Answers

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Dear Ms Rosaldo

Following our discussions, please find enclosed our comments on the Maltese income tax and VAT treatment of the rental receipts derived by MPL, and the tax implications arising on the transfer of the Valletta commercial property with our recommendations.

(a) (i) Income tax treatment of the rental income derived by MPL

MPL is a company incorporated in Malta and is therefore taxable in Malta on its worldwide income.

Since MPL's income for the financial year 2017 is exclusively made up of rental income, it needs to be established whether the income is of a trading or passive nature and whether the 15% flat tax rate option on the gross rental income is available. Generally, rental income is treated as income of a trading nature only when the lessor has an active involvement in the generation of the rental income, which principally is of a short-term nature. The rental income derived from the Bugibba property is classified as short-term income and therefore MPL is entitled to claim as a deduction all expenses incurred wholly and exclusively in the production of the income.

The other rental income is of a passive nature. Accordingly, the allowable deductions are limited to:

(a) any licence fees, rent or ground rent payable on the property;
(b) a 20% further deduction on the gross rent less the deductions referred to in (a) above; and
(c) any interest paid on a loan taken to acquire the property being rented out

provided the deductions do not exceed the gross rent derived. Therefore, any other expense not listed above would be treated as a disallowed expenses.

MPL can opt to tax both the trading and passive rental income at the 15% flat rate on the gross rental income as long as MPL opts to tax **all** rents (unless precluded from doing so) using the final tax system. The 15% final tax system is not available to property leases between two companies which are owned 25% or more by the same individuals. Accordingly, since you own more than 25% of the share capital in both the lessor (MPL) and the lessee (FSL), MPL is subject to a 35% tax charge on the net passive income on the lease of the Valletta commercial property. Note that for purposes of establishing whether MPL is applying the 15% final tax system to **all** rental income, the Valletta commercial lease is ignored since the 15% final tax option is not applicable to the Valletta property lease.

(ii) Tax due for year of assessment 2018

Do not opt for the 15% final tax system

	Gozo	Sliema	Valletta	Gzira	Birkirkara	Bugibba	Total
	€	€	€	€	€	€	
Gross rent	40,000	72,000	80,000	14,000	8,000	17,000	
Ground rent	0	(7,000)	(6,000)	0	(1,000)	(4,000)	
Net rent	40,000	65,000	74,000	14,000	7,000	13,000	
20% further deduction	(8,000)	(13,000)	(14,800)	(2,800)	(1,400)	N/A	
Other expenses	N/A	N/A	N/A	N/A	N/A	(12,500)	
Interest deduction	(3,000)	(20,000)	(5,000)	(2,000)	0	(5,500)	
Taxable rental income	29,000	32,000	54,200	9,200	5,600	(5,000)	
Tax losses available	(5,000)						
Taxable income net of losses	24,000	32,000	54,200	9,200	5,600	0	
Tax at 35%	8,400	11,200	18,970	3,220	1,960	0	43,750

Opt for the 15% final tax system

	Gozo	Sliema	Valletta	Gzira	Birkirkara	Bugibba	Total
	€	€	€	€	€	€	
Gross rent	40,000	72,000	80,000	14,000	8,000	17,000	
15% tax thereon	6,000	10,800	N/A	2,100	1,200	2,550	22,650
Valletta property tax (as above)			18,970				18,970
Total tax							41,620

If MPL opts for the 15% final tax system, the total tax due would amount to €41,620. If MPL does not opt for the 15% final tax system, the trade loss (€5,000) made on the short-term Bugibba rental income can be set off against the passive rental income derived during the year, resulting in total tax of €43,750.

Accordingly, the 15% final tax system with the Valletta lease being taxed at 35% (on the gross rent net of the 20% further allowance and the deductible interest) is the most tax efficient method.

(b) (i) The VAT treatment of the rental/property lease income derived by MPL

Generally, all immovable property leases are treated as exempt from VAT, without a right to a credit for input VAT. However, a number of exceptions to the exemption apply.

Residential property leases are subject to VAT if the service consists of the provision of accommodation requiring a licence in terms of the Malta Travel and Tourism Act. This would be the case if the lessee is classified as a tourist and is not in Malta for employment or trade/business reasons. The Bugibba rental income (let to tourists) is therefore not exempt from VAT and will be subject to VAT, but at the reduced rate of 7%. However, the lease of the Gzira property to the gaming company employee and the lease of the Birkirkara property to the Maltese resident family (not tourists) will be exempt from VAT.

Commercial property leases are subject to VAT if the lessor is a limited liability company and the lessee is registered for VAT in terms of Article 10 of the VAT Act. This means that the Valletta and Gozo leases will be subject to VAT at the standard VAT rate of 18%, whereas the lease of the Sliema property will be treated as exempt without credit since the lessee is registered for VAT in terms of Article 11 and not Article 10 of the VAT Act.

