her sewing business is €13,700.

Required:

Explain the options available to Patricia for the taxation of her business income in the year of assessment 2013 and advise her on the most tax efficient method(s) available to her. Support your advice with a calculation of the tax payable. (4 marks)

(30 marks)

2 **(a)** National Company Limited (NCL) is a company incorporated in Malta whose objects are to hold a range of passive investments worldwide. NCL is a family company and the shareholders of NCL are five individuals who are neither ordinarily resident nor domiciled in Malta.

NCL had the following sources of income in the year to 31 December 2012:

Dividend income

(1) A dividend of €50,000 paid from the final tax account of Maltija 1 Limited, a company registered in Malta.

(2) A dividend of €150,000 paid from the untaxed account of Maltija 2 Limited, a company registered in Malta.

(3) A dividend of €50,000 paid from the foreign income account of Maltija 3 Limited, a company registered in Malta.

(4) A dividend of €30,000 paid from the Maltese taxed account of Malta Listed 1 Limited, a company which is listed on the Malta Stock Exchange.

(5) A dividend of €200,000 (net of tax at source at 30%) distributed by Swedish AB Limited (Swedish AB), a partnership *en commandite* registered in Sweden. The share capital of Swedish AB is divided into shares and NCL's shares in Swedish AB entitle NCL to vote, to profits available for distribution and the right to assets available on a winding up of the company. NCL's shares in Swedish AB have a total value of €600,000, representing 50% of the share capital of Swedish AB.

(6) A dividend of €330,000 distributed by Hungary KFT, a limited liability company registered in Hungary. NCL's shares in Hungary KFT entitle NCL to vote and to profits available for distribution, but not the right to assets available on a winding up of the company. NCL holds 90% of the shares in Hungary KFT. The profits of Hungary KFT consist entirely of passive interest and royalties. The dividend distributed by Hungary KFT was not subject to withholding tax in Hungary.

(7) A dividend of €5,000 distributed by Letterbox Corporation, a limited liability company registered in the Cayman Islands. NCL's shares in Letterbox Corporation entitle NCL to vote, to profits available for distribution and the right to assets available on a winding up of the company. NCL holds 100% of the shares in Letterbox Corporation. The profits of Letterbox Corporation consist entirely of passive royalties. The dividend distributed by Letterbox Corporation was not subject to withholding tax in the Cayman Islands. In the Cayman Islands, Letterbox Corporation is a tax exempt company.

All the above dividend income was received in NCL's bank account in Malta.

Interest income

(8) Interest paid by a Maltese bank of €600 net of withholding tax.

(9) Interest paid by a Maltese bank of €330 received gross (without any withholding of tax at source).

(10) Interest paid by Letterbox Corporation of €150,000. In the Cayman Islands, tax was not withheld on the interest payment.

(11) Interest paid on capital held with a Swiss bank of €150,000. In Switzerland the interest was tax exempt.

All the above interest income was received in NCL's bank account in the Cayman Islands.

Expenditure

In the course of the year, NCL incurred the following expenses:

	€
Rent paid in respect of its offices in Malta	12,000
Salaries and wages	50,000
Legal fees related to the acquisition of the shares in Letterbox Corporation	1,000
Fees in respect of a feasibility study relating to the acquisition of new shares	2,000
Interest paid upon money borrowed to acquire the shares in Letterbox Corporation	10,000
Recurring accountancy fees	5,000

NCL uses the flat rate foreign tax credit (FRFTC) and any other reliefs and exemptions available to reduce its Malta tax liability.

Required:

(i) Allocate National Company Limited's profit chargeable to tax to the relevant tax accounts (including the untaxed account) and calculate its tax payable for the year of assessment 2013; (16 marks)

(ii) Calculate the total tax refund available to its shareholders if the National Company Limited distributed all of its available profits (as calculated in (i) above).

Note: You should assume that there will not be any distribution from the untaxed account. (3 marks)

(b) Evasions Limited was incorporated in Malta in 2010. A new director has just been appointed to the board of directors. When filing the company's tax return in respect of the year ended 30 September 2011, he has discovered that the board had taken a conscious decision to omit to declare foreign source interest amounting to €20,000. The new director wants to rectify this shortcoming.

