

Examiner's report

F6 (POL) Taxation

December 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. All questions tested the candidates' understanding and application of the practical aspects of Polish taxation. 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 POL are advised to work through the pilot paper 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 POL 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

Which of the following are required to withhold personal income tax (PIT) when making payments to individuals?

- (1) An employer from an individual employed under labour contract
- (2) A bank on interest accrued
- (3) A notary public on the sale of an apartment
- (4) An entity from an individual contracting for personal services

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

This question tested the understanding of the PIT scope and a PIT remitter role in the Polish tax system.

Situation 1 referred to a labour contract where the employer is a PIT remitter. It was a standard example of a PIT remitter. Situation 2 mentioned accrued interest which is not the subject to taxation until is paid out thus there was no issue of remitting the tax (otherwise indeed done by the bank) as the tax point has not occurred. A notary public mentioned in the Situation 3 is a Polish CLAT (civil law activity tax) remitter but has no obligation to withhold PIT. This situation was properly excluded from the correct answer by the most candidates. Situation 4 described the contract for personal services when the contracting entity is a PIT remitter.

The correct answer was A, 1 and 4 only.

Example 2

Which of the following can conduct a tax inspection (audit) of taxpayer's settlements?

- (1) The head of the tax office

- (2) The head of the tax inspection office
 (3) The head of the local municipality

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

This question checked the understanding of tax authorities' responsibilities to test candidates' knowledge of the general organisation of the Polish tax system.

Most students knew that the head of tax office and the head of tax inspection office can conduct a tax inspection. However, in accordance to the Polish tax law, the head of the local municipality can also carry out the tax inspection for its relevant taxes. Therefore the correct answer was D - 1, 2 and 3.

Section B

Question One

This 10-mark question covered the topics of the personal income tax (PIT) and Social Security (ZUS) and Health Service Contributions (HSC) based on the Zenobi Miotła case.

The question required candidates to calculate the net (cash) salary which will be paid into Zenobi Miotła's bank account by Podomex SA for the month of October 2015.

Candidates' performance was very good on this question and many of them scored full marks.

Gross salary should be increased by the medical package (only 80% of the total package value as 20% related to labour law required services), meals, travel allowance (only beyond the allowed limit of 30 PLN per day) and hotel allowance (the amount spent less 30*150%*2 days) to arrive to the total emoluments - a ZUS base. The employee ZUS due from the Zenobi's emoluments was calculated at 13.71% rate. Total emoluments less the employee ZUS due were a HSC base. Then employee cost for one month of PLN 111 should be deducted to arrive to a tax base. PIT to be withheld for Zenobi for October 2015 was calculated at 18% rate less 46 PLN (one twelfth of tax free amount) less HSC at 7.75% from the HSC base. The last step was to calculate the net salary. Sometimes the net salary calculation was forgotten which cost some candidates marks. Net salary should be calculated as gross salary (without additional emoluments as they were not part of the salary) less the employee ZUS due, less HSC at 9% and PIT withheld.

Question Two

This 10-mark question required a calculation of Zadłuzona Sp. z o.o.'s taxable income for corporate income tax (CIT) purposes for 2015. Performance on this question was a little disappointing.

Taxable income of PLN 430,000 already calculated by Zadłuzona should be adjusted by four transactions:

1) interest allowed on the loan to shareholder - this part of the question tested thin capitalisation concept. Many students noticed that interest allowed is calculated as the equity:debt ratio x interest for 2015. However, only a few candidates properly calculated the ratio using the equity value as of 30 November 2015 (PLN 30,000) and debt value of 30 November 2015 (PLN 65,500 - loan principal and 11-month interest).

2) interest allowed on the bank loan - a bank loan was drawn on 1 January 2015 to finance the new production line. The production line was put into use on 31 July 2015 therefore interest for 7 months were capitalised on the production line value and should not be included in the CIT calculation. 9-month interest repayment took place on 30 September 2015 and it was the only interest repayment in 2015. Hence interest for 2 months (August and September) should be included in CIT calculation for 2015. Additional difficulty was to apply adequate PLN/EUR rate as the bank loan and interest was expressed in EUR. Interest to be included in CIT

should be calculated as the difference between interest paid at the PLN/EUR rate as of 30 September 2015 (4.4 PLN/EUR) and interest capitalised at the PLN/EUR rate as of 31 July 2015 (4.2 PLN/EUR).

