Professional Level – Options Module

Advanced Taxation (Malta)

Thursday 7 December 2017

Paper P6 (MLA)

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.

Think Ahead

ACCA

MIA

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 2016 (year of assessment 2017) are to be used in answering the questions.

Individual income tax

Resident individual tax rates

Married couples – joint computation

€	€	Rate	Subtract – €
0	to 12,700	0%	0
12,701	to 21,200	15%	1,905
21,201	to 28,700	25%	4,025
28,701	to 60,000	25%	3,905
60,001 and over		35%	9,905

Other individuals

€	€	Rate	Subtract – €
0	to 9,100	0%	0
9,101	to 14,500	15%	1,365
14,501	to 19,500	25%	2,815
19,501	to 60,000	25%	2,725
60,001 and over		35%	8,725

Parents maintaining a child/paying maintenance

€	€	Rate	Subtract – €
0	to 10,500	0%	0
10,501	to 15,800	15%	1,575
15,801	to 21,200	25%	3,155
21,201	to 60,000	25%	3,050
60,001 and over		35%	9,050

Non-resident individuals

€	€	Rate
0	700	0%
701	3,100	20%
3,101	7,800	30%
7,801 and over		35%

Returned migrants

Married couples

€	
0 to 5,900	0%
Remainder	15%

Others

€	
0 to 4,200	0%
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

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
2016	838·29

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

Unutilised provisional tax

Unutilised provisional tax = (0·625 x A) – B

Where:
'A' is the total provisional tax paid, during or in respect of the year preceding any year of assessment; and
'B' is the tax charged on the chargeable income, and in respect of the same year of assessment

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 Emma Gammon, an individual resident in Malta but domiciled in the UK, has been living in Malta for the last ten years, and has invested heavily in immovable property situated in Malta. In view of the recent changes in the law relating to the taxation of transfers of immovable property, Emma wishes to determine the tax implications on the transfer of the property she owns, both directly, and indirectly.

Emma's main investments are held indirectly through three companies as follows:

(1) She is a 50% shareholder in Park Ltd, a company incorporated in 2010 and tax resident in Malta. In 2012, Park Ltd constructed a development of 30 luxury apartments in Mellieha, which obtained the status of a special designated area. Upon the sale of the first apartment, Park Ltd elected to have the development treated as a project for income tax purposes, so opted out of the final tax system. There are currently five apartments left for sale, which Park Ltd is looking to sell in 2018. The proportionate cost of development per apartment was €650,000 and the five apartments are likely to be sold for €900,000 each.

(2) She is a 40% shareholder in Hatt Ltd, a company incorporated and tax resident in Malta. Hatt Ltd has just obtained permits to develop 60 luxury apartments in the south of Malta, which will be held for sale. The development and construction of these apartments will be financed mainly by the company's shareholders (including Emma), but Hatt Ltd is looking at additional means to fund the development, with the current preferred option being to issue bonds on the Malta Stock Exchange. The proportionate cost of development per luxury apartment is expected to be €800,000 and the apartments are likely to be sold for a minimum of €1,000,000 each.

(3) She is the 100% shareholder in Zeppos Ltd, a company incorporated and tax resident in Cyprus, which developed a large office block in Malta in 2010. In order to fund her share of the construction planned for Hatt Ltd, it is proposed that Zeppos Ltd will sell the office block to third parties for a value of €800,000.

Emma also owns the following properties personally:

(1) A house in Mosta which she inherited from her mother. Her mother had owned the property as her own residence and lived in it until she passed away in September 2017. Emma moved into the house within a month of her mother's death, but does not see herself living there permanently and is looking to sell it.

(2) An apartment in Mellieha Bay, which she has been renting out to tourists ever since she acquired it in 2015. She is now looking to sell this apartment.

(3) A large house in Birgu, situated in an urban conservation area. Emma acquired this house in 2010 and has carried out restoration works on the property in terms of a permit issued by the Malta Environment and Planning Authority (MEPA), commencing in 2013 and completed in October 2017.

