Professional Level – Essentials Module

Advanced Taxation (Malta)

Thursday 10 December 2015

Paper P6 (MLA)

Time allowed
Reading and planning: 15 minutes
Writing: 3 hours

This question paper is divided into two sections:

Section A – BOTH questions are compulsory and MUST be attempted

Section B – TWO questions ONLY to be attempted

Tax rates and allowances are on pages 2–5

Do NOT open this question paper until instructed by the supervisor. During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.
This question paper must not be removed from the examination hall.

The Association of Chartered Certified Accountants

The Malta Institute of Accountants

SUPPLEMENTARY INSTRUCTIONS

1. You should assume that the tax rates and allowances shown below will continue to apply for the foreseeable future
2. Calculations and workings need only be made to the nearest €
3. All apportionments should be made to the nearest month unless stated otherwise
4. All workings should be shown

TAX RATES AND ALLOWANCES

The following tax rates and allowances for 2014 (year of assessment 2015) are to be used in answering the questions.

Individual income tax

Resident individual tax rates

Married couples – joint computation		Other individuals	
€		€	
0 – 11,900	0%	0 – 8,500	0%
Next 9,300	15%	Next 6,000	15%
Next 7,500	25%	Next 5,000	25%
Next 31,300	29%	Next 40,500	29%
Remainder	35%	Remainder	35%

Parent rates

€	
0 – 9,800	0%
Next 6,000	15%
Next 5,400	25%
Next 38,800	29%
Remainder	35%

Non-resident individuals

€	
0 – 700	0%
Next 2,400	20%
Next 4,700	30%
Remainder	35%

Returned migrants

Married couples		Others	
€		€	
0 – 5,900	0%	0 – 4,200	0%
Remainder	15%	Remainder	15%

Capital allowances – Income Tax Act

Industrial buildings and structures

Initial allowance	10%
Wear and tear allowance	2%

Plant and machinery

Wear and tear allowance as indicated in the question where applicable

Capital allowances – Business Promotion Act

Investment allowances

Industrial buildings and structures	20%
Plant and machinery	50%

Corporate income tax

Standard rate	35%

Value added tax (VAT)

Standard rate	18%
Reduced rate	5%
Reduced rate – accommodation	7%

Car fringe benefit

Annual value of benefit = (vehicle use + fuel value + maintenance value) x private use percentage

Vehicle use	**% of vehicle value**
Vehicle not more than six years old	17%
Vehicle more than six years old	10%

Fuel value	**% of vehicle value**
Vehicle value not exceeding €28,000	3%
Vehicle value exceeding €28,000	5%

Maintenance value	**% of vehicle value**
Vehicle value not exceeding €28,000	3%
Vehicle value exceeding €28,000	5%

Car value	**Private use percentage**
Not exceeding €16,310	30%
Exceeding €16,310 but not €21,000	40%
Exceeding €21,000 but not €32,620	50%
Exceeding €32,620 but not €46,600	55%
Exceeding €46,600	60%

Capital gains

Index of inflation

1988	439·62
1989	443·39
1990	456·61
1991	468·21
1992	475·89
1993	495·60
1994	516·06
1995	536·61
1996	549·95
1997	567·95
1998	580·61
1999	593·00
2000	607·07
2001	624·85
2002	638·54
2003	646·84
2004	664·88
2005	684·88
2006	703·88
2007	712·68
2008	743·05
2009	758·58
2010	770·07
2011	791·02
2012	810·16
2013	821·34
2014	823·89

Applicability of increase for inflation

$$\frac{\text{Cost of acquisition/improvements}}{1} \times \frac{\text{index(yd)} - \text{index(ya)}}{\text{index(ya)}}$$

Where:
index(yd) is the index for the year immediately preceding that in which the transfer is made;
index(ya) is the index for the year immediately preceding that in which the property in question had been acquired or completed, whichever is the later, or, when it relates to improvements, for the year immediately preceding that in which the cost of carrying out the improvements was incurred.

