Professional Level – Options Module

Advanced Taxation (Malta)

Thursday 8 December 2016

Time allowed: 3 hours 15 minutes

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.

This question paper must not be removed from the examination hall.

Paper P6 (MLA)

Think Ahead

ACCA

MIA

SCIENTIA VIGILANTIA

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 2015 (year of assessment 2016) 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 38,800	25%	Next 45,500	25%
Remainder	35%	Remainder	35%

Parents rates

€	
0 – 9,800	0%
Next 6,000	15%
Next 44,200	25%
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
2015	832·95

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 Jens Noe, an individual resident in Portugal but domiciled in the Netherlands, is the 100% shareholder of three companies, all of which own immovable property situated in Malta.

(i) JN Ltd, a company incorporated in Malta for the purposes of acquiring a number of run down houses in Gzira in May 2007, and developing them into a luxury apartment block of 20 apartments. The apartment block qualified as a project for the purposes of the Income Tax Act. Upon the transfer of the first apartment (property), JN Ltd made an election to exclude the transfer and all subsequent transfers from the remit of Article 5A, thus ensuring that JN Ltd would be taxed on the gain. Ten of the apartments are still unsold but are being held for resale.

(ii) Noe BVI Ltd, a company incorporated and tax resident in the British Virgin Islands (BVI), which acquired a floor in a large premium office block in St Julian's in March 2003. The office block is rented out to third parties.

(iii) Valletta Build Ltd, a company incorporated in Malta, which acquired a large palazzo in Valletta in November 2012. The palazzo, which was acquired from an individual unrelated to either Valletta Build Ltd or Jens Noe, was in desperate need of restoration. Valletta Build Ltd has recently started the restoration process, with the intention of selling the property on completion of these works.

Jens Noe personally owns a large house in Naxxar, acquired in July 2006. This house was used by Jens as his residence for a period of over five years when he lived in Malta. Jens left Malta five years ago and has not lived in the house since.

Jens Noe is now looking to transfer all of the above Malta properties to third parties.

With respect to the remaining (unsold) luxury apartments owned by JN Ltd, three different alternatives are being considered:

1. JN Ltd will transfer the properties directly to third parties.
2. JN Ltd will transfer the properties to a newly incorporated company, Jay Enn Ltd. Jay Enn Ltd will then transfer the properties to third parties. Jay Enn Ltd is also a company wholly owned by Jens Noe.
3. JN Ltd will be put into liquidation and, as a result, the properties will be transferred to Jens Noe personally, who will then transfer the properties to third parties.

Required:

Draft a letter to Jens Noe advising on the Maltese income tax and duty on documents and transfers implications of the transfer of each of the Malta properties referred to above. In the case of the luxury apartments, the implications with respect to each of the alternatives should be considered separately.

Notes:

1. **Your advice should identify the availability of any relevant exemptions, and explain why they would or would not apply in this specific case.**
2. **The following mark allocation is provided as guidance for this question:**

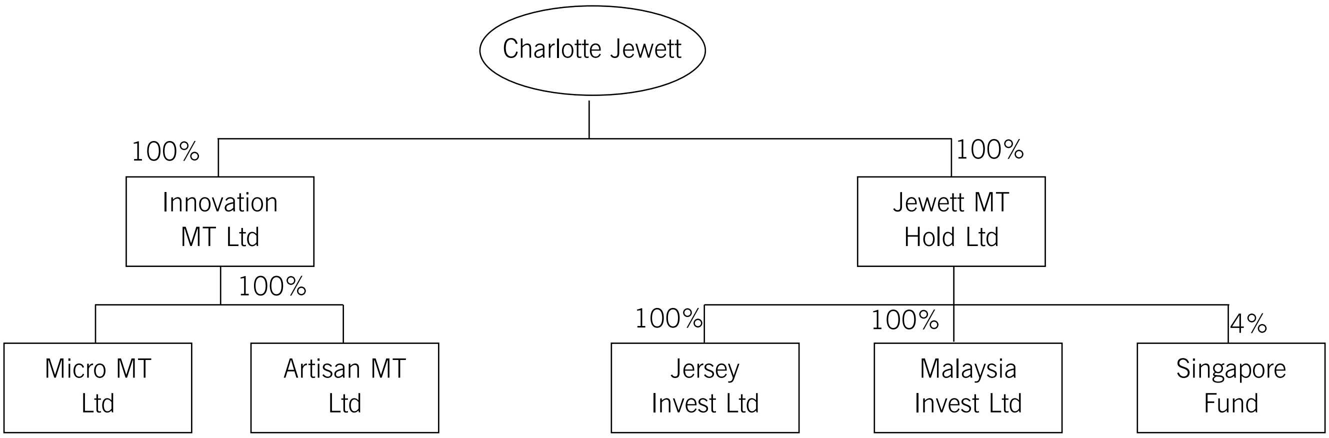
–	**the remaining luxury apartments**	**20 marks**
–	**the office block in St Julian's**	**2 marks**
–	**the palazzo in Valletta**	**4 marks**
–	**the house in Naxxar**	**5 marks**

