Professional Level – Options Module

Advanced Taxation (Malta)

Thursday 9 June 2016

Paper P6 (MLA)

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

This question paper is divided into two sections:

Section A – BOTH questions are compulsory and MUST be attempted

Section B – TWO questions ONLY to be attempted

Tax rates and allowances are on pages 2–5

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

Think Ahead

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%

Parent 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

$Z = ((A - B)/A) \times E$

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.

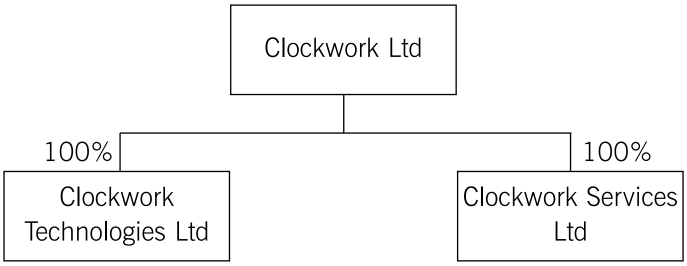
Tax refund calculation when a company benefits from a reduced rate in terms of a tax treaty

$Y = (R - 5\%)/R$

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 You should assume that today's date is 1 September 2015



You met recently with Joe and Clive Cachia, two brothers who are resident and domiciled in Malta. In 1995 they incorporated Clockwork Ltd in Malta with an issued share capital of 10,000 shares of €1 each, of which 5,000 shares were held by Joe and 5,000 shares by Clive. The only assets on Clockwork Ltd's balance sheet are its bank account and its investments in its two 100% owned subsidiaries, Clockwork Technologies Ltd and Clockwork Services Ltd, which are also incorporated and managed and controlled in Malta. Clockwork Ltd accounts for both subsidiaries at the nominal value of the shares.

As at 31 December 2014, Clockwork Ltd's financial statements showed a net asset value of €5,400,000. Clockwork Ltd's profits consist solely of dividends distributed by its two subsidiaries in the same financial year in which they were earned. For the last five years these dividends, gross of tax, have been as follows:

2010: €400,000
2011: €350,000
2012: €450,000
2013: €500,000
2014: €700,000

Clockwork Technologies Ltd was incorporated in 1995 with an issued share capital of 9,000 shares of €1 each. The company manufactures Maltese clocks in a factory in Mriehel, Malta. Clockwork Technologies Ltd acquired the factory in 1995 for €25,000. The acquisition was funded partly by means of a €15,000 bank loan, and partly by means of two loans of €5,000 each from Joe and Clive; neither of these loans was registered at the Public Registry. In December 2012, Clockwork Technologies Ltd sold the factory in Mriehel to Clockwork Services Ltd at its market value which was determined by an architect's valuation to be €500,000 – accounting for just over 25% of the assets of Clockwork Technologies Ltd at that time. Clockwork Services Ltd funded the acquisition of the factory partly from its retained earnings and partly from loans from Joe and Clive. These loans were also not registered at the Public Registry. Following the sale of the factory, Clockwork Technologies Ltd rented part of the factory from Clockwork Services Ltd for use in its manufacturing operations. The current market value of the factory, as determined by a recent architect's valuation, is €550,000.

As at 31 December 2014, Clockwork Technologies Ltd's financial statements showed a net asset value of €1,500,000. For the last five years its profits before tax have been as follows:

2010: €800,000
2011: €600,000
2012: €500,000
2013: €350,000
2014: €300,000

Clockwork Services Ltd was incorporated in 2010 with an issued share capital of 20,000 shares of €1 each. The company is in the business of servicing all types of clock (whether produced by Clockwork Technologies Ltd or other manufacturers) and the maintenance and restoration of old clocks, which it acquires and then resells. As at 31 December 2014, the financial statements of Clockwork Services Ltd showed a net asset value of €750,000. For the last five years its profits before tax have been as follows:

2010: €50,000
2011: €100,000
2012: €75,000

2013: €150,000
2014: €170,000

Clockwork Technologies Ltd and Clockwork Services Ltd have a full dividend distribution policy, whereby they make a dividend distribution every year of all the company's distributable profits.

