# Answers

**1** Notes for the meeting with Otto Fibonacci (OF)

Prepared for: Tax Manager
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**(a)** Impact of the Controlled Foreign Company ('CFC') rules on South American Hotels Ltd (SAH)

Under the CFC anti-abuse rules, SAH is required to tax its relevant share of any undistributed profits derived by any non-Maltese resident company under its control (hereinafter referred to as a CFC) where the actual corporate tax paid by the CFC on its profit is lower than the difference between:

**(i)** the tax that would have been charged on the CFC under the Malta Income Tax Acts; and

**(ii)** the actual overseas corporate tax paid on its profits by the CFC.

The CFC anti-abuse provisions are limited to profits arising from non-genuine arrangements which have been put in place for the essential purpose of obtaining a tax advantage. A non-genuine arrangement being defined under the rules as one where the significant people functions generating the income of the CFC are carried out in Malta rather than in the relevant local territory.

In addition, the CFC anti-abuse provisions specifically only apply if certain *de minimis* thresholds are exceeded, namely:

– The accounting profits of the CFC exceed €750,000 and its non-trading income exceeds €75,000; or

– The CFC's accounting profits exceed 10% of its operating costs for the tax period.

Rio de Janeiro Ltd (RdJ) is potentially treated as SAH's CFC as SAH owns more than 50% of the voting rights or capital or rights to receive the profits of RdJ.

However, the tax rate paid by RdJ on its accounting profit amounts to 25%, whereas the difference between the Brazilian tax rate (25%) and the Maltese corporate tax rate (35%) is 10%. In this respect, since:

– the Brazilian corporate tax rate imposed on RdJ is higher than the difference between the two countries' tax rate; and

– it appears that the significant people functions of RdJ are in Brazil and not in Malta due to the fact that RdJ employs 40 key employees in Brazil; and

– RdJ accounting profits are less than €750,000 and it has no non-trading income;

RdJ should not be considered to be a CFC in terms of Malta's transposition of ATAD into Maltese tax law.

Moreover, even if RdJ were to be considered a CFC of SAH, since RdJ distributed as a dividend to SAH all its profits for the year, the CFC provisions would not result in any additional chargeable income being assessed on SAH in respect of 2019.

**(b) (i)** Applicability of the Consolidated Group Rules (CGR) to the Maltese companies.

Under the CGR, companies which are closely related are entitled to file one tax return and pay taxes as one unit covering all the entities within the CGR rather than having to file separate tax returns. In order to be eligible to apply to form a CGR, all companies within the fiscal unit must have the same accounting period end.

Companies may form a fiscal unit if the parent is registered in Malta and holds at least 95% of at least two of the following rights in the relevant subsidiary company:

(i) voting rights;

(ii) rights to profits available for distribution; and

(iii) rights to any assets available for distribution on a winding up.

If the subsidiary is not a 100% subsidiary, approval must be obtained from the other shareholder(s) in order to apply to be treated as a fiscal unit.

Therefore, Mdina Boutique Hotels Ltd (MBH) as the parent company, can opt to create a fiscal unit with RB since MBH owns at least 95% of RB. However, MBH cannot include SAH within the fiscal unit, since it does not hold the minimum 95% shareholding therein. SAH will therefore continue to be taxed as a standalone entity.

**(ii)** Malta tax consequences arising upon the creation of the fiscal unit

When MBH and RB elect to be treated as a fiscal unit, the following tax implications will arise:

– Any income or loss derived by RB will be computed and brought to tax in MBH's hands as the principal taxpayer of the fiscal unit. RB will be treated as a transparent entity and all its income will be deemed to be received by MBH as the principal taxpayer.

– Any tax balances within RB (as the transparent subsidiary), such as trade losses, wear and tear allowances, tax credits brought forward and the balances in the tax accounts (with the exception of the untaxed account) will be considered to be balances of the principal taxpayer, MBH.

– Any transactions (apart from dividend income arising out of profits derived by RB prior to joining the fiscal unit, and transactions subject to tax under the property transfer tax rules) between RB and MBH are ignored for tax purposes. Therefore, the dividend paid by RB to MBH in 2019 would not be treated as income of MBH if the entities are part of the same fiscal unit.

– The income derived by the fiscal unit is brought to tax at the applicable 35% tax rate. However, as MBH is entitled to tax refunds, the tax refund is taken into consideration when determining the applicable tax rate of the fiscal unit. This is achieved by deducting the applicable refund rate from the 35% tax rate on the consolidated chargeable income of the fiscal unit, resulting in the same effective tax rate.

