

Examiner's report

F6 Taxation (POL)

June 2015

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 candidates' understanding and application of Polish taxes in more depth. The key to passing the exam was proper time allocation between Section A and Section B. A number of candidates performed very well in Section A but appeared to spend too much time on it as certain questions from Section B were unsatisfactorily answered. This is the first examiner's report since the introduction of the new exam format and question types. The following paragraphs report on each section and focus on the selected 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 June 2015 paper and sample questions discussed here as well as the specimen questions 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

Company A sold a product in October 2014 but, in error, did not account for any tax on the sale.

On which date(s) will the value added tax (VAT) and corporate income tax (CIT) liabilities related to this sale expire?

- A 1 November 2019 for both VAT and CIT
- B 1 January 2020 for both VAT and CIT
- C 1 January 2020 for VAT and 1 January 2021 for CIT
- D 1 November 2019 for VAT and 1 January 2021 for CIT

This question tested candidates' understanding of the tax liability expiration period for companies which in Poland is 5 years. This rule means that companies are not responsible for outstanding tax liabilities for an indefinite period by limiting a company's potential tax risks related to past periods to 5 years only. Tax authorities are not able to start new tax audits, check tax calculations and documentation and impose additional tax charges after the expiration period. Such a mechanism also avoids companies being required to retain tax documentation and records indefinitely.

The key to be successful in this question was to know how the expiry period of 5 years was calculated both for value added tax (VAT) liabilities and corporate income tax (CIT) liabilities. The expiry period starts from the end of the year when the tax liability arises and lasts for the next 5 full calendar years.

Therefore, in the case of VAT, the tax liability arises on 25th of the month after the invoice date. The invoice mentioned in the question was dated October 2014 and therefore the VAT liability was due on 25 November 2014. Five full calendar years after 2014 are: 2015, 2016, 2017, 2018 and 2019 and, therefore, the VAT liability expired on 1 January 2020.

In the case of CIT, the ultimate tax liability related to the sales invoice from October 2014 arises on 31 March 2015 – being the deadline for the CIT return for 2014. Five full calendar years after 2015 are 2016, 2017, 2018, 2019 and 2020 therefore the CIT liability will expire on 1 January 2021. The correct answer was, therefore, option C. Some candidates incorrectly assumed that the CIT liability arises on the date of the CIT advance payment which in this question was due on 20 November 2014 and so selected option B.

Example 2

The Polish tax system allows taxpayers to apply for an individual tax ruling from the tax authorities on the tax implications of a given transaction.

Which of the following statement(s) referring to individual tax rulings is/are TRUE?

- (1) The taxpayer is legally bound to follow the ruling
- (2) The tax authorities are legally bound to follow the ruling
- (3) The tax ruling once issued cannot be changed
- (4) Once issued and published, tax rulings are binding for other tax authorities and taxpayers if the case is identical to that addressed in the ruling

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

This question tested candidates' knowledge of the individual tax ruling procedure in Poland. Individual tax rulings are useful when dealing with more complicated tax issues. The taxpayer can describe the tax issue and proposed interpretation based on the Polish tax law in relation to this particular tax issue and send this to the tax authorities for confirmation.

Statement 1 was incorrect as the taxpayer may follow the ruling but does not have to, as they are not legally bound by the ruling. Statement 2 was correct - the tax authorities **are** legally bound to follow the ruling. Statement 3 was incorrect as the tax ruling can be changed. Statement 4 was incorrect as the individual tax ruling only applies to the given issue of the given taxpayer.

Therefore, the correct option was D – 2 only. A number of candidates incorrectly selected option B as they mistakenly thought that the taxpayer was also bound by the ruling.

Section B

Question One

This 10-mark question covered the topic of the tax treatment of non-current assets held under a lease and was based on the case of Franciszek who runs a registered business activity.

Part (a) for 2 marks required candidates to explain briefly the difference between an operating lease and

a finance lease with respect to the tax deductible costs which can be claimed by the lessee. The majority of candidates appeared confident in answering this requirement and were aware of the difference in the tax deductible costs under the two types of lease. However, a few candidates explained general and/or accounting differences between those two types of lease rather than focussing their answer on the tax deductible costs as required by the question.

Part (b) for 3 marks required candidates to calculate the amount of Franciszek's tax deductible costs in respect of the finance lease contract for the year 2014. Candidates performed fairly well on this part of the question. The tax deductible costs consisted of finance costs and depreciation costs applicable to 2014. The total finance costs under the finance lease contract were calculated as the difference between the total charges payable by Franciszek and the equipment value. Once the total finance costs were calculated, those applicable to 2014 then had to be identified. The annual tax deductible depreciation cost was calculated as the equipment value multiplied by the 30% depreciation rate multiplied by a factor of 2 (as the relevant assets quickly become technically obsolete). This then had to be restricted to five months of 2014, as the finance lease contract was signed on 1 July 2014 so the first depreciation charge was accounted for in August 2014.

