Examiner's report
F6 (ROM) Taxation
December 2016

General Comments

There were two sections to the examination 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 taxation in more depth. The following paragraphs report on each section and focus on some of the key learning points.

Specific Comments

<u>Section A</u>

It was very pleasing to see that almost all candidates attempted all of the questions. Candidates preparing for the next examination of F6(ROM) are advised to work through the 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(ROM) 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 Question for Discussion

In July 2016, Rinocerul SRL (Rinocerul) made an intra-EU acquisition of a motor car from Germany for

€18,000. Rinocerul is registered for value added tax (VAT) in Romania and in the intra-EU Operators Register.

The motor car has an engine capacity of less than 3,500 kg and has less than nine seats. Rinocerul will not fill in

logbooks *(rom: foi de parcurs)* for this motor car, but will use it for business purposes.

What is the amount of VAT to be paid to the State budget for the intra-EU acquisition of this motor car by

Rinocerul SRL?

A   8,100 lei

B   0 lei

C   16,200 lei

D   1,800 lei

This question tested the calculation of VAT due when partial deduction right is applicable and was not well answered by the majority of candidates. The question required candidates to have the necessary technical knowledge on the following issues:

- For an intra-EU acquisition the person liable to charge VAT is the buyer;
- the VAT charged may be simultaneously deducted by the buyer according to the general rules for deduction;

- in case of motor cars with an engine capacity of less than 3,500 kg and has less than nine seats, the VAT may be deducted entirely only if the company uses the car strictly for business purposes. The business purpose may be proved only with logbooks. Should the company not be able to prove the business use with the logbooks, only 50% of VAT may be deducted;
- the difference between charged VAT and deducted VAT is the VAT to be paid to the State budget.

The correct answer was A, where the amount of VAT to be paid is calculated as follows:

Output VAT = €18,000*4.5 lei/euro*20% = 16,200 lei

Input VAT = 18,000*4.5*20%*50% = 8,100 lei

VAT to be paid = (16,200 - 8,100) = 8,100 lei

The answer in B involved computing the amount of deductible VAT as if the entire charge was VAT deductible, which was incorrect. The question mentioned that the car is used entirely for business purpose, but as the company did not fill in log-books, it could not justify such a use, so as to be able to deduct 100% of the VAT charged.
The same result could be obtained if the candidates made another basic mistake, i.e. considering that at intra-EU acquisitions no VAT is due.

Output VAT = €18,000*4.5 lei/euro*20% = 16,200 lei

Input VAT = €18,000*4.5 lei/euro*20% = 16,200 lei

VAT to be paid = 16,200 - 16,200 = 0 lei

The answer in C was also incorrect, because it failed to compute the input VAT at all.

Output VAT = €18,000*4.5 lei/euro*20% = 16,200 lei

Input VAT = 0 lei

VAT to be paid = 16,200 lei

The D answer was also incorrect as it involved failing to apply the exchange rate RON to EUR to the amounts in EUR.

Output VAT = 18,000*20% = 3,600 lei

Input VAT = 18,000*20%*50% = 1,800 lei

VAT to be paid = 3,600 - 1,800 = 1,800 lei

Thus, although A was the correct answer, all other variants were possible answers if some basic mistakes were made. That is why candidates are encouraged to spend time computing the correct answer, and reading the questions properly rather than guessing.

<u>Section B</u>

Almost all candidates attempted all of the questions. However many candidates presented very non-organised answers, difficult to follow. Workings were often not clearly shown and many candidates failed to apply the rule of starting each question on a new page. Also, there were frequent confusions of rules application. Thus often candidates applied rules for VAT to non-resident tax, or rules for personal income tax to corporate income tax. Candidates preparing for the next examination of F6(ROM) are advised to better prepare and study so as to gain more technical knowledge. Also, a special attention must be given to organizing answers in an ordered and logical manner.

<u>Question One</u>
This 10-mark question covered the topic of VAT.

Part (a) was divided in two sub-parts (i) and (ii). Part (a) (i) for 5 marks required candidates to compute output VAT, input VAT and VAT to be paid to the State budget for a company de-registered ex-officio by the Tax Authorities which had transactions both before and after the de-registration date. It was surprising to see that very few candidates knew how to compute the VAT. The main mistakes were:

- Deducting VAT for transactions after the de-registration date

- Not charging VAT for transactions after the de-registration date.