(ii) Right to claim back input VAT

The VAT Act grants an Article 10 registered taxable person the right to claim back a credit for input VAT when the input VAT is directly related to taxable supplies. Therefore, MPL is able to claim a full credit for input VAT directly related to the lease of the Gozo, Valletta and Bugibba properties which are subject to VAT. However, no input VAT may be claimed in respect of the Sliema, Birkirkara and Gzira leases which are exempt without credit.

For general overheads which cannot be directly allocated to either taxable or exempt without credit supplies, MPL is required to utilise the partial attribution rules. During 2017 MPL will provisionally claim a portion of input VAT on the general overheads. The portion is established by dividing the lease income subject to output VAT during the previous year (2016) by the total value of supplies for 2016. At the end of 2017, MPL will be able to establish the actual percentage of taxable supplies to the total supplies for the year, and will adjust for any over or under claimed input VAT in the first VAT return for the subsequent year (2018).

(iii) MPL – VAT due for 2017

Property	Rent	Output VAT	Direct expenses	Input VAT
	€	€	€	€
Gozo	40,000	7,200	12,000	2,160
Sliema	72,000	0	19,000	0
Valletta	80,000	14,400	5,100	918
Gzira	14,000	0	2,500	0
Birkirkara	8,000	0	1,400	0
Bugibba	17,000	1,190	12,500	2,250
Total	231,000	22,790	52,500	5,328

Taxable supplies	(40,000 Gozo + 80,000 Valletta) (excluding Bugibba property)	120,000
Partial attribution percentage	(120,000/214,000 excluding Bugibba property)	56·07%
		€
Output VAT		22,790
Direct input VAT		(5,328)
Provisional partial attribution	(€100,000 x 18% x 40%)	(7,200)
VAT due before definitive ratio adjustment		10,262
Definitive ratio adjustment	(€100,000 x 18% x (56·07% – 40%))	(2,893)
VAT due after definitive ratio adjustment		7,369

(c) Property transfer tax and duty on documents applicable on the transfer of the Valletta commercial property

Option A

A transfer of immovable property situated in Malta is, by default, subject to an 8% final tax on the transfer value (i.e. the higher of the consideration and the market value of the immovable property). However, where the property was acquired before 1 January 2004, the final tax is increased to 10% of the transfer value. Therefore, should MPL transfer the Valletta commercial property to you, a 10% property transfer tax plus a 5% duty on documents would arise.

Option B

If MPL were to transfer all of its immovable property to FSL, such a transfer would qualify for an exemption from both the property transfer tax and duty on documents, since MPL and FSL are deemed to be a group of companies. This is the case because the two companies are owned directly by the same shareholder, you, (the minority interest in FSL may be ignored since it is less than 20%) and the variation in shareholding and voting rights between MPL and FSL held by you is less than 20%. If MPL is placed into liquidation and during the winding up procedures the Valletta property (classified as a capital asset for more than five years) is transferred to you, since you hold more than 95% of the share capital for more than five years, such a transfer would also be exempt from both the property transfer tax and duty on documents. Therefore, under Option B no tax or duty leakage is expected.

Option C

Initially the same intra group exemption from the property transfer tax and duty on documents, applicable under Option B, would be available. However, when FSL is converted to a partnership, it is important to establish whether FSL will opt to be treated as a transparent or opaque entity for tax purposes. If FSL opts for a transparent tax treatment and the conversion happens within six years of the intra group transfer, the exemption from the property transfer tax would be clawed back and FSL would be liable to pay the 10% property transfer tax which would have been due on the transfer. Such a claw back would not be triggered if the non-transparent tax treatment is retained by FSL. In neither case will there be a claw back of the duty on documents exemption.

Recommendation

Option B or Option C with FSL opting for an opaque tax treatment post conversion to partnership appear to be the most tax efficient options.

I trust that the above addresses the issues raised to your satisfaction. Please do not hesitate to contact us if you need any further clarifications.

Yours sincerely

Tax consultant

2 (a) Maltese tax treatment of income

RPH, MTL and IREL are companies incorporated, managed and controlled in Malta and are therefore taxable in Malta on their worldwide income.

Malta Trade Ltd (MTL)

MTL's trading income from the manufacture of chocolate through a factory situated in Malta is taxable in Malta at the standard corporate tax rate of 35% and is to be allocated to the Maltese taxed account (MTA). However, since the company owns and uses an immovable property situated in Malta, it is required to make a secondary allocation from its MTA to its immovable property account (IPA) of €250 per square metre, in this case €125,000 (€250 x 500m^2). Should MTL's MTA reserves be insufficient to absorb the secondary allocation to the IPA, any related company would be required to absorb the reallocation. For the purposes of the secondary allocation rules, two Malta resident companies are deemed to be related if one is a more than 50% subsidiary of another or both are more than 50% subsidiaries of a third company resident in Malta. Since RPH does not own at least 50% of MTL, MTL is not deemed to be related to any other company. Therefore MTL would need to carry forward the shortfall and absorb the reallocation in the subsequent year of assessment.

A distribution of profits from MTL's MTA to RPH would entitle RPH to a 6/7ths refund of the tax paid by MTL. However, a dividend from the IPA would not give rise to any such refund.