Part (c) for 5 marks required candidates to explain why setting the buy-out price at 1 PLN under the operating lease contract would create a personal income tax (PIT) problem for the lessor and to calculate the minimum buy-out price needed to avoid such a problem. Candidates' performance was less satisfactory on this part of the question.

The PIT Act provides a restriction on the level at which the buy-out price may be set. The lowest buy-out price level is called the net hypothetical value (NHV) and is calculated using reducing balance depreciation for the asset with a factor of 3. If the buy-out price is set at a lower level than NHV, the lessor has to account for additional deemed taxable income equal to the difference between the buy-out price set and the market value of the equipment at the buy-out date.

Only some of candidates were familiar with the NHV concept and were able to apply this to the scenario in the question.

Question Two

This 10-mark question was designed to test candidates' knowledge of value added tax (VAT) and was based on transactions recorded in a company, Efekt Jo-jo Sp. z o.o. (Jo-jo).

Part (a) for 7 marks required a calculation of the VAT payable/deductible by Jo-jo for March 2014. This part of the question was answered well by the majority of candidates. It was pleasing to see neat layouts of the majority answers as well as clear statements '0' or 'exempt' where needed to indicate no VAT impact.

The majority of candidates noted that the amounts given in the question were generally stated gross (i.e. VAT inclusive) and therefore knew that, to arrive at the relevant VAT amount, they needed to multiply the amount by the fraction $\frac{23}{123}$. In the case of the product display services in the

pharmacies and the purchase of the industrial mixer, input VAT was calculated as the gross amount multiplied by the fraction $\times 23/123$ and then by 75%. This was to take account of the ratio of VATable supplies to total supplies for the year ended 31 December 2013 for these mixed supply purchases. Exported food supplements were subject to 0% VAT. Sales and purchases of pharmaceuticals were exempt, as stated in the question.

Part (b) for 3 marks required candidates to calculate the year-end VAT correction related to the March 2014 transactions. This part of the question was fairly well answered by the majority of candidates.

The VAT correction was applicable only to the mixed supply purchases and was needed to replace the historical ratio of VATable supplies to total supplies for the year ended 31 December 2013 of 75% with the actual one for the year ended 31 December 2014 of 60%. There were only two transactions which related to mixed supplies: being the purchase of product display services in the pharmacies and the purchase of the industrial mixer, as noted above. In the case of the industrial mixer, the calculated VAT correction need to be adjusted for over a 5-year period therefore only 1/5 of the correction applied in 2014.

Question Three

This 10-mark question required candidates to calculate the CIT payable by a Polish company, Marko Polo Sp. z o.o. (MPS), which had many international activities. The question also involved withholding tax (WHT). This question was reasonably attempted by the majority of candidates.

Most candidates were able to start the calculations by taking the taxable income from MPS's trading activities in Poland, deducting the loss from the branch in the Netherlands, adding the dividend from the Chinese subsidiary (grossed up for 10% WHT) and adding the interest from the Chinese and Dutch subsidiaries (grossed up for 10% WHT and 5% WHT respectively) to arrive at the tax basis. 19% tax was then applicable.

Once the tax at 19% was calculated, there were three tax credits available for MPS and the calculation of these proved more challenging for candidates. Credit for the tax on the Chinese dividend should have been calculated as the lower of (1) the Chinese underlying tax and WHT on the dividend and (2) the Polish tax at 19% on the grossed up dividend. Credits were also available for the WHT on the Chinese and Dutch interest.

The dividend from the Polish subsidiary was not required to be included in the calculation of the tax basis and there was no tax credit for the WHT on the Polish dividend as there was no issue of double taxation. Candidates should have indicated by the use of '0' that the Polish dividend was not taxable, as instructed in the question requirement.

Question Four

This 10-mark question covered the topics of the penalty interest calculation and refund procedure based on a company, Akuratny Sp. z o.o. (Akuratny).

Part (a) (i) for 4 marks required candidates to calculate the penalty interest due to be settled by Akuratny using the standard method of CIT pre-payments. This part of the question was relatively well answered. Candidates needed to identify that the outstanding amount of CIT of 19k PLN was payable by 20 December 2014 gave 109 days of delay until it was paid on 10 April 2015. Most candidates

remembered that penalty interest also applied to VAT as well. The outstanding amount of VAT of 23k PLN was payable by 25 December 2014 giving a delay in payment of 102 days. The penalty interest rate was 10% calculated as 4% (the Lombard rate reported by the National Bank of Poland) multiplied by 200% plus 2%.