(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



Charlotte Jewett is an individual not resident and not domiciled in Malta. She is the 100% shareholder of two holding companies, both of which are incorporated and tax resident in Malta:

– Innovation MT Ltd is the 100% shareholder of two other companies, both of which are also incorporated and tax resident in Malta:
  – Micro MT Ltd, which owns and operates a factory producing microchips for sale worldwide. The company's factory is in Bulebel and has a total surface area of 5,000 m^2. In 2015, Micro MT Ltd made a profit of €1,500,000 which it distributed in full to Innovation MT Ltd.
  – Artisan MT Ltd, which acquires and sells high value paintings and sculptures. In 2015, Artisan MT Ltd made a profit after tax of €1,500,000 which it distributed in full to Innovation MT Ltd.
– Jewett MT Hold Ltd, which holds investments in three entities:
  – A 100% shareholding in Jersey Invest Ltd, a company incorporated and tax resident in Jersey. Jersey Invest Ltd provides micro-loans through crowdfunding platforms from which it derives interest of between 10% and 15%. The loans are made to unrelated entities in which Jersey Invest Ltd has no other interest or holding. In 2015, Jersey Invest Ltd derived a profit of €200,000 which it distributed in full to Jewett MT Hold Ltd. No tax is payable in Jersey on this profit.
  – A 100% shareholding in Malaysia Invest Ltd, a company incorporated and tax resident in Malaysia. Malaysia Invest Ltd has invested €40,000,000 in Malaysian bonds, from which it derives annual interest of €3,200,000 on which it suffers tax in Malaysia at the rate of 2%. In 2015, Malaysia Invest Ltd distributed its after-tax profits in full to Jewett MT Hold Ltd. This distribution was not subject to any withholding tax in Malaysia.
  – An investment in 4% of the capital of Singapore Fund, which was acquired in 2013 for €3,150,000. Singapore Fund was set up as a transparent limited partnership in Singapore to acquire minority stakes in companies established in Asia operating in the health industry. Singapore Fund is exempt from tax in Singapore. In 2015, Singapore Fund made a distribution to Jewett MT Hold Ltd of €100,000.

Required:

Advise on the tax treatment of the income derived by Micro MT Ltd, Artisan MT Ltd, Innovation MT Ltd and Jewett MT Hold Ltd, indicating the manner in which the allocation of their profits to the tax accounts should be made, and the implications of these allocations for any refunds which may be available if the profits are fully distributed as dividends. In the case of the three companies in the Innovation MT Ltd group, you should quantify the amount allocated to each company's tax accounts.

Note: The following mark allocation is provided as guidance for this question:

– the Innovation MT group 10 marks
– Jewett MT Hold Ltd 15 marks

(25 marks)

Section B – TWO questions ONLY to be attempted

3 (a) Petra Brown, an individual resident and domiciled in the UK, is one of the directors of Luxury Life Ltd, a company incorporated in Malta having its management and control in Malta and registered for value added tax (VAT) in Malta under Article 10.

Luxury Life Ltd owns various luxury accommodation properties, situated in the South of France, Portugal, Tuscany and Malta. These luxury accommodation properties are rented out to third parties on a short-term letting basis. The accommodation in Malta is licensed under the Malta Travel and Tourism Services Act.