3) forex on the loan repayment - this part of the question was relatively well answered. The forex to be included in CIT for 2015 should be calculated as the loan principal repaid of EUR 40,000 x the difference in forex rates between 1 January 2015 (drawing) and 31 December 2015 (repayment). The amount of the loan repayment itself is not an income or cost item therefore it should not be included in taxable income calculation.

4) fixed asset depreciation - some candidates calculated the depreciation rate properly as $14\% \times 5/12$ months x 2 (considering faster depreciation possibility). However only a few students calculated the initial value of the production line correctly as the production line construction cost of PLN 500,000 plus capitalised interest calculated before of PLN 24,500 and arrangement fee of EUR 1,000 times the forex rate as of 1 January 2015 (4.2 PLN/EUR).

Question Three

This 10-mark question required candidates to calculate the amounts of output VAT and input VAT which should have been included in Zdzisław Pacuła's VAT return for the fourth quarter of 2015. Zdzisław Pacuła was registered for VAT and was a "small VAT taxpayer". The question was answered well by the majority of candidates.

There were 10 transactions to be discussed, each worth 1 mark. Most candidates correctly calculated output VAT at 23% rate on transactions with Janiak (output VAT on prepayment received in October 2015), Kowalski, Kanapex (only for 20% instalment received), Maliniak and Oborniak (unpaid sales but overdue more than 180 days as of 31 December 2015 and Oborniak was not registered for VAT). Three sales transactions resulted with zero output and input VAT in the fourth quarter VAT calculation - transaction with Nowak (unpaid), Karolak (unpaid and 180 days fell in the third quarter) and Wiercinex (unpaid more than 180 days but Wiercinez was a VAT payer).

Payment for goods purchased on 6 October resulted with 23% input VAT and unpaid purchase of goods on 10 October did not generate input or output VAT.

It was pleasing to see that the majority of students indicated by the use of zero (0) all transactions for which VAT entry was not necessary. Candidates who did not use zero were not awarded credit.

Question Four

This 10-mark question covered the topic of CIT related to transactions with related parties.

Part (a) (i) for 3 marks asked for definition of the "related parties" term under the Polish CIT regulations. Performance on this part of the question was average.

Related parties are the parties with the common shareholder controlling directly or indirectly at least 5% of the shares in the entities. Many candidates mentioned common shareholder but quoted a higher percentage shareholding. Only some students described the definition further adding that related parties are also the entities managed directly or indirectly by the same persons or by persons with a family, employment and capital relationship to each other.

Part (a) (ii) for 1 mark required the statement of the circumstances in which transfer pricing documentation needed to be prepared for a transaction with a non-related entity. Candidates scored well on this question.

Transfer pricing documentation must be prepared in the case of transactions with non-related parties who are resident in countries creating harmful tax competition (tax havens)

Part (b) for 5 marks required candidates to list any five key issues required to be addressed in transfer pricing documentation. Performance on this question was average.

Candidates mentioned various issues in their answers but very few candidates gave all of the required points. Key issues are:

- the role of the parties to the transaction (including assets invested and risk taken)
- an estimation of all expected costs of the transition (including payment terms)
- the method of calculation of the profit and transaction price
- an indication of the economic strategy driving the transaction (if the transaction was driven by business strategy)
- an indication of other factors impacting the transaction value (if applicable)
- the expected benefits from the acquired services (in case of an acquisition of intangible services)

Some students mentioned that the transfer pricing documentation must include comparison to the market transactions and prove that the transaction was performed on the market conditions – it should be noted that under the rules examinable in December 2016, the benchmarking analysis were not a mandatory part of required transfer pricing documentation set. This however will change in future years.

Part (c) for 1 mark required candidates to state how the tax authorities will assess any additional taxable income arising from a non-arm's length transaction with a related party in case the company possesses the transfer pricing documentation and when it does not. Performance on this question was average.