Property Lease Ltd (PLL)

Since PLL is neither resident, nor managed and controlled in Malta, it is only liable to tax in Malta on the rental income derived in Malta from the lease of the Valletta office block to unrelated parties. PLL may opt to apply 15% final tax on the gross rental income without any deduction (allocating the income to the final tax account (FTA)) or, alternatively, tax the rental income at 35% after deducting interest on any loan taken to acquire the property being rented out and the further 20% deduction. Any distribution of profits from the FTA (or the IPA if the 15% final tax option is not applied) would not entitle RPH to any tax refunds.

International Real Estate Ltd (IREL)

The income derived by IREL is considered to be income of a trading nature attributable to a permanent establishment situated outside Malta. IREL may opt to claim the permanent establishment exemption (allocating the income to the FTA) or, alternatively,

allocate the income to the foreign income account. In the latter case, IREL should claim double tax relief for the 12% Irish tax, thereby resulting in an effective tax rate of 23% (35% less 12%) in Malta. A distribution of these profits to RPH would entitle RPH to a two-thirds tax refund of the advanced company income tax (i.e. 2/3 x 35% = 23·33%), limited in this case to the actual tax paid in Malta of 23%.

(b) Participation exemption on dividends paid by HKL to RPH

In order to claim the participation exemption on any divided paid by HKL to RPH, RPH's shareholding must constitute an equity shareholding. This means that RPH's shareholding must grant at least two out of the following three rights:

– rights to votes
– rights to profits, and
– rights to assets on winding up.

In the absence of any information to the contrary, it appears that this condition is met. The shareholding qualifies as a participating holding, since it grants RPH the right to appoint a director in HKL.

In the case of dividend income, prior to claiming the participation exemption, the holding must satisfy the following anti-abuse provisions:

– it is either resident or incorporated in the EU, or

– subject to a 15% foreign tax, or

– not more than 50% of its income is made up of passive interest and royalties which were taxed outside Malta at a rate lower than 5%.

Since none of these conditions is satisfied, the participation exemption will not be available, and RPH will allocate the HKL dividend to the foreign income account (FIA).

Depending on the type of double tax relief claimed by RPH, if any, Jessica Rossi would be entitled to tax refunds as follows:

(i) If RPH claims the flat rate foreign tax credit (FRFTC) provisions and assuming no expenses, RPH will pay tax at an effective rate of 18·75%. Jessica can claim a two-thirds tax refund, thereby reducing the effective Malta tax rate to 6·25%; or

(ii) If RPH does not claim any type of double tax relief, the company will be taxed at 35% on the income. Upon a distribution of dividends Jessica can claim a 5/7ths tax refund, thereby reducing the effective Malta tax rate to 10%; or

(iii) RPH can claim underlying tax relief for the 4% tax suffered, in which case Jessica would be able to claim a two-thirds refund of the advanced company income tax (2/3 x 35% = 23·33%). The effective tax rate through the operation of the two-thirds refund would be 7·67% (35% – 4% = 31% less a 23·33% tax refund = 7·67%).

Impact of setting up an intermediary Hong Kong holding company

If RPH holds its shares in HKL through an intermediary holding company in Hong Kong, the holding company would be the entity in receipt of the dividend paid by HKL. Since the new holding company would not be receiving any of its income from passive interest and royalties, the anti-abuse provisions will be satisfied, resulting in RPH being able to claim the participation exemption on any dividend paid to it by the new holding company.

(c) Participation exemption on disposal of investments by RPH

RPH can claim the participation exemption on the disposal of the shares held in its investments as long as such shareholding constitutes a participating holding, a condition which is satisfied since RPH holds more than 10% of the equity share capital in MTL, PLL and IREL and in the case of HKL, RPH's shareholding grants it a right to appoint a director.

In order to claim the participation exemption, such a holding cannot be in a property company. Any of RPH's investments would be considered to be a property company if it either:

– owns immovable property situated in Malta, or

– holds, directly or indirectly, shares or other interests in any entity, which owns immovable property situated in Malta and 5% or more of the total value of the shares or other interests held is attributable to the immovable property.

However, if a company carries on a business through such immovable property, consisting of a factory, showroom, warehouse or office used only for the purpose of carrying on such a business, the company is not treated as owning immovable property if:

– not more than 50% of the value of its assets consist of immovable property situated in Malta, and
– it does not carry on any activity the income from which is derived from immovable property situated in Malta.

Both IREL and HKL are not deemed to be property companies as they do not own any immovable property in Malta. Therefore, the participation exemption is available on any gain arising on the disposal of shares in these two companies.

In the case of a disposal of a participating holding, there is no requirement to satisfy the anti-abuse provisions. Therefore RPH would be able to claim the participation exemption on the sale of the shares in HKL irrespective of whether such shareholding is held directly or through a holding company.

