

---

# Answers

---

Marks

1 Mr Costantinos

(a) Capital/(net worth) statement

|                                   |  | 1 January<br>2006<br>€ | 31 December<br>2011<br>€ |     |
|-----------------------------------|--|------------------------|--------------------------|-----|
| Assets                            |  |                        |                          |     |
| Bank deposit account              | (note 1)                                       | 100.000                | 334.000                  | 1   |
| Business equipment                | (note 5) (20.000 + 5.000)                      | –                      | 25.000                   | 1   |
| Debtors                           | (note 4) (64.000 + 16.000)                     | –                      | 80.000                   | 1   |
| Investments                       | (note 2) (working 1)<br>(6.000 shares at 4,60) | –                      | 27.600                   | 1   |
| Motor vehicles                    | (note 3) (20.000 + 30.000)                     | –                      | 50.000                   | 1   |
| Total assets                      |  | 100.000                | 516.600                  |     |
| Liabilities                       |  |                        |                          |     |
| Personal bank overdraft           |  | (50.000)               | (60.000)                 | 0.5 |
| Business bank overdraft           |  |                        | (40.000)                 | 0.5 |
| Saloon car creditor               | (note 3)                                       |                        | (30.000)                 | 0.5 |
| Trade creditors                   |  |                        | (60.000)                 | 0.5 |
| Net assets                        |  | 50.000                 | 326.600                  |     |
| Less net assets at 1 January 2006 |  |                        | (50.000)                 | 0.5 |
| Capital increase for the period   |  |                        | 276.600                  |     |
| Add:                              |  |                        |                          |     |
| Residential house rent            | (note 6) (72 months x 500)                     |                        | 36.000                   | 1.5 |
| Social insurance contributions    | (note 6)                                       |                        | 22.000                   | 0.5 |
| Income taxes                      | (note 6) (10.000 + 50.000)                     |                        | 60.000                   | 0.5 |
| Loss on sale of investments       | (note 2) (working 1)<br>(4.000 x (4,60 – 4))   |                        | 2.400                    | 1   |
| SDC tax on interest income        | (note 1) ((17.000 x 100/85) – 17.000)          |                        | 3.000                    | 1.5 |
| Living expenses                   | (note 8)                                       |                        | 240.000                  | 0.5 |
| Total assets and expenses         |  |                        | 640.000                  |     |
| Deduct                            |  |                        |                          |     |
| Salaried income                   | (note 6)                                       |                        | (100.000)                | 1   |
| Business income                   | (note 8) (300.000 + 50.000)                    |                        | (350.000)                | 1   |
| Interest income                   | (note 1) (17.000 x 100/85)                     |                        | (20.000)                 | 1   |
| Taxable Income for the period     |  |                        | 170.000                  |     |

Working 1

8.000 shares at €5 each = €40.000

2.000 shares at €3 each = €6.000

|              |                       |                 |    |
|--------------|-----------------------|-----------------|----|
| Average cost | €46.000/10.000 shares | €4,60 per share | 1  |
|              |                       |                 | 17 |

- (b) (i) For businesses who are obliged to keep accounting books, the books should be updated no later than four months from the month the transaction was made. 1
- (ii) Invoices must be issued within 30 days from the date the transaction was made, unless the taxable person requests an extension in writing from the Commissioner and an extension of the deadline is granted to him. 2
- (iii) A business which has inventory must perform an annual stock take and the records of such a stock take should be available to the Inland Revenue Department upon request. 2

- (iv) The Commissioner has the right to enter and inspect buildings used for the purpose of the business (except the private residence), and to inspect the documents and goods of a business, provided that the business which is housed in these buildings is operating during its normal working hours. Reasonable notice must be given for such an inspection.