If the transfer pricing documentation is present, any additional taxable income assessed will be taxed at the standard rate of 19%. If there is no transfer pricing documentation, at the penalty rate of 50%.

Question Five

This 15-mark question was based on Aktywna Sp. z o.o. (Aktywna) case and required to calculate the CIT payable by/refundable to Aktywna for 2015. The question was answered satisfactory.

Net income per accounts of PLN 1,137,000 should be adjusted by the following to arrive to the taxable income:

- 1) exclusion of dividend from Bulgaria in full (PLN 75,000) as Bulgaria is in the EU
- 2) inclusion of the US dividend gross up for withholding tax of PLN 4,444
- 3) elimination of the interest income accrued, refunded penalty interest, the EU grant and forex income on the year-end valuation of the cash deposit
- 4) application of the quickest depreciation method for 15 copiers of the initial total value of PLN 45,000 - withdrawing previously used method of depreciation ($45,000 \times 20\% \times 11/12$) and adding depreciation of PLN 45,000 (100% depreciation rate for low value fixed assets)
- 5) elimination of costs related to bad debts area: increase in the general provision for bad debts of PLN 38,000; loss on sale of deposit receivable of PLN 25,000
- 6) elimination of donation cost of PLN 70,000

The majority of candidates properly deducted from the taxable income the donation in the amount of the maximum 10% of taxable income and tax loss carried forward of PLN 350,000 (50% of the tax loss from 2013) to arrive to the tax base.

Then tax base should be taxed at 19%. The amount of tax to be payable/refundable was calculated as tax amount less tax credit for withholding tax on dividend from the US (PLN 4,444) and tax instalments paid. Some students experienced problems with calculating the tax instalments paid. They should be calculated based on 2012 tax base (there was a tax loss in 2013) adjusted by 12/7 (as Aktywna started its activity on 1 June 2012) times 19%.

Question Six

This 15-mark question was based on the Roman's case.

Part (a) for 13 marks required a calculation of Roman's PIT payable for 2015. Performance on this question was a little disappointing.

Not all students divided Roman's income into two groups: income from the personal service contract, renting a house and apartment, which should be taxed at normal PIT scale and income from the selling of the house, which should be taxed separately at 19% rate.

Although almost all candidates calculated the revenue from the personal services contract as 600 PLN x 12 months, many students forgot to deduct 20% of personal service cost. With respect to the taxable income from the house rental, it should be calculated as rent income less house depreciation, heating system depreciation and repairs. Utilities covered by a tenant were neutral for Roman's tax purposes. House depreciation should be calculated as house market value (PLN 500,000) plus the notary fee (PLN 4,000) related to inheritance procedure x 1.5% x 11/12 months. Heating system depreciation should be calculated as its initial value of PLN 36,000 x 1.5% x 9/12 months.

Taxable income from the apartment rent should be calculated as rent less depreciation, mortgage interest and utilities. Insurance payment is exempt from tax. Depreciation should be calculated as 1.5% of the apartment initial value (PLN 400,000 of the apartment purchase value plus fittings of PLN 50,000).

Only a few students calculated the taxable income from the sale of the house properly as sale price of PLN 600,000 less acquisition cost of PLN 40,000 (notary cost and heating system improvement) less depreciation of house and the heating system as calculated before less PLN 540,000 which was reinvested for housing purposes.

Although some students wrote in the answer for question 6 (b) that Roman did not need to pay ZUS, they calculated ZUS in question 6 (a). Also some candidates calculated HSC in the question 6 (a) which was not required. There were no marks gained (nor lost) for ZUS and HSC calculation in the question 6 (a).

Part (b) for 2 marks required the statement, giving reasons, whether Roman will be required to pay ZUS in relation to his activities. Performance on this question was good. Most candidates pointed out that Roman is not obliged to register and pay ZUS on his income from the personal services as he is a student under 26 years old. Additionally Roman did not need to pay ZUS in respect to his rental income as renting of houses and apartments does not automatically constitute an individual business activity.