In January 2015, Joe donated part of his holding in Clockwork Ltd to his adult children. He donated a 15% holding to his son Mario, and a further 15% holding to his daughter Isabelle, keeping his remaining 20% holding for himself. Each donation was declared in the deed of donation at a market value of €800,000.

Clive is now looking to acquire a further 30% stake in Clockwork Ltd. So far it appears that Mario and Isabelle would each be willing to transfer 10% of the company's share capital from their respective holdings to Clive in September 2015. However, Joe is not keen on transferring any of his remaining shares to Clive. Clive is willing to pay €1,000,000 to acquire each 10% holding.

Joe and Clive both have a marginal tax rate of 35%.

Required:

(a) Draft a letter to Clockwork Ltd advising on the Maltese income tax and duty on documents and transfers implications for all the relevant parties of the following share transactions:

(i) the donation of shares by Joe Cachia to his children Mario and Isabelle in January 2015;

(ii) the proposed transfer of shares by Mario and Isabelle to their uncle, Clive Cachia, in September 2015; and

(iii) a future transfer of shares by Joe Cachia to his brother, Clive Cachia.

The following mark allocation is provided as guidance for this requirement:

(i) 10 marks
(ii) 5 marks
(iii) 10 marks

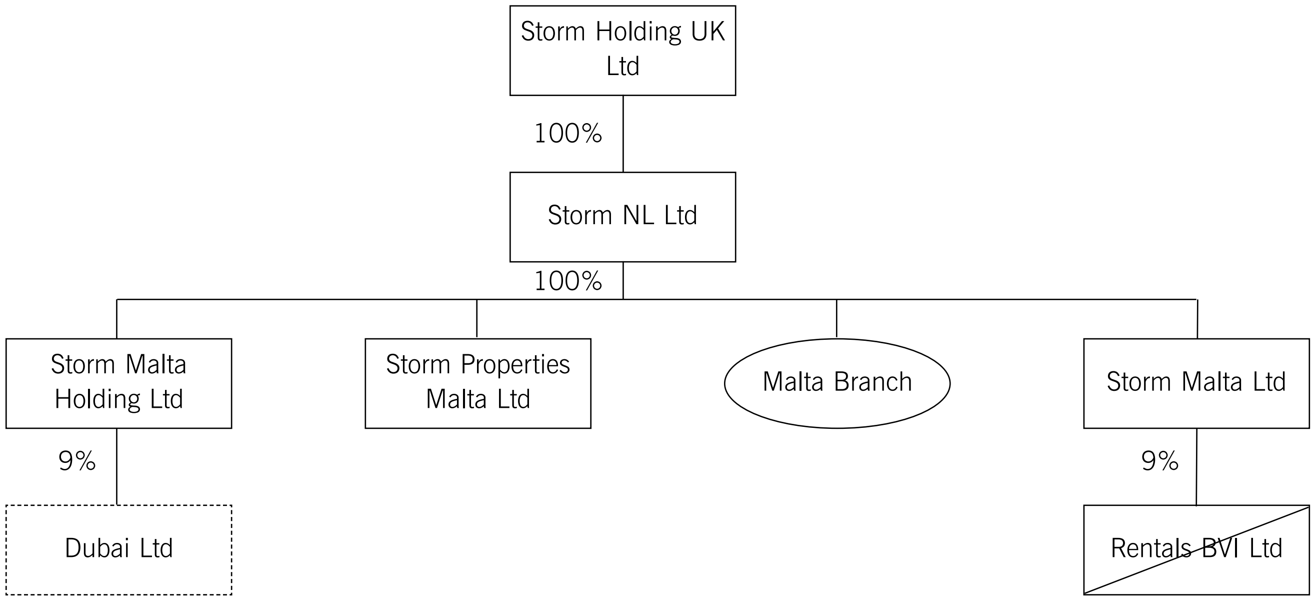
(25 marks)