Transfer of value

$Y = (A - B) + C - D$

Where:
- 'Y' represents the value transferred or acquired by a person
- 'A' is the market value of the shares held in the company immediately before the change
- 'B' is the market value of the shares held in the company immediately after the change
- 'C' is the consideration paid by the person for the acquisition of shares or additional shares issued by the company, where the change consists of an issue of share capital for consideration
- 'D' is the amount paid by the company in respect of a cancellation of shares held by the person, where the change consists of a reduction of share capital

Cost of acquisition of shares in the transfer of value

Z = ((A – B)/A) x E

Where:
'Z' represents the amount to be determined
'A' is the market value of the shares held by the transferor immediately before the change
'B' is the market value of the shares held by the transferor immediately after the change
'E' is the cost of acquisition of the shares held by the transferor immediately before the change

Investment aid regulations

Definition of a medium sized enterprise

An enterprise which is not a small enterprise and:

– has fewer than 250 employees; and
– has an annual turnover not exceeding €50 million and/or annual balance sheet total not exceeding €43 million; and
– is to be treated as being independent.

Definition of a small enterprise

An enterprise which:

– has fewer than 50 employees; and
– has an annual turnover and/or annual balance sheet total not exceeding €10 million; and
– is to be treated as being independent.

Stamp duty

Standard rate	€2 for every €100 in value or part thereof
Property companies (as defined)	€5 for every €100 in value or part thereof

Annual market rent (tax accounting)

The annual market rent of immovable property situated in Malta owned and used by a company for the purpose of its activities (excluding property which is rented by the said company to other parties) is calculated by multiplying the aggregate surface area in square metres of all floors of such premises so owned and used by €250 per annum.

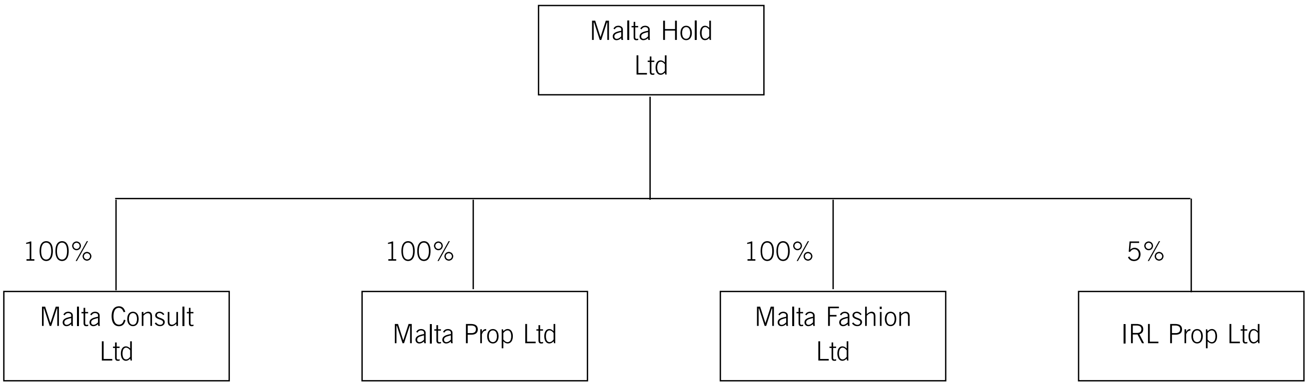
Tax refund calculation when a company benefits from a reduced rate in terms of a tax treaty

Y = (R – 5%)/R

Where:
'Y' represents the rate to be determined; and
'R' represents the reduced rate.

Section A – BOTH questions are compulsory and MUST be attempted

1



Malta Hold Ltd, a company incorporated in Malta, is fully owned by an individual, Mr Xavier, who is neither resident nor domiciled in Malta. Malta Hold Ltd is the 100% shareholder of three Malta companies, Malta Consult Ltd, Malta Prop Ltd and Malta Fashion Ltd; and also holds a 5% investment in the shares of a non-Malta company, IRL Prop Ltd. Further details regarding these four companies are as follows:

– Malta Consult Ltd, a company incorporated in Malta, provides consultancy services to companies incorporated outside Malta.

  Malta Consult Ltd mainly provides its services through offices physically located in Malta, which it rents from third parties.

  Occasionally Malta Consult Ltd's employees travel to other jurisdictions for periods of approximately one month in order to carry out field work. Malta Consult Ltd does not have offices in any country other than Malta.

  In 2014, Malta Consult Ltd derived a profit for tax purposes of €750,000. These profits were fully distributed to Malta Hold Ltd.

– Malta Prop Ltd, a company incorporated in Malta, was set up to own, manage and rent out immovable property situated in Malta.

  Malta Prop Ltd acquired two apartment blocks – Sunflower Court and Sunshine Court – by means of a business loan, and converted them into rental apartments for residential purposes.