– MBH is required to prepare a consolidated profit and loss account and a consolidated balance sheet for all companies in the fiscal unit for each fiscal year.

– The obligation to file a tax return for the fiscal unit sits with MBH, and RB is exempt from the requirement to file a separate tax return.

– The tax payable will be charged in the name of MBH as the principal taxpayer. However, RB as a 100% subsidiary remains jointly & severally liable for the payment of tax.

**(c) Maltese tax treatment of income derived by MBH, RB, SAH and OF**

SAH, MBH and RB are incorporated and managed and controlled in Malta and therefore taxable in Malta on their worldwide income. MDH and RB are subject to tax as one fiscal unit, whereas SAH is taxed in Malta as a standalone entity.

**Tax treatment of income of SAH**

Upon a distribution of profits by RdJ, SAH may avail itself of the participation exemption applicable to income from a participating holding. This is because SAH's 100% shareholding in RdJ is considered to be an equity shareholding, since, as a minimum, it entitles SAH to two out of three equity shareholding rights, namely rights to profits and rights to vote. SAH's equity shareholding is also considered to be a participating holding given it holds more than 5% of RdJ's share capital. In order for dividend income to qualify for the participation exemption, RdJ must also satisfy one of the following anti-abuse conditions:

(1) The shareholding is in a company resident or incorporated in the European Union (EU); or

(2) The dividend is subject to any foreign tax at a rate of at least 15%; or

(3) The shareholding is in a company that does not derive more than 50% of its income from passive interest or royalties.

Since RdJ has been subject to a corporate tax of 25% plus a withholding tax of 10% (and does not derive more than 50% of its income from passive interest and royalties), the anti-abuse provisions are satisfied. Therefore, SAH's dividend will be exempt from tax in Malta in terms of the participation exemption and allocated to the Untaxed Account.

**Tax treatment of income of the MBH and RB fiscal unit**

The fiscal unit receives a dividend of all of SAH's profits for 2019 being its dividend income from RdJ. As noted above, this exempt dividend is allocated to SAH's Untaxed Account and upon a dividend distribution to the fiscal unit, the fiscal unit will remain exempt from tax on such a dividend.

The trading income derived by the fiscal unit through RB's commission income is taxable in Malta at the normal rate of 35% and is allocated to the Maltese Taxed Account since it is not attributable to any permanent establishment outside of Malta or derived directly or indirectly from the provision of accommodation in Malta. The distribution of such income would grant MBH the right to claim a 6/7ths tax refund. The impact of this on the effective rate applied to the RB and MBH fiscal unit should be taken into account by reducing the fiscal unit's tax charge on such income from 35% to 5% (1/7th x 35%).

MBH's trading income, on the other hand, is derived exclusively from commission income which is directly related to immovable property situated in Malta. Such trading income is taxed at 35% and is allocated to the Immovable Property Account.

**Tax treatment of dividends in the hands of Otto Fibonacci (OF)**

As the dividend received by OF from MBH is in respect of the commission income allocated to the Immovable Property Account, this is not subject to further tax in his hands, nor is he entitled to any tax refund in respect of the dividend.

**Calculation of the tax payable by the fiscal unit and tax accounts allocation**

**Tax calculation of the MBH-RB fiscal unit**

| | Untaxed Account (€) | Maltese Taxed Account (MTA) (€) | Immovable Property Account (IPA) (€) |
|---|---|---|---|
| Dividend from SAH | 140,000 | | |
| RB's trading income | | 1,000,000 | |
| MBH's estate agency fees | | | 2,000,000 |
| Tax rate to be applied (W1) | 0 | 5% | 35% |
| Tax thereon | 0 | 50,000 | 700,000 |

**Working 1 – Calculation of tax rate to be applied in terms of the CGR**

| | | |
|---|---|---|
| Chargeable income (MTA & IPA) | 1,000,000 | 2,000,000 |
| Tax refund entitlement | 300,000 | 0 |
| Standard tax rate | 35% | 35% |
| Tax rate reduction (300,000/1,000,000) | 30% | 0 |
| Tax rate to be applied | 5% | 35% |

**2 (a) The income tax and duty on documents implications of the two options for Robert's and Amanda's exit from Cannot Sing a Note Ltd (CSNL)**

**Option A**

**Income tax**

A resident individual making a transfer of shares is subject to tax in Malta on any capital gains made. Since neither Robert nor Amanda hold 25% or more of CSNL's nominal share capital, voting rights and rights to profits, and their shareholding does not entitle either of them to appoint a director, both share transfers are not considered to be transfers of a controlling interest. This means that the transfer value is deemed to be equal to the consideration received and the market value of their shares can be ignored.