3

25

## 2 Paradisos Ltd

### (a) Income tax computation for the year ended 31 December 2010

|  | €            | €                    |     |
|--|--------------|----------------------|-----|
| Net profit   |              | 600.000              | 0·5 |
| Add:   |              |                      |     |
| Legal expenses for the increase in share capital                                 | 750          |                      | 0·5 |
| Saloon car expenses (note 4)   | 1.000        |                      | 0·5 |
| Trade goodwill purchased (note 1)  | 35.000       |                      | 0·5 |
| Loss on revaluation of shares  | 10.000       |                      | 0·5 |
| Bonus paid to the sales director (allowable expense)                             | 0            |                      | 0·5 |
| Provisional tax and defence tax paid (10.000 + 13.000)                           | 23.000       |                      | 1   |
| Depreciation   | 28.000       |                      | 0·5 |
| Balancing addition (note 6(a)) (working 1)                                       | 2.000        |                      | 0·5 |
| Interest restriction on:   | €            |                      |     |
| – director's flat (note 5(a)) (52.000 x 9%)                                      | 4.680        |                      | 1   |
| – purchase of Ouranos Ltd shares (100.000 x 5%)                                  | 5.000        |                      | 1   |
| – private saloon vehicle – no cost   | 0            |                      | 1   |
|  | <u>9.680</u> |                      |     |
| Maximum restriction actual interest paid   | <u>8.000</u> |                      | 1   |
|  |              | 107.750              |     |
| Less:  |              |                      |     |
| Purchase cost of goodwill in 2006 (note 1)                                       | 10.000       |                      | 1   |
| Dividends – exempted from corporation tax  | 2.000        |                      | 0·5 |
| Gross interest on bank deposits (taxed under SDC)                                | 3.000        |                      | 0·5 |
| Interest receivable from a non trading loan to holding company (note 3)          | 9.000        |                      | 1   |
| Computer software – capital allowances fully used (note 6(b))                    | 0            |                      | 1   |
| Capital allowances of the shop in London (note 2)<br>(3% x (100.000 – 28.000))   | 2.160        |                      | 1   |
| Capital allowances on new computer hardware (note 6(a)) (45.000 x 20%)           | <u>9.000</u> |                      | 1   |
|  |              | (35.160)             |     |
| Taxable income   |              | 672.590              |     |
| Loss for the year from Ouranos Ltd (note 5(b)) – classified as inventory (stock) |              | 0                    | 1   |
| Loss for the year from Kipos Ltd (item i)  |              | <u>(18.000)</u>      | 1   |
| Taxable income   |              | <u>654.590</u>       |     |
| Corporation tax 10%  |              | 65.459               | 0·5 |
| Provisional tax  |              | <u>(10.000)</u>      | 1   |
|  |              | 55.459               |     |
| Foreign tax credit on rental income from UK (note 2)                             |              | <u>(15.000)</u>      | 1   |
|  |              | 40.459               |     |
| Additional tax 10% (75% of 40.459 is greater than 10.000)                        |              | <u>4.046</u>         | 1·5 |
| Corporation tax payable  |              | <u><u>44.505</u></u> |     |

**Marks**

**Working 1**

**Balancing statement**

|  | €                   |           |
|--|---------------------|-----------|
| Cost   | 30.000              | 0·5       |
| Capital allowances 2006 to 2009 (4 years x 20% x 30.000) | (24.000)            | 1         |
|  | <u>6.000</u>        |           |
| Tax written down value                                   | (8.000)             | 0·5       |
| Sale proceeds  | <u>2.000</u>        |           |
| Balancing addition                                       | <u><u>2.000</u></u> | <u>23</u> |

**(b) Deemed dividend distribution**

|   | €             | €                     |                  |
|---|---------------|-----------------------|------------------|
| Accounting profit   |               | 600.000               |                  |
| Add:  |               |                       |                  |
| Loss on revaluation of shares   | 10.000        |                       | 1                |
| Depreciation due to the revaluation of immovable property (note 6(c)) | <u>20.000</u> |                       | 1                |
|   |               | <u>30.000</u>         |                  |
|   |               | 630.000               |                  |
| Less: Taxes paid (15.000 + 65.459 + 13.000)                           |               | <u>(93.459)</u>       | 1·5              |
| Adjusted accounting profit  |               | <u><u>536.541</u></u> |                  |
| <b>Special contribution for defence (SDC)</b>                         |               |                       |                  |
| Deemed dividend 70% x 536.541   |               | 375.579               | 1                |
| Less dividend paid  |               | <u>(70.000)</u>       | 0·5              |
| Profit subject to deemed dividend distribution                        |               | <u>305.579</u>        |                  |
| SDC for Cyprus tax resident (Pyli Ltd) (note 3) 17% x 85% x 305.579   |               | 44.156                | 1                |
| The SDC is payable by 31 January 2013                                 |               |                       | <u>1</u>         |
|   |               |                       | <u>7</u>         |
|   |               |                       | <u><b>30</b></u> |

