

# Examiner's report

## F6 Taxation (CZE)

### June 2016

#### General Comments

There were two sections to the examination paper and all of the questions were compulsory. Section A consisted of 15 multiple choice questions (two marks each) which covered a broad range of syllabus topics. Section B had four questions worth 10 marks each and two longer questions worth 15 marks, each testing the candidates' understanding and application of Czech taxation system in more depth. The following paragraphs report on each section and focus on some of the key learning points.

#### Specific Comments

##### Section A

It was very pleasing to see that almost all candidates attempted all of the questions. Candidates preparing for the next examination of F6 are advised to work through the specimen exam and sample questions discussed here and to carefully review how each of the correct answers were derived. Section A questions aim to provide a broad coverage of the syllabus, and future candidates should aim to revise all areas of the F6 syllabus, rather than attempting to question spot. The following two questions are reviewed with the aim of giving future candidates an indication of the types of questions asked, guidance on dealing with exam questions and to provide a technical debrief on the topics covered by the specific questions selected.

#### Sample Questions for Discussion

##### Example 1

Hynek had the following income in 2015:

- (1) Rental income from the lease of a computer to a neighbour from 1 March to 25 March of CZK 1,000.
- (2) Proceeds of CZK 120,000 from the sale of the copyright to a film he inherited from his father.
- (3) A settlement amount of CZK 500,000 after he terminated his participation in MOTO, s.r.o. He had acquired his share in MOTO, s.r.o. in 2001 for CZK 350,000.
- (4) Proceeds in December 2015 from the sale of a car he used for private purposes of CZK 230,000. He had acquired the car in February 2015 for CZK 260,000.

**What is the partial tax base from other income (§10) to be included in Hynek's tax return for 2015?**

- A 120,000 CZK
- B 270,000 CZK.
- C 151,000 CZK.
- D 90,000 CZK.

This question tested candidates' knowledge regarding how the partial tax base from other income of an individual taxpayer is computed. There are certain thresholds for occasional lease and occasional activity, there are also limits for exemption of proceeds from sale of certain movable property and at the same time certain rules for treatment of loss from the sale of private property.

The correct answer was A. Only proceeds from the sale of the copyright should be included in the partial tax base. Rental of computer was exempt as it met the threshold of 30 thousand per year for exemption of occasional lease and occasional activity. The settlement amount is not included in the partial tax base as it had been already taxed by withholding tax. The gain from sale of the car would be taxable since the car was sold after less than a year, however the result from the transaction was a loss. This loss cannot be offset against other income in the partial tax base.

### **Example 2**

**Which of the following accounting expenses are tax deductible for a company in the tax year 2015?**

- (1) A commercial penalty accounted for in 2015 and paid on 21 January 2016 to a supplier for late payment
- (2) The tax residual value of a computer donated to a school
- (3) Marketing expenses for an advertisement in a journal
- (4) Road tax for 2015 paid, with a delay, on 2 January 2016

- A 1 and 2 only
- B 3 and 4
- C 1 and 3
- D 1, 2 and 4

This question tested the tax deductibility of various accounting expenses for corporate tax purpose. Area of tax deductibility for corporations is an important part of the syllabus and requires good technical knowledge.

The correct answer was B. Commercial penalty is tax deductible when it is paid. Residual value of a donated asset is not tax deductible. However it can be “deductible” under gift credit.

## **Section B**

### **Question One**

This 10-mark three-part question was on various aspects of tax administration.

This question was not well answered. A significant number of candidates did not address some parts of this question at all. Some candidates did not show satisfactory knowledge of the formula for computation of penalties and interest. As mentioned in previous examiner’s reports questions on tax administration and management remain unpopular among candidates and performance was again disappointing. Future candidates are advised to pay more attention to knowledge on topics related to tax management and administration. The sanction system in tax administration has certain logical rules and once learned can be easily applied, thus allowing candidates to gain marks in questions on tax administration.

Part (a) for 3 marks was split into two sub-parts. The question was based on Karolina who had asked for an extension on the deadline to deliver certain information as requested by the tax authority. This requirement tested candidate’s knowledge of computation time limits in tax

administration and depended on a number of factors including; whether the tax authority replied negatively or positively, the extension requested by Karolina, when she filed her application and was the reply delivered to her. This was very poorly answered, many candidates did not show enough knowledge of this rule. The answer received from the tax authority was negative, five days were remaining from the deadline when she filed the application, and therefore, she only had these five days in which to deliver the requested information..