  Sunflower Court has five apartments which are mainly rented out to tourists for stays of a maximum of three months. All five apartments are licensed by virtue of the Malta Travel and Tourism Services Act. Advertising for the apartments in Sunflower Court is mainly done online, through a website set up for this purpose which is run by Mr Xavier (the shareholder of Malta Hold Ltd), as well as through listings on various international websites.

  Sunshine Court has four apartments which are all rented out for long lets to Maltese individuals and so these apartments do not need to be licensed under the Malta Travel and Tourism Services Act. Advertising for the apartments in Sunshine Court is also done through the website run by Mr Xavier, as well as through listings with various Maltese estate agents.

  In 2014, Malta Prop Co derived rental income of €120,000 from Sunflower Court and €72,000 from Sunshine Court. Malta Prop Ltd always distributes its annual profits in full to Malta Hold Ltd.

– Malta Fashion Ltd, a company incorporated in Malta, is a retailer of Italian fashion brands in Malta.

  Malta Fashion Ltd has three shops in Malta which it rents from third parties.

  In 2014, Malta Fashion Ltd made a loss for tax purposes of €150,000.

– IRL Prop Ltd, a company incorporated and tax resident in Ireland, owns a large office block in Dublin (in Ireland) which it rents out to third parties.

  IRL Prop Ltd was set up in 2008 with a share capital of €30,000,000. Malta Hold Ltd subscribed for 5% of the shares in IRL Prop Ltd (i.e. 1,500,000 fully paid up ordinary shares of €1 each carrying voting rights) upon initial subscription. The current value of Malta Hold Ltd's shareholding in IRL Prop Ltd is €1,000,000.

  In 2014, Malta Hold Ltd derived dividend income of €300,000 from IRL Prop Ltd.

Required:

Draft a letter to the directors of Malta Hold Ltd which explains the Maltese tax implications of the income derived by the Malta Hold Ltd group of companies with respect to:

- **the income tax treatment of the income derived by Malta Consult Ltd, including the possibility, if any, of Malta Consult Ltd being treated as having a permanent establishment in the countries where its employees carry out field work;**
- **the income tax treatment of the income derived by Malta Prop Ltd, including a consideration of the nature of the income derived;**
- **the income tax treatment of the dividend income derived by Malta Hold Ltd from IRL Prop Ltd, and the extent to which the imputation system, and the right to tax refunds, can be applied to the profits derived by and distributed by Malta Consult Ltd and Malta Prop Ltd; and**
- **the utilisation of the tax losses of Malta Fashion Ltd.**

In the case of each of the Malta companies, clearly identify how the profits will be allocated to their respective tax accounts.

Note: You are not required to carry out any calculations. (31 marks)

Professional marks will be awarded for the format and presentation of the letter and the effective communication of the information. (4 marks)

(35 marks)

2 Peter Zammit is an individual resident and domiciled in Malta. He is the 100% founding shareholder of Maz Ltd, a company incorporated in Malta which owns two properties in Malta:

– a warehouse, which it has owned for the last ten years and currently leases out to third parties; and

– a whole floor in a premium office block, which it acquired in 2010 in order to resell at a profit and holds as a trading asset.

Peter also owns a house in Malta in his own name. He has occupied this house as his dwelling house for the last ten years.

Peter intends to transfer the warehouse and his dwelling house to his only son, Paul. Paul is married and has lived with his wife and family in a separate house in Malta for the last four years.

Peter plans to transfer the immovable property as follows:

– Maz Ltd will transfer the whole floor in the premium office block to Mit Ltd, a company which is owned as to 81% by Peter and as to 19% by Paul, at its cost of acquisition.

– Maz Ltd will be put into liquidation, and in the course of the liquidation the warehouse will be transferred to Paul.

– The dwelling house will be transferred by Peter to Paul by way of inheritance (*causa mortis* transfer).

The whole floor in the premium office block is to remain under the ownership of Mit Ltd until a buyer is found.

Paul has been informed of his father's intention and he has made his own plans as follows:

– Paul will sell the warehouse as soon as he receives it.

– Upon inheriting his father's house, Paul will sell his current house, and he and his family will move into his father's house. However, Paul only expects to live in his father's house for a year or two, following which he will most likely sell it.