Part (a) (ii) for 2 marks required candidates to calculate the penalty interest due to be settled by Akuratny using the simplified method of CIT pre-payments. Candidates also answered this part of the question moderately well. The penalty interest applicable to VAT was the same as in part (a) (i). Penalty interest applicable to CIT should have been calculated based on the outstanding amount of 19k PLN multiplied by the 10% penalty interest rate for 10 days delay out of 365 days. Under the simplified method, prepayments for 2014 are calculated on the basis of the tax due for 2012 with the balance due on 31 March 2015. Therefore, the CIT liability arose on 31 March 2015 - 10 days before the payment date of 10 April 2015.

Part (b) (i) for 1 mark asked candidates to state by when Akuratny could expect to receive the refund of tax and penalty interest. This part of the question was not well answered as, in many cases, candidates referred to the VAT surplus refund instead of the overpaid taxes and penalty interest refund. The correct answer was that they should be refunded within 60 days from the time the tax office receives the refund application and corrected tax return.

Part (b) (ii) for 2 marks required candidates to state the options available to Akuratny if the tax office does not agree to refund the tax overpaid. This part of the question was again generally not well answered and some candidates did not attempt it at all. Akuratny may appeal to the Tax Chamber and, if it upholds the decision of the tax office, an appeal may be filed with the Administrative Court and, finally, to the Supreme Administrative Court.

Part (b) (iii) for 1 mark required candidates to state the tax authorities' obligations if Akuratny eventually wins the refund dispute. This part of the question was not well answered as only a minority of candidates were able to correctly state that the tax office has to refund the tax overpaid and penalty interest, together with interest accrued since the original deadline for the refund.

Question Five

This 15-mark question was based on the case of a married couple, Aldona and Marek, and covered the syllabus area of Personal Income Tax (PIT). It required candidates to calculate the PIT payable by Aldona and Marek for 2014. This question was answered well by the majority of candidates.

Most candidates correctly calculated Aldona's gross salary and added emoluments: training not related to duties, excess per diem and motor car usage to arrive at the social security basis. Social security charge was the calculated and deducted to arrive at the Health Service Contribution (HSC) base. Next, the costs of employment were deducted and rental income was added to arrive at Aldona's taxable income. The rental income was calculated as the monthly rental income multiplied by 12 months less the maintenance costs and depreciation.

In the case of Marek, the majority of correctly correctly took his trading income and deducted the depreciation of equipment and room as well as the calculated social security charge to arrive at his taxable income. However, only a few candidates were able to correctly calculate the equipment

depreciation as 100% of its value. This was due to the rule that low value items can be written off in full. In addition, some candidates struggled with the calculation of the depreciation of the room.

Once the taxable income of both taxpayers was calculated, the majority of candidates were able to confidently complete the calculation to determine the tax due.

It was pleasing to see that the majority of candidates clearly and efficiently laid out their calculations and also correctly indicated by the use of '0' any emoluments of Aldona which were not taxable.

Question Six

This 15-mark question tested the area of CIT based on a company, Ostatex Sp. z o.o. (Ostatex). The question required candidates to calculate the CIT payable/refundable by Ostatex for 2014. This question was not generally well answered by candidates. It is possible that, as this was the last question, some candidates had not managed their time effectively and so time pressure negatively impacted on their performance.

The CIT calculation started with the accounting loss and required a number of adjustments to be made to arrive at the company's taxable income. The first adjustment related to the unpaid interest. Only a few candidates were able to correctly calculate this adjustment. The second adjustment should have been to deduct the German dividend from taxable income. There were also a number of transactions which did not require any adjustment including: advance payment received, capital payment in cash, capital contribution in the form of the perpetual usufruct and penalty interest repaid. Candidates were instructed in the notes to the requirement to indicate any such items not requiring adjustment by the use of zero (0) as there were marks available for this.

The contractual penalty repaid as well as the unexpected cash receipt in respect of bad debts documented by a court collector as irrecoverable should have been added into taxable income. Depreciation of machinery and laptops as well as interest paid and the arrangement fee related to the loan should have been deducted from taxable income.

Machinery was depreciated using the reducing balance method, a 14% depreciation rate and a factor of '2' for faster usage. A few candidates noticed that depreciation for the first year of usage should start in February 2013 therefore the 2013 rate should be multiplied by 11/12. The perpetual usufruct should not have been depreciated. Laptops as low value assets could be written off in full in 2014.

Only a few candidates could correctly calculate the arrangement fee portion for 2014. However, most candidates correctly added the deemed benefit in respect of the free IT services from the shareholder to taxable income. Most candidates also correctly indicated by the use of '0' that the donation did not require adjustment before lowering taxable income by the donation limited to 10% of taxable income. Many candidates also correctly dealt with the tax loss brought forward from 2012.