The second requirement required knowledge of situations when a taxpayer can appeal against the tax authority decision. In this particular case Karolina could not appeal against the negative decision for the extension of the deadline and the majority of candidates answered correctly.

Part (b) for 3 marks required candidates to judge a situation of Jiri who realised after filing a tax return that he had not included certain income in his tax base. The majority of candidates answered that the right remedy is to file an additional tax return. Unfortunately few of them stated a deadline as well. In the second part of the question candidates were required to calculate the default interest.

Performance was satisfactory in this part. It was pleasing to see that many candidates are aware of the “generous” time limit (generally 5 days) for which the tax administrator does not compute interest. Where candidates did not score full marks, this was mainly because they failed to know when the computation of the delay days starts.

Part (c) for 4 marks required candidates to calculate the penalty resulting from reassessment by the tax authority, stating deadlines for paying additional tax and the penalty and finally, stating conditions for remittance of the tax penalty.

Overall performance in this area was unsatisfactory. Many candidates are aware of the penalty in the amount of 20% from the outstanding amount, however few candidates knew the deadline (15<sup>th</sup> day from the delivery of the assessment) and even fewer knew the conditions for remittance of the penalty. This is a new instrument included in the law from 2015. The tax authority may remit up to 75% of the penalty amount under conditions that the tax arrears have been paid and if the penalty is higher than 3,000 the request has to be accompanied by an administration fee of CZK 1,000.

Future candidates should focus more on technical knowledge of computation of days in various situations in tax administration, on the precise knowledge of the formula for default interest and general knowledge of deadlines. It is also important to study instruments or elements that have been recently included in the Tax administration Act.

## **Question Two**

This 10-mark question was based on Katerina, an employee of KORTES, s.r.o. where she has a signed Declaration for personal tax credits. At the same time she receives remuneration as an executive manager from BYTY, s.r.o. The question tested monthly payroll calculations in a situation where there is a concurrence of two employment incomes in a month.

The question was answered very well by most candidates, and many were able to judge appropriately whether fringe benefits are taxable for Katerina or not. Candidates were required to judge vitamin package and vaccination, contribution to vacation and contribution to pension and life insurance provided by KORTES, s.r.o. and the provision of business car which is also for private purposes provided by BYTY, s.r.o. .Candidates were able to gain marks when stating exempt income, i.e. contribution to pension and life insurance – as this was within the annual limit, health

package and part of contribution to vacation (up to the limit of CZK 20,000). The scenario contained such figures that candidates should recognize that the solidarity surcharge had to be calculated in the situation of KORTES, s.r.o.. Many candidates gained marks for correctly rounding up the tax base to hundreds, and for correct inclusion of monthly personal tax allowances – basic one and for children only. The credit for the pre-school facility can be applied only on annual basis.

Many candidates presented their answers well. Again those that explained why certain figures are not included in the calculation, .e.g. exempt amounts, were able to gain full marks. A common mistake made by candidates was to combine the payroll computation for both companies together which practically is not possible as these were separate employers.

### **Question Three**

This 10-mark question was a question on value added tax (VAT). Performance on this question was satisfactory.

The question was based on a company Drevovyroba, s.r.o., a monthly VAT payer. Candidates were asked to prepare their January 2015 VAT return. The structure of the question was similar to previous years.

The question tested whether certain output supplies are taxable or exempt – in case of export or delivery in EU states. As regards input supplies the question focused on the application of the reverse charge mechanism, use of a business asset partly for business and partly for private purposes, advanced payment, purchase of gift items and use of advanced coefficient.

Common mistakes made by candidates was failing to compute the clearance of legal services correctly or applying the coefficient to situations where the payer can apply full input. Overall performance was very good.

Future candidates should pay attention to stating supplies that are exempt or not subject to VAT explicitly, in order to score full marks.

### **Question Four**

This 10-mark question examined transfer pricing and thin capitalisation rules based on Avera, s.r.o. which had three partners, one corporate and two individuals. Candidates were required to assess four situations in Avera's accounting books in the context of the above mentioned rules.