(b) Support the advice given in your answer to part (a) with a calculation of the Malta income tax payable by Joe Cachia should he transfer a 10% stake in Clockwork Ltd to Clive Cachia in December 2015. (6 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



The Storm group is a multinational group of companies headquartered in the United Kingdom, but with a significant presence in Malta. Storm Holding UK Ltd is a company incorporated and managed and controlled in the UK which is owned by persons who are neither resident nor domiciled in Malta.

Storm Holdings UK Ltd is the 100% shareholder of Storm NL Ltd, a company incorporated and managed and controlled in the Netherlands. Storm NL Ltd has a presence in Malta by way of three subsidiaries, which are incorporated and managed and controlled in Malta, and a Malta branch:

- Storm Malta Holding Ltd: is in the process of acquiring a 9% stake in Dubai Ltd for €1 million. Dubai Ltd is a company incorporated and managed and controlled in Dubai, which owns a shopping mall in Dubai. Dubai Ltd does not suffer any tax on its activities in Dubai, and Dubai does not levy any withholding tax on the distribution of its profits to non-residents of Dubai. Storm Malta Holding Ltd's 9% stake in Dubai Ltd will not entitle it to any special rights over Dubai Ltd, but it expects to generate €550,000 dividend income from the holding. Storm Malta Ltd will seek finance from Storm NL Ltd (not from the Malta Branch of Storm NL Ltd) for the acquisition of Dubai Ltd, either through the issue of additional equity or by means of an interest bearing loan.
- Storm Properties Malta Ltd: acquires land in Israel, develops apartments on the land and sells them on to third parties, paying tax in Israel at 10% on the gains. Storm Properties Malta Ltd does not have a permanent establishment in Israel.
- Malta Branch: provides services (back office, legal services and accounting support) to Storm Malta Holding Ltd, Storm Properties Malta Ltd and Storm Malta Ltd in return for a fixed retainer fee of €30,000 per annum from each company.
- Storm Malta Ltd: holds a 9% stake in Rentals BVI Ltd, which it acquired over ten years ago for €50,000. Rentals BVI Ltd is a company incorporated in the British Virgin Islands but managed and controlled in Malta (the diagonal line within the diagram above is used to show that the company is dual resident). Rentals BVI Ltd owns commercial property in the Caribbean which is rented out to third parties. Rentals BVI Ltd derives rental income of approximately €650,000 a year from these properties, none of which is received in a Maltese bank account. Storm Malta Ltd derives dividends of approximately €50,000 a year from Rentals BVI Ltd. Storm Malta Ltd's 9% stake does not entitle it to any special rights over Rentals BVI Ltd.

Required:

Explain the Maltese income tax treatment of the income derived by each of:

(i) Storm Malta Holding Ltd should it acquire Dubai Ltd, including your advice on the best way to fund the acquisition of Dubai Ltd;
(ii) Storm Properties Malta Ltd;
(iii) the Malta branch;
(iv) Storm Malta Ltd; and
(v) Rentals BVI Ltd.

In each case, indicate the manner in which the profits should be allocated to the various tax accounts and the implications of these allocations for any refunds which may be available if the profits of its subsidiaries are fully distributed as dividends to Storm NL Ltd, and on any subsequent distribution of dividends by Storm NL Ltd to Storm Holdings UK Ltd.

Note: You are not required to provide supporting calculations of the actual tax payable/refundable.