Robert and Amanda are allowed a deduction for the cost of acquisition of the shares. However, no deduction by way of an inflation allowances is allowed since the transfer is not a transfer of a controlling interest and the shares were acquired after 25 November 1992.

**Duty on documents**

Transfers of securities are subject to duty on documents at the rate of €2 per €100 increasing to €5 per €100 where the non-current assets of the company in which the transfer is made consist of 75% or more of immovable property situated in Malta. In CSNL's case, since the only non-current asset owned by the company consists of the studio in Malta, a duty rate of €5 per €100 will apply.

This duty rate is applied to the higher of the consideration and the real value of the shares, irrespective of the percentage of shares held by the transferor.

Real value is calculated based on the net asset value of the company but with the book values adjusted for goodwill which is calculated as two years average profits over the last five years. In addition, the book value of any immovable property is replaced by the market value thereof as per an architect's valuation. The tax provisions include further adjusting items being a deduction for the book value of preference shares and a replacement of the book value of any investment (10% or higher) by the market value thereof, although such elements are unlikely to be relevant to CSNL.

Additionally, any excess of liabilities (excluding bank loans and loans with publicly registered security) over assets (excluding immovable property) will require an upwards adjustment to the real value calculation. The effect of this is to ensure that the amount to which duty is applied is not less than the market value of the immovable property (being €700,000 in the case of CSNL) notwithstanding a company's net current liability position.

**Option B**

The income tax and duty on documents implications of each of the proposed steps have been considered in turn:

**Step 1**

The set-up of a new company owned 50% by Irina and Harry, will not give rise to any income tax or stamp duty.

**Step 2**

The asset transfers from CSNL to Newco are by default subject to:

– A charge to CSNL in respect of property transfer tax calculated at 8% of the transfer value of the studio (being the higher of the consideration of €600,000 and the market value of €700,000); and

– Corporate income tax payable by CSNL at 35% on any capital gain arising on the transfer of the business and goodwill to Newco.

However, both transfers, can potentially benefit from an exemption applicable in the case of transfers of assets between companies forming part of the same group.

**Income tax**

In the case of the business and goodwill transfer, it is sufficient for CSNL and Newco to be more than 50% owned by the same shareholders. Since Irina and Harry own 70% of CSNL and will own 100% of Newco, this condition is satisfied. Therefore, any gain arising on the intangible asset transfer is exempt from income tax.

**Property transfer tax**

The transfer of the studio would qualify from an intra group exemption from the property transfer tax if, in addition to satisfying the conditions applicable for the intellectual assets transfer:

(1) Each shareholder owns proportionately the same percentage of nominal share capital and voting rights in both companies, allowing a maximum variation in such holdings of 20% per shareholder.

Applying this to the scenario, since the difference in shareholding between the two companies will be 15% per shareholder (each shareholder holds 15% more or 15% less in CSNL as compared to the respective shareholding in Newco), this condition is satisfied.

and

(2) CSNL and Newco are owned directly or indirectly by the same shareholders. This provision allows a shareholder which holds less than 20% in only one of the two companies to be ignored. However, if there is more than one shareholder which holds less than 20% and when combined such shareholders exceed the 20% threshold, then each such shareholder must be taken into consideration when establishing if the same shareholders test is satisfied.

Applying this to our scenario, although Robert and Amanda individually hold less than 20% each of the shares in CSNL, their combined shareholding (30%) exceeds the 20% threshold and therefore Robert and Amanda must be taken into account when determining if this test is met. Since Robert and Amanda do not own any shares in Newco, this condition is not met and therefore the intra group exemption will not be available and the transfer is subject to the 8% property transfer tax.

Duty on documents

Transfers of businesses and goodwill are outside the scope of stamp duty and therefore, no duty on documents will be due on the transfer of such intangible assets. A stamp duty of €5 for every €100 will be due on the transfer of the immovable property since the conditions for the exemption from duty on the transfers between companies of the same group are not satisfied for the same reasons as for the property transfer tax.

**(b) Income tax due by Robert and Amanda under Option A**

As per the working below, Robert and Amanda will each pay capital gains tax of €21,000 as follows:

– €5,250 payable on the date of transfer (representing 7% provisional capital gains on the consideration €75,000 x 7% ), and

– €15,750 (representing the balance of the tax due on the transfer) payable by 30 June 2021, the due date of the tax return for year of assessment 2021.