Luxury Life Ltd also owns several yachts, which it charters on a short-term basis to third parties. When they are not on charter, these yachts are berthed in Malta.

In July 2016, Petra came to Malta to attend a board meeting of Luxury Life Ltd, and brought her husband along with her and the couple arrived in Malta the day before the board meeting, given that the meeting started at 9 am the following day, and was to last for the whole day. Following the meeting, Petra and her husband stayed in Malta for a further five days, and thereafter went on a sailing trip to Sicily for a three-day holiday.

While in Malta, Petra and her husband stayed in one of the luxury apartments owned by Luxury Life Ltd, which has a market value of €1,500,000, and was acquired by the company for €1,000,000. Their sailing trip to Sicily was made on a yacht also owned by Luxury Life Ltd, which was acquired by the company in 2014 for €2,500,000, but is now valued at €2,000,000. Petra did not pay Luxury Life Ltd for the use of either the apartment or the yacht, and Luxury Life Ltd did not incur any further expenditure in making the apartment and yacht available to Petra and her husband.

Required:

(i) Explain the Maltese income tax implications, if any, for Petra Brown in respect of the director's fees and benefits received from Luxury Life Ltd, supporting your answer with calculations where appropriate. (6 marks)

(ii) Explain the Maltese value added tax (VAT) implications, if any, for Luxury Life Ltd in respect of the use of the apartment and yacht by Petra and her husband.

Note: You are not required to consider the application of the Guidelines on the VAT Treatment of Short-Term Yacht Chartering. (5 marks)

(b) Airline Ltd is a company incorporated in Malta and registered for value added tax (VAT) under Article 10 in Malta. Airline Ltd is a low-cost European Union airline carrier, which operates a return flight between Malta and Copenhagen, with a stopover in Milan (in each direction) to pick up further passengers for onward travel to Copenhagen or Malta, respectively.

Airline Ltd does not serve free meals on its flights, but sells meals and drinks to passengers throughout the flight. On the last flight from Malta to Copenhagen, 40 items of food or beverage were sold, 10 during the Malta–Milan leg and 30 during the Milan–Copenhagen leg. On the return flight from Copenhagen to Malta, 23 items of food or beverage were sold, 15 during the Copenhagen–Milan leg, and 8 during the Milan–Malta leg.

The aircraft underwent general maintenance upon its return to Malta after this flight.

Required:

With respect to the return flights between Malta and Copenhagen, above, explain the value added tax (VAT) implications of the transport of passengers, the sale of food and beverage during the flights, and the maintenance of the aircraft following the return flight. (9 marks)

(20 marks)

4 **(a)** Mr Barone is a national of Italy. On 1 January 2016, he took up residence in Malta together with his wife and daughter. Mr and Mrs Barone are not domiciled in Malta and since taking up residence in Malta have not been deemed resident in Italy.

Mr Barone is the 100% shareholder of an Italian fund management company from which he derives an annual pension income of €200,000. This pension income is paid into a bank account Mr Barone has in Italy.

Since taking up residence in Malta, Mr Barone has been actively investing his funds trading in derivatives, from which he has made significant income and gains. He trades in his own name, and receives the income or gains he makes into a bank account outside Malta. None of the income or gains is remitted to or received in Malta. In 2016 his income and gains will amount to €30,000.

Required:

Explain the income tax treatment of Mr Barone's income and gains. In particular you should consider:

- **the basis of his tax liability in Malta on account of his personal tax status;**
- **the treatment of both his pension income and trading income in terms of Maltese law;**
- **the implications of the double tax treaty between Malta and Italy for the taxability of his pension income.**

Note: When answering this part of the question, you should assume that:

- Mr Barone does not benefit from any special schemes for the taxation of income in Malta; and
- the double tax treaty between Malta and Italy is similar in all respects to the OECD Model Tax Convention.

(4 marks)

(b) Mr Barone intends to acquire a 30% stake in an existing company which holds a fund management licence issued by the Malta Financial Services Authority (MFSA). He will also take up the position of head of marketing with this company, a role which will require him to work mainly outside Malta in order to attend conferences and seminars to source clients. When in Malta he will be expected to carry out research into new markets outside Malta, and report to the company's board of directors on his progress. Mr Barone will be paid an annual salary of €100,000 by this company (excluding fringe benefits), and this will be paid into his Maltese bank account.