Required:

(a) Explain the income tax and duty on documents and transfers implications, and any filing requirements, of the proposed transfers of the immovable properties by Peter Zammit. (19 marks)

(b) Explain the income tax implications of Paul Zammit's plans with respect to the warehouse, the dwelling house transferred to him by Peter, and the sale of his current residence. (6 marks)

(25 marks)

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Section B begins on page 10.

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Section B – TWO questions ONLY to be attempted

3 (a) Anne Goll is an individual who to date has always been tax resident and domiciled in Switzerland. She has recently been appointed as commercial officer (CO) of the Gozo International Airport Ltd (GIAL) under a five-year contract. GIAL is a company tax resident in Malta, and holding an aerodrome licence issued in terms of Article 71 of the Air Navigation Order.

Anne is currently employed by Swiss Airports Ltd (SAL), a company tax resident in Switzerland which operates various small airports in Europe. SAL owns 50% of the shares in GIAL. Anne will remain employed with SAL, a role which will require her to be physically present for work in Switzerland for a period of one month each year. She will also continue to be a director of SAL. Her salary from SAL as an employee will be €20,000 per annum, and her director's fee €15,000 per annum. Both these sums will be paid into Anne's Swiss bank account.

Anne and her partner currently live in Geneva (in Switzerland), in a house which they own there and have lived in for the last ten years. On taking up her appointment with GIAL, Anne will move to Gozo, where she will take up residence with her partner. They will retain ownership of their house in Geneva, and Anne will stay in the house whenever she returns to Geneva during the five-year contract period. They will both re-occupy the house when they return to take up residence in Geneva again, at the end of the contract.

Anne's role as CO will require her to travel outside Malta on a regular basis. She expects to spend approximately one month per year in Switzerland conducting business for GIAL, as well as a further three months per year across the rest of Europe. Taking into account the month per year she will spend in Switzerland conducting business for SAL, Anne will spend a total of five months per year outside Malta. GIAL will not have any offices outside Malta or Gozo, and Anne's business trips will mainly be promotional, to attract airlines to use the airport in Gozo.

Anne will be paid a salary of €120,000 a year by GIAL, and given that she will also sit on the GIAL's board of directors, she will receive a further €10,000 in director's fees. Her salary and director's fees from GIAL will be paid into a bank account she will open in Malta.

During the period of the contract, Anne will be deemed to be tax resident in Malta for domestic tax purposes; she will also be deemed to be tax resident in Switzerland for domestic tax purposes.

Required:

Explain the income tax implications of Anne Goll's employment and directorships with Gozo International Airport Ltd and Swiss Airports Ltd. In particular you should consider:

- **the basis of her tax liability in Malta on account of her personal tax status;**
- **the respective taxing rights of Malta and Switzerland under the double tax treaty between Malta and Switzerland;**
- **the application or otherwise of the highly qualified persons rules; and**
- **the application or otherwise of the rules relating to employment outside Malta.**

Notes:
1. You should assume that the double tax treaty between Malta and Switzerland is similar in all respects to the OECD Model Tax Convention.
2. You are not required to calculate Anne Goll's tax liabilities. (13 marks)

(b) Elton Jones, an Irish resident and domiciled individual, is a former world famous singer who now performs at various hotels around Europe. In 2015, Elton was asked to perform for the guests of a popular hotel in Qawra for five nights during the month of January, and to perform for a further seven nights at another popular hotel in Bugibba in the month of July. He charged €1,500 per night for these performances.

Elton has now been asked to perform in Malta for a further four nights during the 2015 Christmas period, with the last night being New Year's Eve. His fees for the holiday season are €2,500 per night.

When performing in Malta, Mr Jones rents an apartment by the sea front for €100 a night. In January he stayed in Malta for seven nights, in July for ten nights, and over the Christmas period he is planning to stay for a total of 14 nights, starting on Christmas Eve.

His return flights to Malta cost €250 for each visit.

Required:

Explain the tax treatment of Elton Jones' activities in Malta. In particular you should consider:

- **the basis of his tax liability in Malta on account of his personal tax status;**
- **the application of the double tax treaty between Malta and Ireland; and**
- **the taxation of his entertainment activities in Malta.**

Note: You should assume that the double tax treaty between Malta and Ireland is similar in all respects to the OECD Model Tax Convention. (7 marks)

(20 marks)

4 (a) In 2009 Hill Ltd, a limited liability company, built an office block of ten offices in Sliema for which it incurred €700,000 of expenses for construction works and €300,000 on furniture, excluding value added tax (VAT). Hill Ltd paid total VAT of €180,000 on these works and furniture. The cost of the construction and furniture was split equally over the ten offices.