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

(i) 15 marks
(ii) 4 marks
(iii) 2 marks
(iv) 2 marks
(v) 2 marks

(25 marks)

Section B – TWO questions ONLY to be attempted

3 **(a)** Malta Table Ltd is a company registered for value added tax (VAT) in Malta. The company manufactures chairs and tables, which it sells in Malta and around the world. In the Caribbean, Malta Table Ltd sells its goods through an agent, NL Supplies Ltd, which acts in the name and on behalf of Malta Tables Ltd. NL Supplies Ltd charges a commission to Malta Table Ltd for this. NL Supplies Ltd is a company incorporated and registered for VAT in the Netherlands. All of the chairs and tables are shipped to its customer by Malta Tables Ltd directly from its warehouse in Malta.

Required:

Explain the Maltese value added tax (VAT) implications of the sale of its chairs and tables by NL Supplies Ltd as an agent of Malta Tables Ltd to non-EU purchasers in the Caribbean, and of the commission charged by NL Supplies Ltd on these sales. (6 marks)

(b) Malta Sailing Ltd is a company with a place of business in Malta, and registered for VAT purposes in Malta. Malta Sailing Ltd owns two super yachts, Queen of the Sea and Total Eclipse, which it charters to non-taxable persons for their private use.

Queen of the Sea is to be chartered for a period of two weeks to Mr Bocconi, a private individual resident in Italy. The charter will start from Monaco, where Queen of the Sea is currently moored.

Total Eclipse is to be chartered for 100 days to Mr Saad, a private individual resident in Saudi Arabia. The charter will start from Malta, given that Total Eclipse is currently moored in Malta.

Required:

Explain how the place of supply of the two charters will be determined in terms of the VAT Act. (6 marks)

(c) Bruce Smith, a UK national, has recently moved his residence to Malta. Bruce is a freelance consultant who advises an entirely non-EU client base comprising both business customers to which he provides business advice, and private individuals to whom he provides personal financial advice. Following his move to Malta, Bruce will continue providing his consultancy services from his house in Malta. His annual income from these consultancy services is approximately €120,000.

Bruce employed Express Transport Ltd, a company established and registered for VAT in the UK, to transfer all his personal belongings to Malta. He also transferred his television satellite service contract with Great Sports Ltd, another company established and registered for VAT in the UK, to his Malta address, so that he can continue to follow his favourite football team.

Required:

Explain the place of supply in terms of the VAT Act and the Maltese VAT implications, if any, of:

(1) the services provided by Bruce Smith; and
(2) the services Bruce received from Express Transport Ltd and Great Sports Ltd as part of his move to Malta. (8 marks)

(20 marks)

4 (a) List ANY EIGHT activities which are considered qualifying activities under the Investment Aid Regulations. (4 marks)

(b) (i) Global Products Malta Ltd, a company incorporated and managed and controlled in Malta, is involved in the manufacture and sale of pharmaceutical products. Global Products Malta Ltd is wholly owned by Global Products International Ltd, a company incorporated in Malta whose sole asset is its holding in Global Products Malta Ltd. Global Products International Ltd is in turn wholly owned by Joe Grech, an individual resident and domiciled in Malta.

Global Products Malta Ltd is currently benefitting from tax credits and qualifies as a small enterprise under the Investment Aid Regulations, given that it has an employee headcount of 40 workers, a turnover of €5 million and a balance sheet total of €9 million.

Global Products International Ltd is looking to make further acquisitions in and outside Malta as follows:

– 15% of CypPharma Ltd, a company incorporated and managed and controlled in Cyprus which operates various pharmacies in Cyprus. CypPharma Ltd has an employee headcount of 20, a turnover of €2 million and a balance sheet total of €3·5 million.

– 30% of Belux Ltd, a company incorporated and managed and controlled in Belgium which owns retail shops in Brussels. Belux Ltd has an employee headcount of 10, a turnover of €3 million and a balance sheet total of €7 million.

– 55% of MediMalta Ltd, a company incorporated and managed and controlled in Malta, which carries out research and development activities for various pharmaceutical companies. MediMalta Ltd has an employee headcount of 100, a turnover of €10 million and a balance sheet total of €12 million.