However, MTL owns immovable property situated in Malta and although such immovable property is used in the course of its business, the factory accounts for more than 50% of the assets of the company. Therefore the participation exemption will not be available should RPH dispose of its holding in MTL. Similarly, RPH cannot avail itself of the participation exemption should it dispose of its shareholding in PLL since all of PLL's income arises directly from immovable property situated in Malta leading to PLL being considered a property company.

3 (a) (i) The importation of goods into Malta

Third country imports are deemed to take place where the goods are situated when customs duties become payable. Therefore, when goods are imported into Malta and customs duties are charged, the chargeable event is deemed to be in Malta and is subject to Maltese import VAT.

For intra community acquisitions (ICA) of goods, the chargeable event is deemed to take place where the goods are situated when the transport of the goods to the person acquiring them ends. Therefore, on the ICA of detergents to Malta:

– the supplier in the other member state would not have imposed any VAT on the intra community supply,

MDL is required to

– self-assess Maltese VAT on the purchase, and

– apply the reverse charge mechanism.

(ii) The supply of goods

As a company registered under Article 10, MDL is required to charge VAT on its taxable supplies with a right to claim a credit for any input VAT related to its taxable supplies. The place of supply of domestic supplies by MDL is in Malta irrespective of whether the goods are transported (transport starts in Malta) or picked up from MDL's warehouse (goods are in Malta when placed at disposal of the customer), therefore, Maltese VAT (18%) is applicable.

Where the place of supply is outside Malta, MDL would not charge any Maltese VAT on its supplies.

The supply of goods with transport to taxable customers established in other EU member states is an intra community supply (ICS) of goods with transport and is deemed to take place where the transport starts, in this case Malta. ICSs are zero rated and MDL would shift the responsibility to account for and pay VAT to the taxable person established in the other EU country.

Exports of goods to customers outside the EU are also supplies of goods with transport deemed to take place where the transport starts (in the case of MDL, Malta) and are also exempt with credit for Maltese VAT purposes.

(b) The place of supply of sales to non-VAT registered customers in Italy

The supply of goods with transport by MDL to the final customers in Italy is normally (in terms of the general supply of goods rules) deemed to take place where the transport begins. However, as MDL's customers are not VAT registered in Italy, the place of supply of the detergents and the applicable VAT treatment will depend on the following factors:

– If the total value of sales of goods transported to Italy during the year exceeds the Italian distance sales threshold (€35,000), then the place of supply would be in Italy and MDL would be required to obtain an Italian VAT registration and charge Italian VAT on the supplies.

– If the €35,000 threshold is not exceeded, as in this case, the place of supply will remain where the transport starts (i.e. Malta) and Maltese VAT at 18% applies, unless MDL voluntarily opts for an Italian VAT registration and charges Italian VAT on the supplies.

(c) Taxable value in terms of Maltese VAT provisions

The Maltese VAT Act provides that the 'taxable value' (i.e. the value on which VAT is chargeable) must include

– any taxes and duties (excluding VAT) payable by reason of the supply; and

– incidental expenses, such as commissions, packing, transport and insurance cost;

and exclude

– discounts for early payment and quantity discounts;

– penalties and interests charged for late payment;

– disbursements paid in the name and for the account of the person to whom the supply is made, and resulting from documents held by the supplier, which are recorded in a suspense account; and

– any amount charged to the customer by way of a deposit on returnable packing of goods where the deposit is lower than the cost of the packing.

MDL will be liable to pay VAT on the cost of the goods, transport cost to Malta and import duties imposed by the Maltese customs authorities.

MDL should exclude from the taxable value of its supplies all discounts provided to its customers, the deposit payable on the returnable packaging and any interest/charges imposed for late payment of invoices.

(d) MDL's VAT return – October to December 2018

Transaction type	Taxable amount €	VAT due in Malta €	
Output VAT			
Domestic supplies (300,000 – 15,000 – 35,000)	250,000	45,000	
Deposit on containers	0	0	
Late payment penalties/interest	0	0	
Intra community supplies	80,000	0	
Exports	24,000	0	
Supplies to non-VAT registered clients in Italy	30,000	5,400	
Intra community acquisitions	75,000	13,500	
Transport by EU taxable persons	25,000	4,500	
Total output VAT			68,400
Input VAT			
Imports from outside EU (70,000 + 20,000 + 10,000)	100,000	18,000	
ICA	75,000	13,500	
Transport cost on ICA	25,000	4,500	
Total input VAT			36,000
VAT due			32,400

4 (a) Intra group transfer of losses between SCL and SPL

(i) Group definition for intra group transfer of tax losses

In order to transfer tax losses between companies, they must be part of a group of companies.

Two companies are deemed to be a group of companies if:

– they are resident in Malta but not resident for tax purposes in any other country, and

– either one owns more than 50% of other company's share capital, voting rights, rights to profits and rights to assets on winding up, or

– a third company resident in Malta holds more than 50% of these rights in the two Maltese tax resident companies.

Since SCL is fully owned by SPL, they are considered to be a group of companies and tax losses can be transferred between the two companies.