**3 Alexandros**

**(i) Sale of main residence**

|   | €               | €                |   |
|---|-----------------|------------------|---|
| Sale proceeds 15 January 2010 (€720.000 x 50%)              |                 | 360.000          | 1 |
| Less:   |                 |                  |   |
| Cost 12 April 1995 (€400.000 x 50%)                         | (200.000)       |                  | 1 |
| Indexation allowance ((€200.000 x 112·60/75·47) – €200.000) | <u>(98.397)</u> |                  | 1 |
| Renovation cost October 2005 (€100.000 x 50% x 50%)         | (25.000)        |                  | 1 |
| Indexation allowance ((€25.000 x 112·60/102·38) – €25.000)  | <u>(2.496)</u>  |                  | 1 |
|   |                 | <u>(325.893)</u> |   |
| Capital gain  |                 | 34.107           |   |
| Lifetime exemption (working 1)                              |                 | <u>(34.107)</u>  | 1 |
| Taxable capital gain  |                 | <u>0</u>         |   |
| <b>Working 1</b>  |                 |                  |   |
| Lifetime exemption available (€85.430 x 50%)                |                 | 42.715           | 1 |
| Lifetime exemption used for the main residential house      |                 | <u>(34.107)</u>  |   |
| Remaining lifetime exemption                                |                 | <u>8.608</u>     |   |

|  |           |           | Marks     |
|--|-----------|-----------|-----------|
| <b>(ii) Sale of land in Limassol</b>   |           |           |           |
|  | €         | €         |           |
| Sale proceeds 15 September 2010  |           | 400.000   | 0·5       |
| Less:  |           |           |           |
| Cost September 2002  | (100.000) |           | 0·5       |
| Indexation allowance ((€100.000 x 112·69/92·74) – €100.000)                                  | (21.512)  |           | 1         |
| Transfer fees  | (8.000)   |           | 1         |
|  |           | (129.512) |           |
| Capital gain   |           | 270.488   |           |
| Lifetime exemption not used  |           | (8.608)   | 1         |
| Taxable capital gain   |           | 261.880   |           |
| Capital gains tax payable at 20%   |           | 52.376    | 0·5       |
| <b>(iii) Exchange of the plot no. 14</b>   |           |           |           |
|  | €         | €         |           |
| Sale proceeds of plot 14 October 2010 (market value)   |           | 200.000   | 0·5       |
| Less:  |           |           |           |
| Cost of plot no. 14 February 1997  | (100.000) |           | 0·5       |
| Indexation allowance ((€100.000 x 114·14/78·08) – €100.000)                                  | (46.240)  |           | 1         |
|  |           | (146.240) |           |
|  |           | 53.760    |           |
| Roll over relief (nil, since €152.962 is greater than value of plot 24, €140.000)            |           | 0         | 1         |
| Capital gain   |           | 53.760    |           |
| Capital gains tax payable at 20%   |           | 10.752    | 0·5       |
| Readjusted value not applicable (no roll over relief).                                       |           |           | 0·5       |
| <b>Tutorial note:</b> <i>Indexation applies from date plot 24 was bought in August 1995.</i> |           |           |           |
| <b>(iv) Exchange of flat</b>   |           |           |           |
|  | €         | €         |           |
| Sale proceeds of flat November 2010 (market value)   |           | 150.000   | 0·5       |
| Less:  |           |           |           |
| Cost of flat August 2000   | (60.000)  |           | 0·5       |
| Indexation allowance((€60.000 x 115·05/86·81) – €60.000)                                     | (19.518)  |           | 1         |
|  |           | (79.518)  |           |
|  |           | 70.482    |           |
| Roll over relief (€79.518 is less than value of plot of land, €120.000)                      |           | (40.482)  | 1         |
| Capital gain   |           | 30.000    |           |
| Capital gains tax payable at 20%   |           | 6.000     | 0·5       |
| <b>Readjusted value of land for future disposals</b>   |           |           |           |
|  |           | €         |           |
| Deemed cost November 2010  |           | 120.000   |           |
| Roll over relief used  |           | (40.482)  |           |
| Readjusted value   |           | 79.518    | 1         |
|  |           |           | <b>20</b> |