Required:

(i) Explain the consequences of Evasions Limited's failure to declare the interest income and what the company should do to rectify the omission; (4 marks)

(ii) Calculate the additional tax and interest payable by Evasions Limited if it corrects the omission and pays the outstanding amount on 30 June 2013. (2 marks)

(25 marks)

3 **(a)** Paul is single and both resident and domiciled in Malta. In 2012 Paul retired and disposed of his business interests to Mr Ogden, who is neither resident nor domiciled in Malta, as follows:

(1) The disposal of the plant and machinery held at his factory in Marsa. Paul had claimed capital allowances on all of the plant and machinery transferred. Details of the assets disposed of are as follows:

Description of asset	Year of acquisition	Original cost	Disposal proceeds
		€	€
Computers and electronic equipment	2006	10,000	1,000
Commercial motor vehicles	2005	150,000	20,000
Non-commercial motor vehicle	2004	18,000	3,000
Furniture and fittings (antiques)	2007	15,000	25,000
Air-conditioners	2010	10,000	4,000

(2) The disposal of his factory in Marsa. Paul had bought the factory in 1990 at a consideration of €120,000. He had availed himself of the initial allowance and wear and tear allowances on the factory. In 2006, he refurbished the factory at a cost of another €70,000 and claimed capital allowances on the expenditure. The factory was sold at a consideration of €400,000.

(3) The disposal of the shares he holds in Properties Limited, a company registered in Bermuda which owns a number of developments in Malta and which was incorporated in 1998. Paul acquired all of the shares in Properties Limited upon its incorporation. A summary of Properties Limited's balance sheet as at 31 December 2012 is as follows:

	€
Fixed assets – plant and equipment	520,000
Fixed assets – immovable property (at market value)	530,000
Current assets	200,000
	1,250,000
Current liabilities	(250,000)
Long-term borrowings	(500,000)
	500,000
Share capital (shares of €1)	200,000
Reserves	300,000
	500,000

Other information:

Aggregate profits for the five years, 2008 to 2012 inclusive	€285,000
Total consideration on sale	€600,000
Cost of property (acquired upon incorporation)	€55,000

(4) The disposal of the shares he holds in Intangibles Limited, a company registered in Malta which owns a business and which was incorporated in 2009. Intangibles Limited is not a property company as defined in the Income Tax Act. Paul acquired all of the shares in Intangibles Limited upon incorporation. A summary of Intangibles Limited's balance sheet as at 31 December 2012 is as follows:

	€
Intangible assets	124,000
Other assets	56,000
	180,000
Current liabilities	(30,000)
Borrowings	(20,000)
	130,000
Share capital (shares of €1)	95,000
Reserves	35,000
	130,000

Other information:

Profit/(loss) before tax:

	€
2009	(20,000)
2010	(8,000)
2011	12,754
2012	23,000
Total consideration on sale	€150,000

Paul's other taxable income in the basis year 2012 exceeded €20,000.

Required:

Calculate the total tax payable by Paul in year of assessment 2013 as a result of disposals in (1) to (4) above. In relation to disposals (2), (3) and (4), briefly explain the basis for your calculations. (16 marks)

(b) Christopher is a single individual who is resident but not domiciled in Malta. For tax treaty purposes, he is considered to be a resident of the UK. Malta has a tax treaty with the UK which provides for the elimination of double taxation on capital disposals.

Christopher disposed of the following assets in the year 2012:

1. 5,000 shares in Britain Limited for €35,000. Britain Limited is incorporated in England & Wales with a share capital of 10,000 shares of €1 each, is not quoted on any stock exchange and is not a property company as defined in the Income Tax Act. Christopher became a shareholder in the company upon incorporation. The net asset value of Britain Limited as at 31 December 2011 was €150,000 and the company's two years' average profits for the five financial years immediately preceding the year in which the sale was made is €50,000.
2. His flat in the UK. Christopher had occupied the flat as his sole ordinary residence since 2010. He had bought the flat in 2010 for €290,000 and sold it in 2012 for €320,000.
3. 1,000 shares in Offshore Limited for €35,000. Offshore Limited is incorporated in Malta with a share capital of 1,000 shares of €1 each, is not quoted on any stock exchange and is not a property company as defined in the Income Tax Act. Christopher became a shareholder in the company upon incorporation. The net asset value of Offshore Limited as at 31 December 2011 was €50,000 and the company's two years' average profits for the five financial years immediately preceding the year in which the sale was made is €32,000.
4. An apartment in Malta. Christopher used to rent out this apartment to tourists. Christopher had bought the apartment in 1999 for €50,000 and sold it for €150,000.