Actually, candidates failed to recognise the obligations of a company which was de-registrated ex-officio by the Tax Authorities, namely: charging VAT for all transactions after the de-registration date, but not-deducting VAT for all transaction after the same. Usually candidates either both charged and deducted, or both did not charge and did not deduct.

Another major mistake was failing to make VAT adjustments for the VAT deducted for capital goods on the de-registration date.

Part (a) (ii) for 1 mark asked candidates to explain how the VAT calculated in part (a) (i) has to be declared to the State budget. Many candidates knew to declare the obligation to submit the VAT and even mentioned the correct deadline return.

Part (b) requested computation of VAT for self-supplies. Candidates were asked to recognise circumstances when a self-supply takes place and VAT has to be charged. There were some good answers, but the main mistakes were:

- failing to identify the limit of 100 lei per present for which VAT is not charged;

- not identifying that for restaurant services no VAT shall be charged. Many candidates charged VAT only for the value of services above the threshold, which seemed to be computed as the threshold used for computing the tax deductibility of protocol expenses for corporate income tax. It was surprising to see candidates attempting to compute such a threshold, as the question did not provide data enough for its calculation. Candidates are reminded to carefully study the legislation and apply the correct rules for each tax.

- not identifying that a cash sponsorship does not fall within the scope of VAT.

<u>Question Two</u>
This 10 mark question required explanation on the obligations of taxpayers.

In part (a) candidates were asked to present the declaration of payment obligations for different types of revenues obtained by an individual. Some good answers were presented. However, many candidates simply did not mention all revenues. The most often omitted was the employment revenue. Another very common mistake was

failing to clearly identify Andreea's obligations. Candidates are advised to read carefully the text of the questions and answer accordingly. The revenue for which most often obligations were presented incorrectly was the revenue from transactions on the Stock Exchange. This is most probably due to the fact that for this type of revenue a new rule was introduced by the New Tax Law and many candidates presented the old rule. Thus, according to the old rule the tax was withheld at source, whereas according to the New Tax Code it has to be paid by the taxpayer.

In part (b) candidates were asked to state the information and records which a self-employed person must retain for tax purposes. Whilst many candidates identified supporting documents (i.e. invoices), very few mentioned the accounting and tax ledgers.

Part (c) required candidates to explain the tax pre-payments system for corporate income tax and compute the prepayments of corporate income tax for a company. It was surprising to see the large amount of answers which mentioned that prepayments are based on an estimated profit. Candidates are reminded that for corporate income tax there is no rule to compute prepayment based on an estimated profit similar to the personal income tax, the basis being last year's income tax adjusted with inflation rate. It was also surprising to see that many candidates failed to actually make the computation, thus losing the opportunity to easily gain marks. Thus, candidates are advised to carefully read the requirements and answer them accordingly.

Question Three
This 10-mark question covered the topic of corporate income tax and non-resident tax.

Part (a) for 3 marks required the identification of non-taxable revenues for computing corporate income tax. There were a few correct answers, as candidates failed to identify that dividend revenues from Romanian companies are non-taxable, without any further condition. Moreover, some candidates discussed about withholding tax for payment of dividends, not about taxing with corporate income tax the dividend revenue received by a company.

Part (b) for 4 marks required candidates to identify types of revenues that are taxable with the non-resident tax, the conditions for withholding or not withholding the tax and to calculate the withholding tax. This part was very poorly answered. It was very surprising to see that many candidates confused the non-resident tax with VAT. Thus, many of them mentioned rules for the place of supply of services for VAT with services as a condition to tax and computed VAT applying 20% tax rate and even a reverse charge. The candidates who did identify the non-resident tax failed to identify arguments for taxing or non-taxing. Again, there was evidence of candidates not reading carefully the requirements, as many of those who correctly explained the rules failed to make the computation, although it was clearly stated in the requirement that a calculation must be done.

Part (c) for 3 marks required candidates to calculate the corporate income tax. Again, some basic mistakes were made, as many candidates, even if they identified non-taxable revenues in part (a) simply forgot to take them into account when computing the corporate tax. Another common mistake was not forwarding the tax loss or forwarding the tax loss for both years 2008 and 2009, although only the 2009 tax loss could have been forwarded. It was very surprisingly to see that many candidates deducted the tax loss from the corporate income tax and not from the taxable profit. Candidates are reminded that only by a thorough technical preparation marks may be earned.