Working – capital gains tax

| | |
|---|---|
| Transfer value equal to consideration (15,000 shares x €5) | €75,000 |
| Cost of acquisition (15,000 shares x €1) | (€15,000) |
| Capital Gain | €60,000 |
| Tax thereon at 35% | €21,000 |

**(c) The tax consequences of a distribution of profits upon exit under Option B**

CSNL's reserves prior to liquidation are assumed to consist of the gain from the transfer of the business and the goodwill (the intangibles) and the gain on the transfer of the studio.

The gain from the transfer of the intangibles will be exempt from income tax within CSNL (refer to part (a)) and thus will be allocated to the Untaxed Account. A dividend distribution from the Untaxed Account to the four shareholders will require CSNL to withhold 15% tax from the dividend payments. This tax must be paid to the tax authorities by the 14th day following the end of the month in which the dividend was paid – being 14 January 2021.

The transfer of the studio will be subject to a property transfer tax of €56,000 (€700,000 x 8%). The profit after tax arising from the transfer is allocated to the Final Tax Account and no further tax is due upon the distribution of such profits to the shareholders.

**3 (a) Value added tax (VAT) treatment of the supplies of Freya Abela (FA)**

For VAT purposes, leases of immovable property are deemed to take place where the immovable property is situated, in this case Malta. Transfers of immovable property are deemed to take place where the property is situated since they are a supply of goods without transport.

Since immovable property transfers are exempt without credit, FA will not be required to account for VAT on the sale of Apartment 1.

Leases of immovable property are generally treated as exempt without credit for Maltese VAT purposes. However, there is an exception where the lease is executed by a limited liability company to a person who is registered for VAT purposes in terms of Article 10 of the VAT Act. In this case, the supply is subject to VAT at the standard VAT rate of 18%. Given that FA will lease out the office in her personal name, irrespective of whether the lessee is VAT registered under Article 10 or Article 12 of the VAT Act, the lease will be treated as exempt without credit for Maltese VAT purposes.

The provision of accommodation to tourists is a taxable supply, subject to a reduced VAT rate of 7%. Therefore, VAT at 7% should be charged on the rent of Apartment 2.

**(b) FA's obligation to register for VAT purposes in Malta**

FA is established and resident in Malta and therefore she is required to register for VAT purposes in Malta within 30 days from the first taxable supply. Given that the provision of accommodation is deemed to be a taxable supply, FA is required to register for VAT. Since her expected annual turnover of €32,000 exceeds the small undertaking threshold for service provision, FA cannot opt to be registered under Article 11 of the VAT Act which would allow her not to charge VAT on the rental (with no entitlement to claim tax credit on the inputs). Instead, she will be required to register for VAT in terms of Article 10 of the VAT Act and charge VAT on her taxable supplies.

**(c) Right to claim a credit for input VAT**

**(i)** Given that all of FA's supplies, with the exception of the provision of accommodation, are exempt without credit supplies, FA will have limited rights to claim a credit for input VAT, as explained below.

Input VAT on construction and finishing costs of Apartment 2

The input VAT on the construction and finishing costs which are directly related to the apartment to be rented to tourists (Apartment 2) may be claimed in full. Such expenses are considered to be of a capital nature provided the costs exceed €1,165 since the benefit thereof is derived on a long-term basis.

Under the Capital Goods Scheme, FA is required to consider any changes in the taxable use of the apartment for 20 years following the date the apartment is first rented out. If, in any year during this period, the apartment is used to make exempt without credit supplies, FA will be required to refund to the tax authorities 1/20th of the input VAT initially claimed on the construction and finishing costs. Such an adjustment will require to be made for each year during the 20 year period that there is such a change in use.

Input VAT on construction and finishing costs of Apartment 1, the penthouse and the office

On the other hand, no input VAT may be claimed on the construction and finishing costs directly related to the office and to the apartment which will be disposed of (Apartment 1), since such exempt without credit supplies do not grant FA any right to claim input VAT. Similarly, no input VAT can be claimed on the construction and finishing costs relating to the penthouse which will not be used for the purpose of any taxable supply but instead will be used as FA's main residence.

Again, under the terms of the Capital Goods Scheme, if in subsequent years the office and/or penthouse start being used for purpose of conducting an economic activity which is deemed to be a taxable supply, FA will each year be entitled to a 1/20th refund of the total original directly related input VAT on the construction and finishing costs of the relevant building.