Overall the performance of this question was mixed. The majority of candidates' demonstrated awareness of the rules theoretically however were not able to apply the rule to the particular situations in the question.

Many candidates were able to correctly judge whether a loan/credit was from a related or non-related person. Candidates scored well for considering the transfer pricing rules. As regards thin capitalization rules future candidates should focus on good understanding of the computation of shareholder capital and the average daily amount of credits.

Future candidates should ensure that they carefully read the question scenario and ensure that they consider the layout used to present their answer to ensure that explanations provided are clear.

### Question Five

This 15-mark question was based around Pavel, an employee and also an independent consultant. His family situation was described to allow candidates to decide what personal credits shall be applied in his tax return. His situation was a little complicated as he married during 2015, lived with his new wife and her two children and their recently born daughter. In addition the situation of his new wife, Martina was described. Martina was on maternity leave but also had certain income from her own business. Candidates were required to judge what children credits were available and for which months Pavel can use them and further, whether after judging the amount of Martina's annual income if he can apply a spouse credit.

Performance on this question was satisfactory. Part (a) for 14 marks required candidates to prepare Pavel's 2015 income tax return and calculate the tax payable. Candidates showed good knowledge of setting partial tax bases for employment, business, rental and other income. Candidates managed to structure the whole income tax return correctly, using tax allowances that are to be subtracted from the tax base and tax credits to be subtracted from the tax liability. It is pleasing to see that candidates were able to determine whether to use actual expenses or lump-sum expenses for business or for rental income even in the situation when Pavel received his portion on Reality, v.o.s. tax base. However those who did not consider whether Pavel can at the same time use spouse and children credits scored less. Future candidates should focus more on the rules for using children credits, and on the rules when income from *Dohoda o provedeni prace* is or is not included in the tax base.

The layout and working calculations provided by some candidates were unclear and future candidates should pay attention to layout and providing explanations as to why they did not include certain income in the tax base, e.g. it was exempt or not subject to tax.

Part (b) for 1 mark required candidates to state the due date for filing Pavel's tax return. Performance on this requirement was very good.

### Question Six

This 15-mark question was based on ArchStudio, s.r.o., and tested candidates' knowledge of the corporate income tax (CIT) rules regarding determination of the income tax base. In comparison with previous years' structure of CIT questions, candidates are no longer required to prepare a profit/loss account from the information given in the question. The accounting profit is stated directly in the question itself. The question listed events which occurred in the corporation and tested candidates' knowledge of how to adjust the accounting issues in the tax return.

Part (a) for 13 marks required candidates to calculate the corporate income tax liability coming from the accounting profit set in the question. It tested candidates' ability to prepare the corporate income tax return, through adjusting the accounting profit to comply with the relevant tax legislation and using relevant tax allowances such as for gifts or education of students. Performance on this question was very good.

Many candidates were able to determine what adjustments had to be made to the accounting profit. The question focused on tax deductibility of employees benefits (theatre tickets, kindergarten expenses), treatment of accounting versus tax depreciation in various situations (sale, liquidation due to damage), treatment of certain expenses that are tax deductible only if they are paid or paid

on time (social security contributions, contractual penalty). As regards receivables many candidates showed awareness of the difference between rules used until the end of 2013 and rules applied from 2014.

The majority of candidates showed very good knowledge of various structural elements of the tax base and the structure of calculating the tax liability.

Where candidates did not tend to score as well was because of adding back the kindergarten expenses, or not computing education allowance, or not correctly computing the difference between accounting and tax residual value of the damaged car for which an insurance compensation was received by the company. Future candidates should explicitly mention any items where no adjustments are necessary through explanation, in order to gain full marks. Further they should focus on better layout and a more succinct way of presenting adjustment figures.

Part (b) for 2 marks required candidates to state the due date for filing tax return, stating who is responsible for its filing and what type of mailing channel is to be used.

This was quite a straightforward requirement. Performance on this question was very good. Many candidates were able to correctly state the due date which was 1 July 2016. Common mistakes by candidates were to state that Archstudio was responsible for filing to send it through its databox. The correct answer was that the tax advisor shall send it through its databox, or the Ministry of Finance web EPO. It is pleasing to see the candidates are aware of electronic filing liability.