Question Four
This 10-mark question covered the topics of social contributions and it was very poorly answered.

The candidates were asked to compute the social security fund contribution (*rom: CAS*) and health care insurance fund contribution (*rom: CASS*) for three types of revenues: employment, self-employment and rent. The requirement clearly stated that for each case prepayments and final values have to be computed. Candidates are

reminded that for this type of requirement they should clearly identify both: prepayments and final values and in case no pre-payments are due to clearly mention this. The common mistakes were:

- for the employment revenue: omitting to make the computation for this type of income; not mentioning that no prepayments are due; failing to limit the taxable base for the social security fund contribution to 5 times the average monthly earnings OR limiting both the social security fund contribution and health care insurance fund contribution taxable base to 5 times the average monthly earnings.
- for the self-employment revenue: not testing the obligation to pay social security fund contributions in 2016, based on whether or not the previous year's monthly net income was above 35%*monthly average earnings; not using the 35%*monthly average earnings as the basis for computing the social security fund contribution pre-payments in 2016; not testing if the monthly realised net income in 2016 is above 35%*monthly average earnings, so as to establish if the final values for the social security fund contributions shall be computed based on realised income or shall remain at pre-payments' value; not computing the monthly realised net income, so as to make the comparison with 35%*monthly average earnings, but instead using the annual realised net income.
- for the rent revenue: not limiting the monthly taxable base to 5 times the average monthly earnings; computing the social security fund contribution, although it was not due.

Question Five

This 15-mark question was on corporate income tax and was well answered by many candidates. However, still come very basic mistakes were made. Also, there was evidence that the requirement was not carefully read. This was visible mainly due to the fact that the requirement clearly stated: " You should list all the items referred to in the question and indicate by the use of zero (0) any items which have no impact on the corporate income tax calculation ". However, very few candidates followed this instruction, thus losing the opportunity to easily gain marks. The most common mistakes were:

- failing to identify as non-taxable the increase in value due to the revaluation made;
- failing to correctly compute the tax depreciation;
- considering that the bonus for employees is a social expense. As the bonus is paid for meeting targets, it is paid for work, not for social purposes;
- limiting the deductibility of travel allowance using the rules for personal income tax;
- failing to offset the value of exchange rate expenses with exchange rate revenues and put only the difference as non-deductible;
- putting 50% of research and development expenses as non-deductible instead of as a tax credit;
- subtracting the tax loss from the corporate income tax, not from the taxable profit.

Although many candidates made good calculations, very often their presentation was chaotic. Candidates are reminded that a good organisation of the question may lead to better understanding of requirements, thus more marks.

Question Six

This 15-mark question was on personal income tax.

Part (a) for 4 marks required computation of deductions from employment revenue for an employee who had two employment contracts and for his wife. It was very surprising to see many very basic mistakes to a very straightforward and basic knowledge question. Some candidates added both Mihai's employment revenues and decided that no personal deduction is to be given to him, as the employment revenue is above 3,000 lei. Candidates are reminded that the analysis is to be made separate for each employment contract. Then, candidates should know that only at the basic contract all deductions are allowable, if certain conditions are met, whilst for all other contracts no deduction is allowed other than social contributions. Other mistakes were: deducting the first employer amounts paid at the second employer (i.e. union contribution); not computing the limitation for the facultative private pension insurance; stating that Maria does not have the right for deductions.

Part (b) for 11 marks was divided into 4 subparts. In part (b) (i) candidates had to enumerate at least 4 criteria for qualifying an activity as independent. Many good answers were presented at this part. Parts (b) (ii) and (iii) requested calculations of personal income tax and social contributions under the supposition that same revenue could be qualified as independent or dependent. Many candidates confused the rules and the most common mistakes were:

- in part (b) (ii): not computing the annual revenue, but computing the tax on a monthly revenue; not including deductible expense into the net income calculation; not computing depreciation; not computing social contributions.
- in part (b) (iii): not computing social contributions.

In part b(iv) candidates were required to mention who has the responsibility to classify the activity as dependent/non-dependent. It was surprising to see the large amount of candidates that placed the entire responsibility to the Tax Administration and none to the individual or the company.