Required:

Draft a letter to Emma Gammon advising her on:

(i) The Maltese income tax and duty on documents and transfers implications of the intended sales of properties by Park Ltd, Hatt Ltd and Zeppos Ltd. Support your advice with calculations of the income tax to be paid by each company.

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

Park Ltd	3 marks
Hatt Ltd	9 marks
Zeppos Ltd	4 marks

(16 marks)

(ii) The duty on documents and transfers implications of the acquisition by way of a *causa mortis* transfer of the house in Mosta, and the income tax and duty on documents and transfers implications on the potential sale of this house. (6 marks)

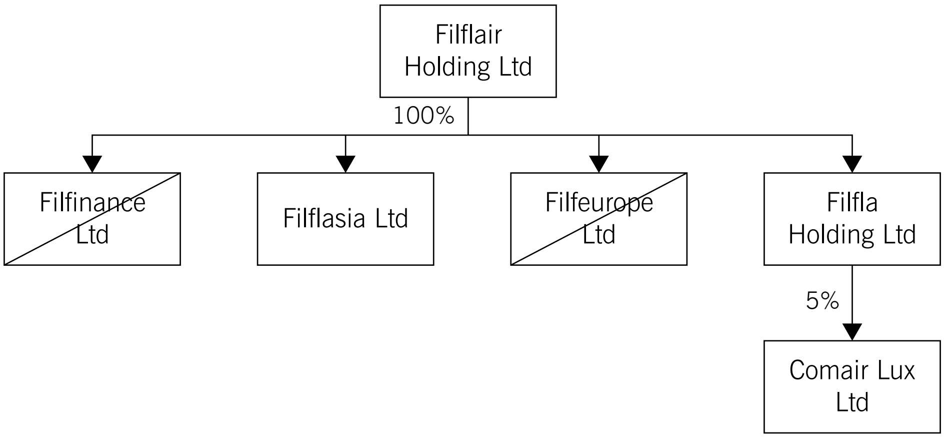
(iii) The income tax and duty on documents and transfers implications of the intended sales of the Mellieha apartment and the house in Birgu. (5 marks)

(iv) The tax implications of Ms Gammon receiving dividends from Park Ltd, Hatt Ltd and Zeppos Ltd following the sale of their properties. (4 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 Filflair Group, a group of companies involved in the aviation industry, is structured as shown below.



The parent company, Filflair Holding Ltd, is incorporated and tax resident in Malta but is owned and controlled by five individuals who are neither resident nor domiciled in Malta. Filflair Holding Ltd is the 100% shareholder of four companies:

(1) Filfinance Ltd: a company incorporated in Jersey but tax resident in Malta, by virtue of having its management and control in Malta, is the finance arm of the group. In 2016, Filfinance Ltd derived interest income of €14 million, as follows:

– €5,000,000 from Filflasia Ltd, in respect of a loan provided for the acquisition of five Gulfstream G250 private jets.

– €7,500,000 from Filfeurope Ltd, in respect of a loan provided for the acquisition of five Gulfstream G350 private jets.

– €1,500,000 from Filfla Holding Ltd, in respect of a loan provided for the acquisition of a 5% holding in Comair Lux Ltd.

The interest is all paid into a bank account held by Filfinance Ltd outside Malta.

(2) Filflasia Ltd: a company incorporated and tax resident in Malta, which owns and leases, by way of an operating lease, five Gulfstream G250 private jets to an Asian company which charters private jets to individuals. The five aircraft were acquired for €30 million each (i.e. a total of €150 million), fully debt financed. For accounting purposes the aircraft will be depreciated over 20 years, using the straight line method, and if possible, the company intends taking tax wear and tear allowances over the same period. In 2016, Filflasia Ltd derived lease income of €15,000,000 (i.e. €3,000,000 per aircraft).

(3) Filfeurope Ltd: a company incorporated in Jersey but tax resident in Malta, by virtue of having its management and control in Malta, which owns and leases, by way of an operating lease, five Gulfstream G350 private jets to a Maltese company which charters private jets. The five aircraft were acquired for €36 million each (i.e. a total of €180 million), fully debt financed. For accounting purposes the aircraft will be depreciated over 20 years, using the straight line method, and if possible, the company intends taking tax wear and tear allowances over the same period. In 2016, Filfeurope Ltd derived lease income of €17,500,000 (i.e. €3,500,000 per aircraft). Filfeurope Ltd has an office in Malta of 200m^2, which it owns and uses for the purpose of its operations.