(ii) Utilisation of intra group tax losses between tax accounts

Although it is possible to transfer intra group losses irrespective of the tax account to which they would have been allocated, the claimant company is restricted from utilising trade losses which, had they been profits, would have been allocated to the MTA, IPA and FIA tax accounts, as follows.

Where the trade loss of the surrendering company relates to:

– either IPA or MTA sources of income, the claimant company may only deduct the loss from its total income in its IPA and/or MTA tax accounts (i.e. an MTA loss transferred by the surrendering company can only be deducted from the claimant company's MTA or IPA account or both, and vice versa).

– FIA sources of income, the claimant company may only deduct the loss from its total income allocated to its FIA tax account.

Since SCL's income will be allocated to the IPA, losses arising can only be set off against any income allocated to SPL's IPA or MTA tax accounts, but not against SPL's income arising from the disposal of immovable property situated in Portugal which is allocated to its FIA, or against the income arising from transfers of immovable property subject to the property transfer tax, which is allocated to the FTA.

(iii) Limitation to deductions in the case of services provided to related persons

Income derived from construction work carried out on immovable property situated in Malta which is owned by a related person is treated as a separate source of chargeable income.

Two companies are considered to be related if more than 25% is directly or indirectly controlled or beneficially owned by the same persons. Accordingly, SCL and SPL are considered to be related persons.

When determining the separate chargeable income derived from immovable property services provided to the related person, the total deductions allowed cannot exceed the amount of the consideration received or receivable for that work.

Therefore, SCL is required to prepare two separate tax computations which clearly distinguish between the income generated from transactions with non-related persons and the income derived from the transactions with SPL. In the latter case, the total deductions allowed cannot exceed the total consideration received from the services rendered to SPL. Any excess expenses over income in this situation are not considered to be a trade loss. Therefore SCL's loss arising from the transactions with SPL cannot be set off against its own income arising from transactions with unrelated parties, nor can it be transferred to SPL to be set off against SPL's income.

SCL may only transfer to SPL the trade losses arising from the transactions with unrelated parties. These losses can then be set off against SPL's income from the transfers of rights acquired through the promise of sales agreements and which is allocated to the IPA.

(b) SCL's computation of chargeable income – year of assessment 2018

	Construction and finishing services to SPL	Property development services to unrelated persons
	€	€
Profit before tax	(330,000)	(20,000)
Add back:		
Inventory shown at lower of cost and NRV	0	
Depreciation of plant and equipment	25,000	
Advertising and promotion	0	
Unrealised currency exchange losses	2,000	
Administrative penalty for late filing of VAT returns	1,000	
Interest charged by the VAT Department for late payment	0	
Charitable donations	1,000	
Casual labour not reported under the FSS rules	8,000	
Motor vehicle running expenses	0	
Expenses not supported by valid tax invoice	3,000	
Non-commercial motor vehicle lease disallowed portion (8,000 – (14,000/28,000 x 8,000)	4,000	
Provision for obsolete inventory		1,500
Specific provision for impaired debts		1,500
General provision for impaired debts		3,000
Irrecoverable debts		0
Chargeable income/losses before capital allowances	(286,000)	(14,000)
Loss disallowed due to provision of immovable property services to SPL	286,000	0
Tax loss for the year (IPA) which can be transferred to SPL	0	(14,000)

Wear and tear allowances for the year – all carried forward

Commercial motor vehicles (50,000/5)	10,000
Computer equipment (8,000/4)	2,000
Plant (100,000/10)	10,000
	22,000

5 (a) The basis of Jack's tax liability in Malta

Should Jack Osprey decide to retire in Malta, he would be considered a Maltese resident individual for tax purposes but as he does not wish to reside in Malta permanently, he is not expected to acquire Maltese domicile. Accordingly, he will be taxable in Malta on a remittance basis, on any Malta source income and on foreign source income remitted to Malta but not on foreign source capital gains.

As Australia will also consider Jack to be an Australian tax resident, the tie breaker clause in Article 4 of the treaty will need to be invoked to establish his country of residence. The first test requires that one identifies the country where his permanent home is situated. It appears that Jack will acquire a permanent home in Malta but will also maintain his present home in Australia. In such a case, one needs to establish his centre of vital interests. Although he will keep his social interests in Australia, it is clear that his family interests will be in Malta since his wife will be in Malta and his children in law are in Malta, albeit adult children do not have a significant bearing on the central of vital interests. In such a case, the family interests are to be given more importance than the economic and social factors, clearly indicating that Jack should be considered a Maltese tax resident for the purposes of the treaty.

Under the terms of the treaty, Jack's retirement pension from Australia will be taxable only in Malta as his country of residence. Australia is prohibited from taxing the pension income. On the other hand, the rental income derived from the Australian property may be taxed in Australia. Malta may also tax such rental income but is required to grant double tax relief for the tax paid in Australia.

(b) Applicability of a special tax programme

The decision as to whether Jack will opt for the pension commutation option or not will determine whether he should opt for the global residence programme (GRP) or become a Maltese tax resident without opting for any special scheme. Note that, although Jack's main income will be a pension income, the Malta retirement programme is not available to him as it is only applicable to EU and EEA nationals.