- 4 (a) The following conditions must be satisfied for input VAT to be recoverable:
1. The claimant must be a taxable person at the time of the supply (*unless qualifying under the pre-registration conditions*).
  2. The supply must be made to the claimant.
  3. The supply must be supported by the required evidence (e.g. VAT invoice/customs clearance documentation).
  4. The goods or services must be used by the claimant for business purposes.
  5. The goods or services provided must not be specifically non-deductible (e.g. business entertaining; the cost of a private passenger car).
  6. The goods or services must not relate to the making of exempt supplies (*unless within the de minimis limits*).

1 mark each condition, maximum 5

**Note:** Candidates were not expected to include the qualifications given in italics in their answer. This information is provided for tutorial purposes only.

(b) Sotiroulla

Value added tax (VAT) return for the quarter ending 30 June 2011

|   |                |                  |
|---|----------------|------------------|
| <b>Output VAT</b>   | €              |                  |
| Cash sales (€42.000 x 15%)  | 6.300          | 1                |
| Credit sales (€12.000 x 95% x 15%)                                | 1.710          | 2                |
| Total output VAT  | <u>8.010</u>   |                  |
| <b>Input VAT</b>  | €              | €                |
| Purchases and expenses (standard rated)                           | 11.200         |                  |
| Less leasing of saloon car (private motor vehicle)                | <u>(2.000)</u> | 1.5              |
| Purchases and expenses  | <u>9.200</u>   |                  |
| VAT input on standard rated purchases and expenses (€9.200 x 15%) |                | 1.380 1          |
| Purchases (reduced rate)  | 6.000          |                  |
| Less lunch with clients (business entertaining)                   | <u>(300)</u>   | 1.5              |
| Purchases   | <u>5.700</u>   |                  |
| VAT input on reduced rate purchases (€5.700 x 5%)                 |                | 285 1            |
| Expenses (exempt from VAT)  |                | <u>0</u> 0.5     |
| Input VAT   | <u>1.665</u>   |                  |
|   | €              |                  |
| Total output VAT  | 8.010          |                  |
| Total input VAT   | <u>1.665</u>   |                  |
| VAT payable   | <u>6.345</u>   | 0.5              |
| Due date of submission of return is 10 August 2011                |                | <u>1</u>         |
|   |                | <u>10</u>        |
|   |                | <u><b>15</b></u> |

5 (a) The self assessment system for temporary tax

- Self-assessment for temporary tax for self-employed individuals means that the self-employed individual has to calculate their own income tax on form IR5 during the year and make current year payments. 1
- The self assessment temporary tax return should be completed and used to pay the first instalment of the temporary tax due by 1 August. It is submitted in duplicate. One copy is returned to the taxpayer to be used for making the following two current year payments due by 30 September and 31 December. 2
- The temporary self-assessment may be revised by the taxpayer at any time before the end of the current year, i.e. before 31 December. The revision is made on a similar new return. If the revised tax payable is higher than the tax declared on the first temporary tax return, interest on the balance of tax payable is calculated from the due date of payment (1 August, 30 September). 2

**Marks**

If the temporary income declared is lower than the income finally determined by more than 25%, the final tax payable is increased by an additional amount of tax equal to 10%. The imposition of the 10% additional tax is also made where no temporary tax return is submitted and the Director does not issue a temporary tax return, because in such a case the temporary income is deemed to be nil for the purposes of the temporary tax provisions.

2  
7

**(b) The self assessment system for final tax and the filing of the return**

Individuals with an obligation for the keeping of accounting books and records and the preparation of audited accounts should submit the self assessment and pay the tax due on or before 1 August of the year that follows the year of assessment. Filing of the return is on 31 December following the year of assessment.

1·5

Individuals with an obligation to issue invoices and receipts and an obligation for keeping accounting books and records and the preparation of unaudited accounts may submit their return up to 30 June of the following year of assessment. Payment of final tax is on or before 1 July of the year that follows the year of assessment.

1·5  
3  
**10**