**(ii)** Input VAT on general overheads

With respect to the general overheads which cannot be directly allocated to either the taxable or exempt without credit supplies, FA is required to utilise the partial attribution rules. FA will be required to calculate a provisional partial attribution ratio by dividing the revenue generated from the taxable supplies (provision of accommodation to tourists) by the total revenue generated from all supplies for the calendar year. At the end of the first year of her economic activity (when she sells Apartment 1 and begins renting out Apartment 2), she will be able to calculate the definitive ratio for that particular year and will be required to adjust in her favour for the unclaimed portion of VAT on general overheads in the previous year. Each year, the definitive ratio of the previous year will be used as the provisional ratio for that year with an adjustment between the provisional and definitive ratio for the year being made in the first VAT return that ends in the following calendar year. Given that in the subsequent years FA is expected to generate only taxable income from the provision of accommodation in the apartment, one would expect that, in later years, FA will have a right to claim a full credit for VAT on general overheads.

**(d) Income tax implications arising on the transfer of the penthouse**

Transfers of immovable property situated in Malta are by default subject to a final property transfer tax of 8% on the transfer value (being the higher of the consideration received and the market value of the immovable property). However, the sale of an individual's own residence is exempt from property transfer tax provided the immovable property has been owned and occupied by the transferor for a period of at least three consecutive years immediately preceding the date of transfer and the property is disposed of within twelve months of the individual vacating the premises. The property must also be declared by the transferor to be his main residence.

Therefore, FA should be exempt from property transfer tax on the sale of her penthouse if she were to sell it after living there for 10 years.

**4 (a) Liability to income tax of Paolo Speranza (PS) in Malta in terms of Malta's jurisdiction to tax and the double tax treaty between Malta and Nearland.**

An individual is deemed to be tax resident in Malta, if he is in Malta either:

– for more than a temporary purpose; or
– with the intention of becoming resident; or
– if he actually stays in Malta at one or more times for a period equal in the whole to six months in the year preceding the year of assessment.

Given that, as of September 2020, PS intended to move to Malta in January 2021, he may be considered to be tax resident in Malta under Maltese tax legislation based on his intentions even during 2020. PS will certainly be deemed to be tax resident in Malta during 2021 as he will spend more than six months in Malta during 2021.

Since Nearland will also consider PS to be resident there, the residence tie breaker rules in the tax treaty must be invoked to establish PS' tax residence. During 2020, PS will have a permanent home in Nearland and potentially also in Malta (Maria's apartment) but his centre of vital interest remains in Nearland where he is employed. In this case, his recent relationship with Maria Sultana (MS) should not be deemed to give rise to a 'family" centre of vital interests in Malta. During 2021, PS will still have a permanent home in both countries, but his centre of vital interests will shift to Malta.

In terms of the double tax treaty with Nearland, PS would not be deemed to be tax resident in Malta during 2020, and is therefore taxable in Malta only on a source basis. However, since PS does not have a permanent establishment (PE) in Malta, the business profits derived from the lecturing services are not connected to a Maltese PE, thereby resulting in Malta losing its right to tax such profits under the terms of the treaty.

From 2021, Nearland will be able to assess to tax PS only on a source basis, subject to the tax treaty provisions. In the case of the Nearland source employment income, Nearland will be able to tax such salary only if:

(i) PS will spend more than 183 days, in any twelve-month period in Nearland; or

(ii) PS' employer is tax resident in Nearland; or

(iii) PS' salary is borne by an Nearland PE of the university in Nearland.

Since the second condition is satisfied, Nearland has the primary jurisdiction to tax his employment income from the university in Nearland and Malta would be required to grant double taxation relief for the tax payable in Nearland. Given that the employment is derived from an activity carried out wholly in Nearland, PS is entitled to opt to pay tax in Malta on his Nearland employment income at a flat tax rate of 15% which will be neutralised by the 15% tax paid in Nearland, resulting in no further tax being due in Malta on such income.

During 2021, PS will be deemed to be a Maltese tax resident but will not be considered to have acquired a Maltese domicile, as he is not excluding the possibility of eventually retiring in Nearland. Accordingly, he will be taxable in Malta on a remittance basis, meaning he will be assessed to Maltese tax on his Malta source income and any foreign source income remitted to Malta. In terms of the remittance basis of taxation, PS is not taxed in Malta on foreign source capital gains irrespective of remittances. Therefore, PS will not be taxed in Malta on the gain resulting from the sale of the shares in GEN. PS will be subject to a tax of €8,525 on his Malta salary of €45,000 (being ((€45,000 x 25%) – €2,725) which exceeds the minimum annual tax of €5,000.

