

# Examiner's report

F6 Taxation (CZE)

December 2013



## General Comments

The examination consisted of five compulsory questions. Question 1 was for 30 marks, question 2 for 25 marks and questions 3, 4, and 5 were for 15 marks each.

The vast majority of candidates attempted all five questions, and there was little evidence of time pressure. Where questions were left unanswered by candidates, this appeared to be due to a lack of knowledge or poor exam technique, as opposed to time pressure.

As in previous sessions, a majority of candidates answered questions in the same order as in the question paper. However, some candidates answered questions 5 and 4 first and their answers were often incomplete as they seemed to be rushed due to leaving questions 1 and 2 until last.

Candidates performed particularly well on questions 1(a), 2(b), 3(a), 4(c), 5(a) and 5(c). The questions candidates found most challenging were questions 1(b), 2(a), 3(b)(ii), 3(c), and 4(b). This appeared mainly due to candidates not allocating their time properly when studying core syllabus areas. Candidates gave the impression of studying some areas of the syllabus more thoroughly than others.

A number of common issues arose in candidates' answers:

- Failing to read the question requirement clearly and therefore providing irrelevant answers which scored few if any marks.
- Poor time management between questions, some candidates wrote far too much for some questions and this put them under time pressure to finish the remaining questions.
- Providing more than was required on some points and not enough on others.
- Crossing out whole parts of computations resulting in no marks for the relevant parts. Candidates should not delete parts they have spent valuable time on unless they replace these with a better answer.
- Illegible handwriting and poor layout of answers.

## Specific Comments

### Question One

This 30-mark question was based on a Czech tax resident company. Part (a) tested candidates' ability to prepare the corporate income tax return, calculate the accounting profit and arrive at the tax base from it including adjustments to comply with the relevant legislation. Part (b) focused on the distinction between maintenance costs and technical appreciation in the case of the refurbishment of buildings. Part (c) was on the application of the rules for the statute of limitations. Topics covered included tax deductible and non-deductible costs, unpaid debts, tax depreciation, carry forward of losses, allowances for charitable gifts, conditions for binding rulings and the statute of limitation. The format of question 1 was similar to in previous years.

Most candidates performed well on part (a) of the question, although mistakes were made. Most candidates performed very well on the tax depreciation calculations, nevertheless some candidates lost valuable time by calculating tax depreciation allowances on fully written down cars instead of looking at the acquisition year and arriving at the correct answer directly. A significant number also forgot to apply the 10% increase in case of the purchase of a new van in 2011. The performance on the calculation of tax deductible provisions was not satisfactory. Some candidates forgot that tax deductible allowances cannot be applied in the case of a receivable owed by a related party and others confused maximum allowable amounts.

Other problems encountered in part (a) were as follows:

- Many candidates forgot to include the insurance company compensation and/or the release of other reserves in the accounting revenues.
- Candidates made mistakes when calculating the employer's share of social security insurance on fringe benefits. Very few candidates included the social security insurance on the interest on the interest-free loan to Mrs Jaklova that exceeded the exempt amount of CZK 100,000 or the social security insurance on the cars used by employees and the apartment rent in excess of the exempt amount.
- Some mistakes occurred in adjustments of the tax base. A few candidates did not adjust for the qualifying social benefits of employees. Candidates should have mentioned that the creation and payments from the social security fund were considered a balance sheet operation which is a valid option. Many candidates made no correction for the non-arm's length rent paid to a related owner. Many candidates also forgot to add back the non-deductible donation.
- Application of the gift allowance before the allowance for carry forward of losses.

In part (b) many candidates struggled to differentiate between refurbishment comprising regular maintenance and that enhancing the functionality of the building and therefore were not able to gain high marks. Obligatory requirements of an application for a binding ruling were listed by many, though some candidates forgot some basic items such as identification data of the taxpayer. A significant minority of candidates omitted this part of the question altogether.

Part (c) was omitted by many. Those who answered often did not provide very consistent answers. Those candidates who replied 2011 in (i) received full marks as this was correct based on the Supreme Court ruling. 2012 was in this case considered a correct answer as students of F6 CZE are not, in principle, required to study court decisions.

### Question Two

This 25-mark question covered the personal income tax calculation of a Czech tax resident Ms Bauerova who moved from the Czech Republic to the Netherlands during the fiscal year and had income from both the Czech Republic and the Netherlands. It covered rules on the determination of tax residency of an individual taxpayer according to the Czech tax legislation, identification of taxable employment income including severance payments, calculation of tax advances withheld from employment income (including calculation of a solidarity surcharge), identification of tax-exempt income, application of an exemption method for the elimination of double taxation of income from abroad, application of tax base and tax liability deductions.