Required:

Calculate the Malta tax payable by Christopher as a result of the disposals above, taking advantage of any exemptions and/or reliefs available. Clearly identify, and give the reason for, any transaction which is exempt from tax or on which no tax is payable. (4 marks)

(20 marks)

4 (a) State the rate of value added tax (VAT) applicable to each of the following supplies made by a Maltese taxable person:

(i) The supply of accountancy services to a non-taxable person established outside the European Union (EU).
(ii) The supply of an insurance policy to a taxable person established in Malta.
(iii) The supply of takeaway foods by a supermarket to non-taxable persons in Malta.
(iv) The supply of textiles to a retailer established outside of the EU.
(v) The supply of items of jewellery (golden bracelets) to non-taxable persons resident in Malta.
(vi) The supply of legal services to a taxable person who has a fixed establishment in Malta. (3 marks)

(b) Books Limited is registered for value added tax (VAT) and acts both as a retailer and a wholesaler. The company had the following transactions for the quarter ended 30 September 2012. All amounts (sales and expenses) are stated excluding any applicable VAT.

Sales

1. Received €100,000 from the sale of textbooks to students who are non-taxable persons.
2. Received €30,000 from the sale of stationery to non-taxable persons.
3. Received €1,000 from the sale of opera tickets to individuals who are non-taxable persons.
4. Received €20,000 from the sale of batteries to retailers who are taxable persons.
5. Received €15,000 from the sale of paper to retailers who are taxable persons.

Expenses

	€
Electricity	1,800
Petrol for a commercial vehicle used for the carriage of goods	1,200
Purchase of shelving	5,000
Salaries and wages	10,000
Total	18,000

Required:

Calculate the amount of value added tax (VAT) payable by Books Limited for the quarter ended 30 September 2012. List all of the items referred to in the question, clearly identifying any which are exempt from VAT and/or for which no credit is available. (9 marks)

(c) Tuffieha Limited has received a provisional assessment dated 1 June 2013 from the Commissioner of VAT on the grounds that the company's VAT return for its quarter ended 31 March 2013 was incorrect.

Required:

(i) Assuming that Tuffieha Limited wishes to contest the provisional assessment, state what action it should take, together with the time limit; (2 marks)

(ii) Assuming that Tuffieha Limited does nothing, state the further action the Commissioner will take, together with the time limit. (1 mark)

(15 marks)

5 **(a)** Infrastructures is a partnership *en nom collectif* established in Malta in 2011, which began to trade in 2012. The income of Infrastructures consists in the letting of a cable infrastructure. It only has one client, a company which is a telecoms operator. Summaries of Infrastructures' profit and loss accounts for the years 2011 and 2012 are as follows:

2011

	€	€
Turnover		0
Less: overheads		
Depreciation	(225,000)	
Expenses incurred on trench works	(200,000)	
Geological study	(20,000)	
Feasibility study	(30,000)	
Consultancy fees (architects)	(10,000)	
Consultancy fees (lawyers)	(5,000)	
		(490,000)
Loss		(490,000)

2012

	€	€
Turnover		500,000
Less: overheads		
Depreciation	(225,000)	
Expenses incurred on trench works	(25,000)	
Consultancy fees (architects)	(3,000)	
Consultancy fees (lawyers)	(500)	
		(253,500)
Profit		246,500

The depreciation charges for 2011 and 2012 were arrived at by depreciating the cost of the assets using the straight-line method over their economic life. All assets were acquired in 2011.

Asset	Cost	Estimated economic life	Annual depreciation charge
	€	No. of years	€
Communication equipment	100,000	4	25,000
Cable	1,000,000	5	200,000

Required:

Calculate Infrastructure's profit chargeable to tax for the year of assessment 2013. (5 marks)

(b) Internazzjonali Limited is a company incorporated in Malta. Internazzjonali Limited has established fixed places of business (branches) in France and Italy, two jurisdictions which have signed tax treaties with Malta which provide for relief from double taxation on corporate profits using the credit method.

In 2012, the profits attributable to the Italian fixed place of business amounted to €30,000 (net of Italian tax at the rate of 27·5%), and the profits attributable to the French fixed place of business amounted to €5,000 (net of French tax at the rate of 33·5%). Internazzjonali Limited did not derive any Malta source income in 2012.

Required:

Calculate Internazzjonali Limited's profits chargeable to tax and tax payable for the year of assessment 2013. (5 marks)

(10 marks)

End of Question Paper