**(b) Impact of marriage on the couple's tax status**

Prior to marrying PS, MS is taxable in Malta on a worldwide basis, that is on all her income and gains irrespective of source and remittances. From 2022, irrespective of whether PS or MS is appointed as the responsible spouse, due to his marriage with MS, PS will become subject to tax in Malta on a worldwide basis. This is because the remittance basis is not available to an individual whose spouse is ordinarily resident and domiciled in Malta.

**(c) Tax benefits upon returning to work after birth of a child**

Upon returning to employment after the birth of her first child, MS will be entitled to benefit from the person returning to work scheme. She will be entitled to either a tax credit of €2,000 spread over two consecutive years starting in 2024, or alternatively to a one-year tax credit capped at €5,000. In both cases, the tax credit may be utilised only against MS' employment income and cannot be offset against the dividend income she derives from the overseas company.

| | | | Available | Maximum |
|---|---|---|---|---|
| 1 | (a) | **Impact of the Controlled Foreign Company rules on South American Hotels Ltd** | | |
| | | CFC rules bring into charge to tax in Malta the proportionate share of the undistributed profits of a non-Maltese controlled entity if: | 0·5 | |
| | | – the actual corporate tax paid by the CFC is lower than the difference between: | 0·5 | |
| | | (i) the tax that would have been charged on the CFC in Malta and | 0·5 | |
| | | (ii) the actual corporate tax paid by the CFC | 0·5 | |
| | | CFC provisions limited to profits arising from non-genuine arrangements without significant people functions | 1·5 | |
| | | Inapplicable where accounting profits amount to no more than €750,000 and the non-trading income does not exceed €75,000 or accounting profits do not exceed 10% of its operating costs for the tax period | 1·5 | |
| | | SAH owns more than 50% in RdJ | 0·5 | |
| | | Reasons why CFC provisions not applicable: | | |
| | | – RdJ tax rate > difference between Malta and RdJ tax rate | 1·0 | |
| | | – key people functions are in Brazil and not in Malta | 1·0 | |
| | | – RdJ accounting profits < €750,000 and the non-trading income <€75,000 | 1·0 | |
| | | – RdJ distributed all profits for the year | 1·0 | |
| | | | 9·5 | 8 |
| | (b) | **(i) Applicability of the Consolidated Group Rules** | | |
| | | Option to file one tax return and pay taxes as a fiscal unit vs separate tax returns | 0·5 | |
| | | Companies within the fiscal unit must have the same accounting period end | 0·5 | |
| | | Can consolidate if the parent is registered in Malta and holds at least 95% of at least two of the following rights: voting rights, rights to profits available for distribution and rights to any assets available for distribution on winding up | 1·5 | |
| | | Approval must be obtained from the other shareholders if not 100% subsidiary | 1.0 | |
| | | MBH can create a fiscal unit with RB but not with SAH as it holds less than 95% in SAH | 1·0 | |
| | | | 4·5 | 4 |
| | | **(ii) Malta tax consequences arising upon the creation of the fiscal unit** | | |
| | | Income/losses derived by RB, will be computed and brought to tax in MBH's hands and RB is treated as a transparent entity | 1·0 | |
| | | RB balances – trade losses, wear and tear allowances, tax credits and tax account balances (with the exception of the untaxed account) deemed to be MBH balances | 1·0 | |
| | | Transactions between RB and MBH ignored including dividends paid by RB to MBH | 1·0 | |
| | | Fiscal unit taxed at 35%. However, since MBH entitled to tax refunds, the 35% tax rate is reduced by the effect of the tax refund | 1·0 | |
| | | MBH required to prepare a consolidated P&L and balance sheet including RB's results | 0·5 | |
| | | The obligation to file a tax return for the fiscal unit sits with MBH and RB is exempt from the requirement to file a separate tax return | 1·0 | |
| | | Tax charged in the name of MBH but RB remains jointly and severally liable for payment | 1·0 | |
| | | | 6·5 | 5 |