If Jack opts for the pension commutation, his expected income will be €6,500 (€4,000 pension and €2,500 rental income) per month or €78,000 per annum. The associated tax at the progressive married tax rates, after double tax relief, would be €14,395 (W1).

If Jack opts for the GRP, he would still be required to pay the minimum annual tax of €15,000 (after double tax relief), meaning that the GRP would result in a higher tax liability.

Note that, under both options, Jack will be able to claim full credit for the 10% Australian withholding tax on the rental income since the effective Malta tax on the Australian rent would exceed 10% in both cases.

If Jack does not opt for the pension commutation, his expected annual income will be €114,000 (€7,000 pension and €2,500 rent per month). The associated tax would be €26,995 (after double tax relief) at the progressive married tax rates (W2).

The tax (after double tax relief) payable under the GRP would still amount to €15,000 (W3) since this is the minimum annual amount payable under the GRP. Therefore the GRP programme is the better option only if the pension commutation is not taken.

In order to qualify for the GRP, Jack must satisfy the following conditions. He must:

- not be a permanent resident of Malta;
- not be an EU, Swiss or EEA national;
- not benefit from the Residents Scheme Regulations, the High Net Worth Individuals Rules, the Malta Retirement Programme Rules, the Residence Programme Rules, or the Highly Qualified Persons Rules;
- hold a qualifying property holding, which includes property in Malta acquired for a minimum value of €275,000. Furthermore, the only people who may live in the qualifying property are the beneficiary, his wife, any adopted child and any household staff who have been in an employment relationship with the beneficiary for at least the last two years;
- be in receipt of stable and regular resources which are sufficient to maintain himself and his dependants without recourse to the social assistance system in Malta;
- be in possession of a valid travel document;
- be in possession of sickness insurance in respect of all risks across the whole of the EU normally covered for Maltese nationals for himself and his dependants;
- be able to communicate adequately in one of the official languages of Malta;
- be a fit and proper person.

SIX ONLY required.

Workings

(W1) Commutation option – *de facto* tax residence

	€
Annual pension (4,000 x 12)	48,000
Annual rent (2,500 x 12)	30,000
Total	78,000
Tax thereon at the married rates	17,395
10% Australian withholding tax (30,000 x 10%)	(3,000)
Tax due	14,395

(W2) No commutation option – *de facto* tax residence

	€
Annual pension (7,000 x 12)	84,000
Annual rent (as above)	30,000
Total	114,000
Tax thereon at married rates	29,995
10% Australian withholding tax	(3,000)
Tax due	26,995

(W3) **No commutation option – global residence programme**

	€
Total foreign income	114,000
Tax at 15%	17,100
10% Australian withholding tax	(3,000)
Tax due	14,100
Minimum tax due on foreign income	15,000

(c) Pension commutation tax treatment

If the pension commutation were to occur after Jack becomes a Maltese tax resident, the commutation would be exempt from tax in Malta since it does not exceed 30% of the total pension amount.

(d) Acquiring a Maltese nationality

Jack must be aware that, should he decide to apply for and become a Maltese citizen, he will be required to renounce all benefits in terms of the GRP since the programme is not available to Maltese nationals, so the 15% flat tax on foreign source income would no longer apply. Jack would then be taxable in Malta on a remittance basis at the progressive rates (as long as he does not acquire a Maltese domicile).

				Available	*Maximum*
1	**(a)**	**(i)**	**Income tax treatment of the rental income derived by MPL**		
			Differentiate between the tax treatment of passive rental income and rental income of a trading nature	1·0	
			Allowed deductions in the case of passive rental income	1·5	
			15% tax option on gross rent	0·5	
			All in vs all out	0·5	
			Inapplicability of final tax option to rent derived from related parties	1·0	
				4·5	4·0
		(ii)	**Calculation of the tax due**		
			Opt out of the 15% final tax option		
			Deduction of ground rent	1·0	
			20% Further deduction	1·0	
			20% Further deduction not available in the case of trading income	1·0	
			Deduction of other expenses only in the case of trading income	1·0	
			Interest deduction	1·0	
			Utilisation of trade losses against any of the passive rental income (in calculation)	0·5	
			15% final tax option		
			Calculation of the 15% final tax	1·0	
			Not available on Valletta property, tax calculated using 20% further deduction	1·0	
			Comparison of the available options and identification of best option	1·0	
			Utilisation of trade losses (explained in words)	0·5	
				9·0	8·0
	(b)	**(i)**	**VAT treatment of the rental/property lease income derived by MPL**		
			Property leases – exempt without credit	1·0	
			Exceptions:		
			Provision of accommodation and identify treatment for Gzira, Bugibba and Birkirkara properties, distinguishing between the MTTA accommodation (Bugibba) and exempt residential leases (Gzira and Birkirkara)	1·5	
			Commercial property and distinguishing between the property leases to Art 10 lessees (Valletta and Gozo) and Art 11 lessees (Sliema)	1·5	
				4·0	3·0
		(ii)	**Right to claim back input VAT**		
			Right to claim back input VAT related to taxable supplies	0·5	
			No right to claim back input VAT related to exempt without credit supplies	0·5	
			Partial attribution rules explanation	2·0	
				3·0	3·0
		(iii)	**Calculations**		
			Calculation of output VAT on Gozo, Sliema and Bugibba properties (0·5 x 3)	1·5	
			Calculation of input VAT on supplies related to Gozo, Sliema and Bugibba properties (0·5 x 3)	1·5	
			Calculation of partial attribution percentage and the VAT claimable on general overheads	2·0	
			Calculation of definitive ratio adjustment	1·0	
				6·0	5·0