Required:

Explain the effect of the proposed acquisitions by Global Products International Ltd on Global Products Malta Ltd's qualification as a small enterprise. (12 marks)

(ii) For the purposes of this part you should assume that the holdings in CypPharma Ltd, Belux Ltd and MediMalta Ltd (identified in part (i)) were acquired on 1 January 2015.

In the year ended 31 December 2015, Global Products Malta Ltd invested €400,000 in qualifying expenditure, made a taxable profit for the year of €700,000, and had a balance brought forward of unutilised investment tax credits of €175,000.

Required:

Calculate the tax payable in Malta by Global Products Malta Ltd for 2015, as well as the investment tax credit carried forward, if any, and state the tax account to which the profits will be allocated.

Note: Your answer should take into account an inflation reference rate of 0·17%. (4 marks)

(20 marks)

5 (a) Pamela King, a Hong Kong national who is resident but not domiciled in Malta, lives in Malta with her husband, Paul, who is also resident but not domiciled in Malta.

Pamela is an employee of Xiang Ltd, a company incorporated in China, under a contract of service which requires her to spend the majority of her time in China. However, she is given the concession to carry out research relevant to her work when she is at home in Malta. Her salary is paid into her bank account in Malta.

Pamela is the 100% owner of Sail Pro Ltd, a company incorporated and managed and controlled in Jersey. Sail Pro Ltd wholly owns Sail Ltd, a company incorporated and managed and controlled in Malta, whose sole asset is a 35 metre yacht which it charters to third parties in South East Asia. Pamela is now looking to transfer her interest in the yacht to a third party indirectly, using one of the following two options:

– Sail Pro Ltd will sell its shares in Sail Ltd; or
– Pamela will sell her shares in Sail Pro Ltd.

Pamela is in receipt of an annual pension which is paid by the government of Hong Kong through a pension scheme which was created for the employees of a public authority in Hong Kong. Prior to moving to Malta, Pamela had been employed by the public authority in Hong Kong for a period of 20 years. The pension is paid into Pamela's Maltese bank account.

Additional information:

1. The tax treaties between Malta and China and Malta and Hong Kong are based in all material respects on the OECD Model Tax Convention.
2. Pamela is deemed to be a resident of Malta in terms of Maltese domestic law, and she is not deemed to be a resident in China in terms of Chinese domestic law.
3. China is claiming taxing rights over the employment income derived by Pamela from Xiang Ltd.
4. Hong Kong is claiming taxing rights over Pamela's pension income.

Required:

Based on Maltese domestic law and the provisions of the OECD Model Tax Convention, explain the Malta income tax implications of:

(i) the employment income derived by Pamela King from Xiang Ltd;

(ii) any gains derived from the transfer of shares, either in Sail Ltd by Sail Pro Ltd or in Sail Pro Ltd by Pamela, and whether one option would be preferable to the other; and

(iii) the pension derived by Pamela from her service with the Hong Kong public authority.

Note: You are not required to consider the application of any residence programmes to Pamela King.

The following mark allocation is provided as guidance for this requirement:

(i) 9 marks
(ii) 3 marks
(iii) 3 marks

(15 marks)

(b) Paul Mifsud, a national of Malta who is unmarried, emigrated to Canada together with his parents 30 years ago, when he was 17 years old. Since leaving Malta, he has returned to Malta for a period of two weeks during December, to visit his relatives. Over the years, Paul set up and later sold a successful business in Canada. He is now looking to return to Malta and become tax resident in Malta again. To this effect, he has already acquired a property in Malta. Paul holds bank accounts in Canada from which he derives considerable interest income, holds shares in various companies listed on the Canadian stock exchange from which he derives dividend income, and from the age of 60 will be entitled to a pension from the company in Canada which he set up and later sold.

Required:

State the conditions required for Paul Mifsud to qualify under the rules relating to returned migrants, and explain the basis on which he will be taxed in Malta if he does qualify under those rules. (5 marks)

(20 marks)

End of Question Paper