| | Available | Maximum |
|---|---|---|
| **(c) Maltese tax treatment of income derived by MBH, RB, SAH and OF** | | |
| SAH and the fiscal unit (MBH and RB) are incorporated and managed and controlled in Malta and therefore taxable in Malta on their worldwide income | 1·0 | |
| **SAH** | | |
| Identification of participation exemption | 0·5 | |
| 100% holding qualifies as an equity shareholding | 0·5 | |
| Qualifies as a participating holding – 5% holding | 1·0 | |
| One of three anti abuse conditions and application to the scenario | 2·5 | |
| **Fiscal unit – dividend from SAH** | | |
| Participation exemption dividend allocated to Untaxed Account and remains exempt at fiscal unit level | 1·0 | |
| **Fiscal unit – RB commission income** | | |
| RB's income taxed at 35% and allocated to the MTA since not attributable to a foreign PE or derived from immovable property in Malta | 1·0 | |
| Dividend distribution entitles MBH to a 6/7ths refund thereby enabling the fiscal unit to pay tax at 5% directly | 1·5 | |
| **Fiscal unit – MBH commission income** | | |
| MBH's income derived from commission income which is directly related to immovable property situated in Malta, taxed at 35% and allocated to the IPA | 1·0 | |
| **OF dividend income** | | |
| No further tax and no right to any tax refund by OF on the dividend from MBH's commission income allocated to the IPA | 1·5 | |
| **Fiscal unit tax computation** | | |
| SAH dividend untaxed account allocation | 0·5 | |
| RB's income allocated to the MTA and MBH income to the IPA | 1·0 | |
| MTA income taxed at 5% with effective tax calculation | 2·0 | |
| IPA income taxed at 35% | 0·5 | |
| | 15·5 | 14 |
| | | |
| **Presentation:** | | |
| Appropriate format of letter | 1·0 | |
| Logical development | 1·0 | |
| Effectiveness of communication | 2·0 | 4 |
| | | **35** |

| | | | Available | Maximum |
|---|---|---|---|---|
| **2** | **(a)** | **Income tax and stamp duty of the two options for Robert's and Amanda's exit** | | |
| | | **Option A** | | |
| | | Transfers of shares are subject to income tax on capital gains | 0·5 | |
| | | Explanation why the transfer is not of a controlling interest. Transfer value is equal to consideration | 1·5 | |
| | | Deduction for share cost of acquisition, but not inflation allowances | 1·0 | |
| | | Transfer subject to duty. Default rate of €2 per €100 increased to €5 per €100 in CSNL's case since assets consist to the extent of 75% or more of immovable property situated in Malta. | 2·0 | |
| | | Stamp duty calculated on higher of consideration and real value. | 0·5 | |
| | | Real value components: | | |
| | | Net Asset Value | 0·5 | |
| | | Goodwill | 0·5 | |
| | | Property adjustment | 1·0 | |
| | | Other adjustments – e.g. 10%+ investments adjustment, preference shares adjustment | 0·5 | |
| | | Disallowed liabilities adjustment explained | 1·0 | |
| | | Practical impact for CSNL | 1·0 | |
| | | **Option B** | | |
| | | Set up of new company does not give rise to any tax implications | 0·5 | |
| | | Property transfer subject to default 8% tax on transfer value whereas transfer of business and goodwill by default subject to 35% on the capital gain | 2·0 | |
| | | Intra group exemption for the business and goodwill transfer | 0·5 | |
| | | Group definition and explanation why Newco and CSNL are considered to be a group and therefore intangible assets transfer is exempt from tax on any capital gain | 2·5 | |
| | | Transfer of studio to satisfy stricter group definition: | 0·5 | |
| | | Each shareholder proportionate shareholding and voting rights (maximum 20% difference) | 1·5 | |
| | | CSNL and Newco owned by same shareholders. Shareholders holding less than 20% in only one company ignored but if more than one shareholder holds less than 20% to be aggregated and if they exceed 20% each to be taken into consideration | 2·5 | |
| | | Exemption not available and transfer subject to the property transfer tax | 0·5 | |
| | | Transfers of business and goodwill are outside scope of stamp duty | 0·5 | |
| | | Transfer of studio not eligible for the intra group exemption for same reasons as income tax, and subject to duty of €5 per €100 | 1·5 | |
| | | | 22·5 | 20 |
| | **(b)** | **Calculation of income tax due by Robert and Amanda under Option A** | | |
| | | Calculation of total tax due | 1·0 | |
| | | Split between provisional and settlement tax | 1·0 | 2 |
| | **(c)** | **Tax consequences of a distribution of profits upon exit under Option B** | | |
| | | Gain on transfer of intangible is exempt and allocated to the Untaxed Account. 15% withholding tax imposed upon a distribution to resident individuals and paid to tax authorities within 14 days from end of month when paid | 2·0 | |
| | | Profit after tax from the transfer of studio allocated to Final Tax Account and no further tax on distribution | 1·0 | 3 |
| | | | | **25** |