Required:

(i) **Advise Mr Barone on the qualifying conditions for the special scheme for the taxation of income derived by highly qualified persons, whether he is likely to satisfy these conditions, and the tax implications if he does so, showing calculations.** (12 marks)

(ii) **State, with reasons, whether Mr Barone will be entitled to benefit from the rules with respect to taxation of income derived from an employment requiring the performance of duties outside Malta and, if so, by showing a calculation of the tax due, determine whether this scheme or the highly qualified persons scheme would be the better option.** (4 marks)

(20 marks)

5 (a) Simulate Ltd, a company incorporated in the Isle of Man and managed and controlled therein, owns an aircraft which it leases to Fly UK Ltd. Fly UK Ltd is an airline resident and domiciled in the UK, which operates flights all around Europe. The leased aircraft is kept at an airport in the UK, and is used by Fly UK Ltd to fly the technicians employed by that company to the different airports from which it operates when there is trouble with the passenger aircraft operated by Fly UK Ltd.

Simulate Ltd also owns an office block in the UK, from which it derives rental income. This office block is also leased to Fly UK Ltd and is used as the company's headquarter offices. The lease contract for the office block is due to expire in three years, at which time Simulate Ltd will probably sell the office block. The office block was acquired in 2000 for €2,000,000, and has recently been valued by a professional property valuer as being worth approximately €3,500,000.

Simulate Ltd is considering transferring its management and control to Malta, while maintaining its domicile in the Isle of Man. It may also consider moving its domicile to Malta at some point in the next two to three years.

Required:

(i) Explain Simulate Ltd's current Malta tax status and basis of taxation, and the effect if the company (1) transfers its management and control to Malta, and (2) also transfers its domicile to Malta. (2 marks)

(ii) Discuss, by reference to both the rules relating to aircraft used in international transport, and general tax principles, whether the income derived by Simulate Ltd from (1) the lease of the aircraft to Fly UK Ltd, and (2) the rental of the immovable property, will be deemed to arise in Malta or outside Malta. (6 marks)

(iii) Advise Simulate Ltd whether to opt for a step-up in the value of its assets when the company transfers its management and control to Malta, or to wait to do so until it decides to move its domicile to Malta. (4 marks)

(b) Ray Grech is an individual resident and domiciled in Malta, who has significant interests in Portugal, as follows:

- A 100% shareholding in Integre Ltd, a company incorporated and tax resident in Portugal. In 2015, Integre Ltd declared a dividend of €500,000 to Mr Grech. The company's accountants have advised Mr Grech that Portuguese law imposes withholding tax at the rate of 25% on dividend distributions made to non-residents.
- A 50% shareholding in Grech Ltd, a company incorporated in Greece which has a permanent establishment in Portugal. In 2014, Mr Grech personally provided a loan to Grech Ltd in order to finance the operations of the permanent establishment in Portugal. In 2015, Mr Grech derived interest income of €40,000 from this loan, which was paid by the permanent establishment in Portugal. The company's accountants have advised Mr Grech that the interest payment may be subject to tax in both Greece and Portugal. Greek law imposes withholding tax at the rate of 15% on interest paid to non-residents, and Portuguese law imposes withholding tax at the rate of 20% on interest paid to non-residents.
- Mr Grech personally assigned a licence over software to Gong Ltd, a Portuguese company, subject to a yearly licence fee of €100,000. The company's accountants have advised Mr Grech that Portuguese law imposes withholding tax at the rate of 10% on royalties paid to non-residents.

Required:

(i) Explain why the information provided to Mr Grech by the respective company accountants, relating to withholding tax on the payments made to him, is incorrect under the provisions of the relevant double tax treaties.

Note: You should assume that double taxation agreements are in force between Malta and Greece and between Malta and Portugal, and that they are similar in all respects to the OECD Model Tax Convention. (6 marks)

(ii) State, with reasons, whether the Parent–Subsidiary Directive and/or the Interest and Royalties Directive will apply to any of the payments made to Mr Grech. (2 marks)

(20 marks)

End of Question Paper