		Available	*Maximum*
(c)	**Property transfer tax and duty on documents applicable on the transfer of the Valletta commercial property**		
	Option A – Default 8% final tax on transfer value, increased to 10% since property acquired before 1 January 2004	1·5	
	Option B – Transfer to FSL intra group transfer – exempt from property transfer tax and duty on documents	0·5	
	Owned directly by the same shareholders (ignoring shareholders less than 20%) and each shareholder holding the same percentage of share capital and voting rights in both companies, allowing a maximum 20% variation	2·0	
	No property transfer tax and duty on documents on transfer of Valletta property during liquidation as held as a capital asset for more than five years and CR held 95% or more of the share capital for more than five years	2·0	
	Option C – Same initial repercussions as Option B		
	Upon conversion of FSL into a partnership reference to option for tax treatment as transparent or opaque	1·0	
	Transparent treatment leading to degrouping charge if happening within six years – 10% on transfer value. Degrouping charge has no stamp duty repercussions	1·5	
	Recommendation with reasons	0·5	
		9·0	8·0
Presentation:			
Appropriate format of letter		1·0	
Logical development		1·0	
Effectiveness of communication		2·0	
		4·0	4·0
			35

			Available	*Maximum*
2	**(a)**	**Malta tax treatment of the income derived by Malta Trade Ltd, Property Lease Limited and International Real Estate Limited**		
		RPH, MTL and IREL resident and domiciled in Malta, taxable on a worldwide basis	0·5	
		MTL's income initially allocated to the MTA	0·5	
		IPA allocation of the annual market rent €250/m^2	1·5	
		Analysis of whether any of the other companies is related for the purpose of excess secondary allocation – no relationship and therefore MTL required to carry forward the shortfall	2·0	
		MTA 6/7ths refund, no refund on IPA dividends	1·0	
		PLL subject to tax in Malta on a source basis	0·5	
		15% Final tax versus 35% tax with loan interest and 20% further deduction	1·5	
		No refunds on FTA and IPA dividends	0·5	
		IREL's income qualifies for the permanent establishment exemption with reason	1·0	
		Option to allocate income to FIA and claim a 2/3rds refund of the 35% ACIT which would result in a full refund of Malta tax paid since the foreign tax to be relieved exceeds the 1/3rd of the tax on the profit	2·0	
			11·0	10·0
	(b)	**Participation exemption on dividend income from HKL**		
		Equity shareholding: two out three rights	1·5	
		To meet anti-abuse provisions (0·5 x 3) + none met	2·0	
		Three options:		
		– FRFTC – 6·25% tax leakage	1·0	
		– No DTR – 10% effective tax	1·0	
		– Double tax relief for the underlying tax, 7·67% leakage	1·0	
		Interposition of dividend feeder would reclassify the passive interest into dividend income thereby meeting one of the anti-abuse provisions and resulting in the availability of the participation exemption	1·5	
			8·0	7·0
	(c)	**Participation exemption on disposal of investments**		
		All investments constitute a PH – 10% in MTL, PLL and IREL and right to appoint a director in HKL	1·0	
		Property company – not possible to claim participation exemption	0·5	
		Definition of a property company, including proviso	3·0	
		IREL and HKL not property companies	1·0	
		HKL – anti abuse provisions do not need to be met therefore no benefit in interposing a holding company	1·0	
		MTL is a property company – although its uses the property in the course of its business it accounts for more than 50% of its total assets; PE not available	2·0	
		PLL is a property company	0·5	
			9·0	8·0
				25