| | | | Available | Maximum |
|---|---|---|---|---|
| 3 | (a) | **VAT treatment of FA's supplies** | | |
| | | Place of supply of immovable property transfers and rentals | 1·0 | |
| | | Transfers of immovable property – exempt without credit | 1·0 | |
| | | Property leasing is exempt without credit with exception for leasing by a limited liability company to an Article 10 registered person. Exception not applicable to FA | 2·0 | |
| | | Provision of accommodation – 7% VAT | 1·0 | |
| | | | 5·0 | 4 |
| | (b) | **FA's obligation to register for VAT purposes in Malta** | | |
| | | Required to register due to the provision of accommodation. FA's annual turnover of €32,000 exceeds the Article 11 small undertaking threshold and therefore required to register under Article 10 | 2·0 | 2 |
| | (c) | **FA's right to claim input VAT** | | |
| | | **(i) Construction and finishing costs** | | |
| | | Construction input VAT directly related to provision of accommodation can be claimed in full | 1·0 | |
| | | Explanation of capital goods scheme and adjustment for a 20 year period for construction input VAT if asset used for exempt supplies | 3·0 | |
| | | No input VAT may be claimed on costs directly related to the exempt supplies (office rent and apartment sale) since such supplies do not grant FA any right to claim input | 2·0 | |
| | | No input VAT may be claimed on costs related to penthouse used privately | 1·0 | |
| | | However, right to input VAT in terms of the 20 years capital goods scheme if there is a change of use for taxable supplies. | 1·0 | |
| | | **(ii) General overheads** | | |
| | | Use of the partial attribution rules for general overheads not directly allocated to FA's supplies | 0·5 | |
| | | Explanation of partial attribution rules: provisional ratio (taxable supplies/total supplies) and adjustment in first VAT return of subsequent year through the calculation of the definitive ratio | 2·5 | |
| | | Analysis of how the partial attribution rules will apply to FA | 2·0 | |
| | | | 13·0 | 11 |
| | (d) | **Income tax implications arising on the transfer of the penthouse** | | |
| | | Default 8% property transfer tax | 0·5 | |
| | | Own residence exemption with conditions | 2·0 | |
| | | Application to FA – exemption should apply | 0·5 | 3 |
| | | | | **20** |

| | | | Available | Maximum |
|---|---|---|---|---|
| 4 | (a) | **Paolo's liability to tax in Malta in terms of Maltese tax law and the Malta-Nearland tax treaty** | | |
| | | Definition of tax residence in terms of Maltese tax law | 1·5 | |
| | | Paolo may be considered to be resident for 2020 since he is in Malta for more than a temporary purpose and plans to remain in Malta | 1·0 | |
| | | Paulo definitely resident for 2021 when present in Malta for more than 6 months | 0·5 | |
| | | **Tie-breaker rules:** | | |
| | | Permanent home in both countries | 1·0 | |
| | | 2020 Centre of vital interests in Nearland and therefore tax resident in Nearland | 1·0 | |
| | | 2021 Centre of vital interests in Malta and therefore tax resident in Malta | 1·0 | |
| | | During 2020, Paolo taxable in Malta only a source basis. His lecture fees are not connected to a permanent establishment in Malta and therefore Malta is not entitled to tax such profits | 2·5 | |
| | | As from 2021, Nearland to tax only on source basis but still entitled to tax his Nearland salary since he is employed by an Nearland tax resident employer (1 mark allocated also for reference to other conditions in terms of Article 15 of the tax treaty) | 2·5 | |
| | | Malta to grant double tax relief for tax paid in Nearland on salary. In Malta can opt to tax such employment income at 15% tax since it is derived in terms of an employment contract requiring him to carry out his employment activities outside of Malta | 2·0 | |
| | | 15% Malta tax neutralised by Nearland 15% tax, no further tax to pay in Malta on the salary | 1·0 | |
| | | As from 2021, Paolo taxable in Malta on a remittance basis (explained) | 2·0 | |
| | | Maltese tax on Malta salary | 1·0 | |
| | | Foreign source capital gain therefore not taxed in Malta | 1·0 | |
| | | | 18·0 | 16 |
| | (b) | **Impact of marriage on the couple's tax status** | | |
| | | Since Maria is resident and domiciled in Malta, once married, Paolo will no longer be taxable in Malta on a remittance basis and will be taxed on a worldwide basis | 2·0 | |
| | | Any other relevant point | 1·0 | |
| | | | 3·0 | 2 |
| | (c) | **Tax benefits upon returning to work after birth of first child** | | |
| | | Person returning to work scheme – either €2,000 tax credit split over 2 years or €5,000 maximum tax credit in one year of assessment without any carry forward of any excess tax credits | 2·0 | |
| | | Tax credit to be used against Maria's income | 0·5 | |
| | | | 2·5 | 2 |
| | | | | **20** |