Part (a) for 2 marks required candidates to give the criteria for the tax residence of an individual taxpayer according to the Czech Income Taxes Act. Part (d) for another 2 marks was related to this task. It required candidates to explain what happens in dual residence situation. In part (d) candidates were simply expected to briefly describe the procedure (application of the tax treaty) with no particular detail, e. g. tie breaker criteria. Nevertheless candidates' performance on these two parts was unsatisfactory. Some confused physical presence with the economic activity and many showed a lack of knowledge of the basic concept that is crucial for the correct calculation of the individual income tax.

Part (b) consisted of the computation of the personal income tax and a large number of candidates provided excellent answers. Some candidates did not include the income from the Netherlands in Ms Bauerova's worldwide income. This may have been the result of the poor application of the above mentioned residency concept, which is essential in this area. In addition, those candidates did not gain very high marks for this part because they also often did not apply the elimination of double taxation through the exemption method correctly.

Another common mistake was not claiming life insurance or mortgage tax base allowance. Many candidates did not apply the credits correctly. Some candidates applied the spouse credit for Mr Clang and also a child credit for his child. They scored no marks as Ms Bauerova married him only in December 2013 and there was no mention

in the question that at the same time she would be adopting his child. Others thought that no personal credit was available in the tax return if the taxpayer did not sign the declaration on allowances with the employer.

Part (c) on individual income tax advances was correctly answered by many, though a significant number of candidates did not even attempt this part.

### Question Three

This 15-mark question focussed on Lombok, a. s., a VAT payer performing local as well as international transactions and renting out premises. It covered local and international transactions, exempt supplies without recovery of input VAT, calculation of actual coefficient and tax administration.

The structure of the question was similar to previous years, though in part (a) candidates were required to verbally describe the individual transactions. Marks were given also to candidates who, in addition to stating whether the supply was taxable, exempt, etc. carried through their answers into "input or output" VAT. Those students could score well, although they spent more time than was necessary on this question as they were doing something in addition to what was required.

In part (b) (i) candidates were required to calculate the actual coefficient and many provided very satisfactory answers. In contrast to that in part (b) (ii) the performance was disappointing despite similar questions having been tested in the past. Candidates were asked to state how the advance and actual coefficients are being reconciled and only a very few were able to provide relevant answers.

Part (c) was on the consequences of non-compliance. This part was omitted by many and those who attempted it generally did not do well. Traditionally questions on tax administration are unpopular in the F6 exam and candidates continue to show a lack of knowledge on topics related to tax management and administration regardless of whether they are included in a separate question or are a part of a question on another subject. It is difficult to comment on the nature of the mistakes and potential causes as the answers on this particular part were very brief.

### Question Four

This 15-mark question was based on a newly established company Hoza, s. r. o. and its partners. It focused on tax registration obligations of individuals and a limited liability company starting their business activity.

Parts (a) and (b) covered competent authority, deadlines, information to be provided and rules for changing a taxable period for the purpose of value added tax. The performance on these two parts was variable and the most common mistakes included:

- Omission of competent authority or required deadline
- Forgetting that Hoza, s. r. o. would be obliged to open a wage payer because of the restaurant and its employees
- Confusing the general threshold for VAT payers with the distinction between a monthly and a quarterly VAT payer

Part (c) was on the obligatory parts of the application for registration of a corporate taxpayer. The vast majority of candidates gave very satisfactory answers for this part.

### Question Five

This 15-mark question was based on Mr Dolensky and required the personal income tax base calculation of a Czech tax resident having different types of income. It covered taxation of income of an executive based on a contract of mandate, dividend income, rental income and business income, income taxed by final withholding



tax, application of lump sum expenses, calculation of future tax advances and calculation of social security and health care insurance contributions in relation to business activity.

In part (a) candidates were required to calculate the individual income tax base comprising employment income, business income, capital income and rental income. Candidates performed very well on this part. However, some forgot to include the obligatory social security insurance on the statutory representative fee and others did not mention that the dividend and interest was subject to a withholding tax. The vast majority of candidates correctly applied the lump-sum expenses, though some errors occurred regarding the percentage or a failure to apply the lump-sum expenses. A significant minority of candidates seemed to have been mixing up employment income with business income and the capital income as far as namely statutory representative fees, exhibition design remuneration and interest income were concerned.

In part (b) candidates were required to calculate tax advances. Some candidates did not attempt this part, but those who did generally provided very satisfactory answers.

Part (c) was on social security and health care insurance base and contributions computation and was well performed.