Hill Ltd's plan was always to lease the offices to companies registered under Article 10 of the VAT Act and in the years 2009 (the year of completion of the construction works) to 2014 inclusive this is what it did. However, in 2015 Hill Ltd terminated the lease of the office on the top floor in order to convert that floor into an apartment for use by its sole Maltese shareholder. Following the conversion works, which will be carried out and paid for by the shareholder, Hill Ltd will rent the floor out to the shareholder for a period of 16 years.

Required:

Explain the value added tax (VAT) implications for Hill Ltd of:

– **the construction and rental of the offices; and**
– **the conversion of the top office to an apartment and the application of the capital goods scheme.**

(12 marks)

(b) Malta Bank Ltd is a company tax resident in Malta, licensed as a credit institution with the Malta Financial Services Authority and engaged in the granting and negotiation of credit and the management of credit. In 2010, Malta Bank Ltd undertook a refurbishment of the offices owned and used by it, at a total cost of €1,770,000, including value added tax (VAT) of €270,000.

Malta Bank Ltd provides its banking services to both EU and non-EU clients. During 2010, it was established that 40% of its turnover was generated from customers who are established in the EU and 60% of its turnover from customers who are established outside the EU. This proportion was kept constant throughout the following four years, but in 2015 the proportion of turnover from non-EU customers increased to 70%, with only 30% of turnover being from the EU customers. Malta Bank Ltd intends to achieve a proportion of EU to non-EU customers of 50:50 in 2016.

Required:

In respect of Malta Bank Ltd's value added tax (VAT) position, explain:

– **the registration requirements;**
– **its right to claim a credit for the input VAT incurred on the refurbishment, and the extent thereof; and**
– **the application of the capital goods scheme in view of the changes to the bank's customer base.**

(8 marks)

(20 marks)

5 **(a)** Sailfar Ltd is a company incorporated in Jersey, but managed and controlled in Malta. In 2010, Sailfar Ltd acquired a large ferry boat for €12,000,000. The purchase was fully financed from the company's own (equity) funds. The ferry boat was immediately leased on a fully equipped basis under an operating lease to Turk Ferry Ltd, a ferry operator tax resident in Turkey, for a period of ten years for an annual lease charge of €1,500,000. Turk Ferry Ltd operates the ferry for nine months a year between Turkey and Lebanon.

In 2015, Sailfar Ltd sold the ferry for €9,000,000 to Ferry Italia Ltd, a ferry operator in Italy. In order to honour its contractual obligations with Turk Ferry Ltd, Sailfar Ltd acquired a second ferry for €8,000,000 which it continued to lease to Turk Ferry Ltd for the remaining five years for the same lease charge of €1,500,000 a year.

All income or gains derived by Sailfar Ltd are received in a Maltese bank account. Sailfar Ltd depreciates its ferries for both accounting and tax purposes on a straight line basis over a period of ten years.

In terms of Turkey's domestic tax legislation, a withholding tax of 15% applies on lease payments made by residents of Turkey to persons not resident in Turkey.

Required:

(i) Explain the income tax implications for Sailfar Ltd of:

- **the lease of the ferry boat to Turk Ferry Ltd, taking into consideration the application of the double tax treaty between Malta and Turkey; and**
- **the sale of the ferry boat to Ferry Italia Ltd, taking into consideration the application of the double tax treaty between Malta and Turkey, any balancing allowance or charge which may be claimed or due, and the impact of the sale on the capital allowances which may be claimed on the second ferry.**

Note: You should assume that the double tax treaty between Malta and Turkey is similar in all respects to the OECD Model Tax Convention. (14 marks)

(ii) Prepare the balancing statement for Sailfar Ltd on the sale of the first ferry, and calculate the base cost of the second ferry for the purpose of capital allowances. (2 marks)

(b) The transfer of marketable securities is generally subject to duty on documents and transfers. However, where acquisitions or disposals are made by certain persons or trusts or other fiduciary arrangements, in an international scenario the transfer or acquisition may be exempt from duty.

Required:

Identify the persons and/or entities (other than international trading companies and the transferors of securities in listed companies) to which such an exemption from the duty on documents and transfers applies. (4 marks)

(20 marks)

End of Question Paper