				Available	Maximum
3	(a)	(i)	**The importation of goods into Malta**		
			The place of supply of the importation of goods – where the goods are when the customs duties become payable	1·0	
			MDL to pay import VAT on goods imported from third countries	0·5	
			The place of supply of ICA of goods is where the goods are when the transport of the goods to the person acquiring them ends	1·0	
			Reverse charge obligations	1·0	
		(ii)	**The supply of goods**		
			Registered in terms of Article 10, and therefore required to charge VAT on taxable supplies with a right to claim a credit for any input VAT related to taxable supplies	1·0	
			Domestic supplies subject to 18% VAT	0·5	
			ICS deemed to take place in Malta where transport starts but zero rated, exports also exempt with credit	2·0	
				7·0	6·0
	(b)		**Distance sales rules**		
			Supply of goods with transport to the final customers in Italy is, in terms of the general supply of goods rules deemed to take place where the transport begins	1·0	
			If threshold exceeded, place of supply shifted to Italy – required to register for, charge and account for VAT in Italy	1·0	
			If threshold not exceeded, option to remain subject to Maltese 18% VAT or register for VAT In Italy and charge VAT on all supplies to customers in Italy	1·5	
				3·5	3·0
	(c)		**Taxable value in terms of Maltese VAT provisions**		
			Includes any taxes and duties (excluding VAT) payable by reason of the supply and incidental expenses, such as commissions, packing, transport and insurance cost	1·0	
			Excluded from the taxable value discounts for early payment and quantity discounts, penalties and interests charged for late payment, disbursements, deposit on returnable packing of goods	2·0	
			Upon the importation of the goods from outside of the EU, MDL will be liable to pay VAT on the cost of the goods, transport cost to Malta and import duties imposed by the Maltese customs authorities	1·5	
			Note to markers: *These marks are for application to the facts of the question*		
			Exclude from its taxable value all discounts provided to its customers, the deposit payable on the returnable packaging and any interest/charges imposed for late payment of invoices	1·5	
			Note to markers: *These marks are for application to the facts of the question*		
				6·0	5·0
	(d)		**Calculation of VAT due**		
			Calculation of output VAT on domestic supplies, excluding VAT on container deposits and penalties/interest	1·0	
			No VAT on deposits, late payment penalties/interest, ICS or exports	2·0	
			18% VAT on sales to individuals in Italy	0·5	
			18% VAT on imports	0·5	
			Reverse charge for ICA and transport costs	2·0	
				6·0	6·0
					20

			Available	Maximum
4	(a)	**Intra group transfer of losses between SCL and SPL**		
		(i) Group definition for trade loss transfer purposes	2·0	2·0
		(ii) MTA and IPA losses of surrenderer may be offset only against MTA/IPA of claimant	1·0	
		FIA losses of surrenderer company may be offset only against FIA of claimant	1·0	
		SPL will allocate income from Portugal property disposal to FIA and therefore no SCL trade losses may be used against such income	1·0	
			3·0	3·0
		(iii) Work carried out with respect to immovable property situated in Malta owned by a related person is considered to constitute separate source of chargeable income	1·0	
		Related persons = 25% + common ownership	1·0	
		The total deductions allowable cannot exceed the amount of the consideration received or receivable for work on immovable property provided to related person. Any SCL trade loss arising from the transactions with SPL to be added back as a disallowed expense	1·5	
		Only loss from transactions with unrelated parties may be transferred to SPL to be set off against SPL's income from the transfers of rights acquired through the promise of sales agreements	1·5	
			5·0	5·0
	(b)	**Computation of chargeable income**		
		Add back: (0·5 each)	5·5	
		Inventory shown at lower of cost and NRV		
		Depreciation of plant and equipment		
		Unrealised currency exchange losses		
		Administrative penalty for late filing of VAT returns		
		Charitable donations		
		Casual labour not reported under the FSS rules		
		Expenses not supported by valid tax invoice		
		Non-commercial motor vehicle lease disallowed portion		
		Provision for obsolete inventory		
		Specific provision for impaired debts		
		General provision for impaired debts		
		No add back: (0·5 provided none added back)	1·0	
		Accountancy and audit fees		
		Motor vehicle running expenses		
		Interest charged by the VAT Department for late payment		
		Irrecoverable debts		
		Separate calculation of loss on services to unrelated persons	1·0	
		Loss disallowed due to immovable property services being provided to SPL	1·0	
		Wear and tear allowances for the year and c/f	1·5	
			10·0	10·0
				20

			Available	*Maximum*
5	**(a)**	**The basis of tax liability in Malta and the respective taxing rights of Malta and Australia**		
		Resident not domiciled – taxable on a remittance basis	1·0	
		Invoke tie breaker rules	0·5	
		Permanent home in both countries	1·0	
		Centre of vital interest – family connections with examples, more important than economic therefore resident for treaty purposes in Malta	1·5	
		Taxation of pension income exclusively in Malta as the residence country	1·0	
		Australia cannot tax pension	0·5	
		Rental income may be taxed by Australia	0·5	
		Malta may tax rental income and must grant double tax relief	1·0	
			7·0	5·0
	(b)	**Special scheme**		
		Options available: global residence programme v factual tax residence	1·0	
		Malta retirement programme not available since Jack is not an EU/EEA/Swiss national	1·0	
		Calculation of taxable income and tax charge before double tax relief under both options with and without commutation (1 mark x 3)	3·0	
		Double tax relief including comments on how Australian tax is below the Maltese effective tax charge allowing a full credit for the Australian withholding tax	1·0	
		GRP minimum tax payable in any case	1·0	
		Conditions to abide with to qualify for GRP (6 conditions x 1 mark)	6·0	
			13·0	13·0
	(c)	Pension commutation 30% exempt	1·0	1·0
	(d)	Maltese citizenship would lead to automatic disqualification of GRP status and taxable on remittance basis	1·0	1·0
				20