The lease income is paid into a bank account held by Filfeurope Ltd outside Malta.

(4) Filfla Holding Ltd: a company incorporated and tax resident in Malta, which holds a 5% investment in Comair Lux Ltd, a company incorporated and tax resident in Luxembourg. Filfla Holding Ltd's holding in Comair Lux Ltd entitles it to appoint a director to the board of Comair Lux Ltd. In 2016, Filfla Holding Ltd derived dividend income of €5,250,000 (gross of a 15% withholding tax) from its investment in Comair Lux Ltd. Comair Lux Ltd qualified for a deduction against its chargeable income in Luxembourg in respect of this dividend.

Required:

Advise on the Malta tax treatment of the income derived by the Filflair group companies, indicating the manner in which the profits of each should be allocated to their respective tax accounts, and the implications of these allocations for any refunds which may be available if the profits are fully distributed as dividends to Filflair Holding Ltd.

Note: Support your advice with relevant calculations to the extent the information permits and state clearly any assumptions you make.

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

Filflair Holding Ltd	4 marks
Filfinance Ltd	2 marks
Filflasia Ltd	4 marks
Filfeurope Ltd	7 marks
Filfla Holding Ltd	8 marks

(25 marks)

Section B – TWO questions ONLY to be attempted

3 **(a)** Consult Ltd, a newly incorporated Maltese company, intends to furnish its offices with furniture it will acquire for €38,000 from Ufficii di Lusso Spa, a company incorporated in Italy. Ufficii di Lusso Spa will organise the transport of the furniture but the assembling of the furniture in Malta will need to be organised by Consult Ltd. Consult Ltd is in the process of becoming registered for value added tax (VAT) in Malta under Article 10, and is uncertain whether to acquire the furniture prior to finalising its VAT registration, or after it has its VAT number.

Required:

Explain the Maltese value added tax (VAT) implications, if any, of Consult Ltd's acquisition of furniture from Ufficii di Lusso Spa, if Consult Ltd acquires the furniture (1) prior to obtaining its VAT number and (2) after obtaining its VAT number. (7 marks)

(b) **Set out the circumstances in which the letting of immovable property is NOT an exempt without credit supply for value added tax (VAT) purposes.** (6 marks)

(c) Global Transport Ltd is a company incorporated in Malta, which provides passenger transport and freight forwarding services between Malta and various Eastern European EU Member States. Global Transport Ltd is registered for value added tax (VAT) under Article 10.

Global Transport Ltd owns three passenger transport vehicles, which can each transport up to 45 passengers. Each vehicle makes one round trip per week starting from Malta. One of the vehicles travels from Malta to Slovenia and Croatia; the second from Malta to Hungary and Slovakia; and the third from Malta to the Czech Republic and Poland. Passengers may board at stops in each of the countries.

Global Transport Ltd owns six freight forwarding vehicles, which travel the same routes as the passenger transport vehicles. Again, each vehicle makes one round trip per week, timetabled to ensure departures from Malta on each route twice per week. The goods are loaded in Malta for delivery to their country of final destination, or are collected from the respective countries on each route to be brought to Malta.

Required:

Explain the Maltese value added tax (VAT) implications of the transport of passengers and goods by Global Transport Ltd between Malta and Eastern European countries. (7 marks)

(20 marks)

4 (a) Mary Curmi, a Maltese resident and domiciled person, is 44 years old and is the mother of two children, aged 11 and 17 years. Prior to having children, Mary worked as a financial controller for eight years; she stopped working once she had her first child. Now her children are older, she is looking to return to gainful employment, on a 30-hour per week basis. She has been offered a job with an annual salary of €17,000 for 30 hours per week.

Joanne Dingli, a Maltese resident and domiciled person, is 31 years old, and works as an accountant earning a salary of €40,000 per annum. Joanne is currently on maternity leave, as she recently gave birth to twins, but she plans to return to work at the end of her maternity leave, reducing her hours from 40 to 20 hours per week. Her salary will be reduced pro-rata.

Both Mary and Joanne will opt for separate computations for income tax purposes on their return to work.

Required:

Explain the application of the *Tax Credit (Women Returning to Employment) Rules* to (1) Mary Curmi and (2) Joanne Dingli, and determine by means of a calculation the best option available to each of them.

(15 marks)

(b) Kevin and Josephine Mallia are a married couple who are both resident and domiciled in Malta. They are both employed by Kamp Limited, a company resident and domiciled in Malta. Kevin is employed on a full-time basis with a salary of €10,000 per annum, and Josephine is employed on a part-time basis, also with a salary of €10,000 per annum.

George Borg, an individual resident and domiciled in Malta, is a sole trader, who operates an importation of goods business in his own name. He is married to Corinne, who is also resident and domiciled in Malta, and is employed on a part-time basis as a hotel receptionist.

Both married couples pay income tax at the married rates.

Required:

Explain the application of the *Part-Time Work Rules* with respect to the income derived by (1) Josephine Mallia and (2) Corinne Borg. (5 marks)

(20 marks)

5 **(a)** Rovelli Holding Ltd, a company incorporated in Luxembourg, is the 100% shareholder of Rovelli Ltd, a company incorporated in Malta but having its management and control in Thailand. There is no double tax treaty between Malta and Thailand.

Rovelli Ltd is the 10% shareholder of Rovelli Italy Ltd, a company incorporated and tax resident in Italy. Rovelli Italy Ltd distributes an annual dividend of €5 million to Rovelli Ltd. In terms of Italian domestic law, dividend distributions to non-residents are subject to a withholding tax of 26%. There is a double tax treaty between Malta and Italy.

Rovelli Holding Ltd has funded Rovelli Ltd through a profit participating loan, i.e. a loan which has attributes of both debt and equity. In terms of this loan, 90% of the profits of Rovelli Ltd will be paid up to Rovelli Holding Ltd. Rovelli Ltd is allowed a deduction against its chargeable income in Malta for the payment made to Rovelli Holding Ltd.

Required:

(i) **Explain the taxation of the dividend distributed to Rovelli Ltd from Rovelli Italy Ltd in terms of the Malta–Italy Double Tax Treaty and the application of the Parent–Subsidiary Directive, with specific reference to the conditions required for the application of the Directive.**

Note: For the purposes of answering this question you should assume that the Malta–Italy Double Tax Treaty is similar in all respects to the OECD Model Tax Treaty. (9 marks)

(ii) **Assuming that the conditions for the application of the Parent–Subsidiary Directive are satisfied, comment on the application of the Parent–Subsidiary Directive with respect to the profits paid to Rovelli Holding Ltd in terms of the profit participating loan in Luxembourg.** (3 marks)

(b) Penguin Holding Ltd, a company incorporated in Luxembourg, is the 100% shareholder of two companies: Penguin Malta Finance Ltd, a company incorporated and managed and controlled in Malta, and Penguin Spain Ltd, a company incorporated and tax resident in Spain. Penguin Spain Ltd is the 100% shareholder of Penguin Software Ltd, a company also incorporated and tax resident in Spain.

Penguin Malta Finance Ltd provided a loan of €50 million to Penguin Software Ltd on which interest at 2% is payable annually. In terms of Spanish domestic law, interest payments to non-residents are subject to a withholding tax of 19%. There is a double tax treaty between Malta and Spain.

Required:

Explain the taxation treatment of the interest paid to Penguin Malta Finance Ltd by Penguin Software Ltd in terms of the Malta–Spain Double Tax Treaty and the effect, if any, of the Interest and Royalties Directive. You should make specific reference to the conditions necessary for the application of the Directive.

Note: For the purposes of answering this question you should assume that the Malta–Spain Double Tax Treaty is similar in all respects to the OECD Model Tax Convention. (8 marks)

(20 marks)

End of Question Paper