
Answers

1 (a) Costas Costoulas

Marks

(i) Income tax for 2012

	€	€	
Employment (worldwide)			
Salary income		110.000	½
Accommodation benefit		12.000	½
Accommodation ancillary expenses benefit (1.700 + 500)		2.200	1
Car benefit (200 + 700 + 2.000 + 5.000) x 30%		2.370	1
		<u>126.570</u>	
Less: Exemptions			
Executive exemption (50% x €126.570)		(63.285)	1
First employment exemption (will be available in 2013–2015)		0	1
		<u>63.285</u>	
Less: Deductions from gross income			
Subscription to ETEK	(300)		1
Donation to FC Apoel	0		½
Donation to an approved charity	(300)		1
Seminar related to his job	(200)	(800)	1
		<u>62.485</u>	
Net employment income			
Add: Other sources of income			
Paphos apartment – rental income (€24,000 x 50%)	12.000		½
Less: 20% deduction on rental income (€12.000 x 20%)	(2.400)		½
Less: Capital allowances: ((€300.000 – €100.000) x 3% x 12/12) x 50%	(3.000)		1
Less: Loan interest (€2.000 x 50%)	(1.000)	5.600	½
		<u>68.085</u>	
Net income			
Less: Personal allowances			
Social insurance contributions payable (maximum €53.304 x 6,8%)	(3.625)		1
Life insurance in his own name (€8.000, but restricted to 7% of the sum assured – €100,000 x 7% = €7.000)	(7.000)		1
		<u>(10.625)</u>	
Restricted to 1/6th of net income (1/6 x €68.085 = €11.348)		(10.625)	1
Taxable income		<u>57.460</u>	
Tax liability			
€0–€19.500 at 0%		0	
€19.501–€28.000 at 20%		1.700	
€28.001–€36.300 at 25%		2.075	
€36.301–€57.460 at 30%		6.348	
		<u>10.123</u>	½
Total tax liability			
Less: Tax paid		(10.500)	½
PAYE			
Income tax refundable		<u>(377)</u>	
			<u>15</u>

(ii) Exemptions available

1. Executive exemption

- Non-Cyprus tax resident before the commencement of employment in Cyprus.
- Total emoluments above €100.000.
- 50% of employment income will be exempt for five years.

1½

2. First employment income

(not available based on the IR position if the executive exemption is given)

- Non-Cyprus tax resident before the commencement of employment in Cyprus.
- The lower of €8.550 or 20% of employment income will be exempt for three years, starting from the next year.

1½

3

(iii) Special defence contribution (SDC)**Rent from apartment**

	€	
Gross rental income (€24.000 x 50%)	12.000	
Less: 25% deduction	(3.000)	½
Taxable	9.000	
SDC liability x 3%	270	½
Payable half-yearly, due dates:		
– 30 June 2012	€135	
– 31 December 2012	€135	1
		<u>2</u>

(b) Eleni**(i) Employed or self-employed**

The following criteria should be considered when deciding whether an individual is employed or self-employed. All relevant factors need to be taken into account and a common sense approach adopted.

Engagement agreement

If the business does not have an obligation to offer work and the individual is not obliged to accept any of the contracts offered to her, this is an indication of a self-employment agreement. An employee is not in a position to decline work given to her if this is within the duties of the post for which she is employed. Eleni is not obliged to accept the work offered by Clever Ideas Ltd.

Control test

If the individual is not under the control and supervision of the employer as to the manner in which the work is carried out, this would suggest the individual is self-employed. Eleni carries out the work under her own control.

Place of work

If the individual does not have an obligation to attend the place of work at specified times, this would suggest the individual is self-employed. Eleni works from her own home.

Payment

If the payment for the work does not consist of a fixed salary element which is payable at regular intervals, this would suggest the individual is self-employed. Eleni will be paid a fixed fee for each software development project which she works on.

Employment benefits

If the individual carrying on the work is not entitled to benefits which are usually given to employees, such as sick leave, vacation leave, workplace pension, etc, this would suggest the individual is self-employed. There is no indication that Eleni will be entitled to such benefits.

Work performance and correction of unsatisfactory work

If the individual is required to correct unsatisfactory work at her own expense before payment is made, this would suggest the individual is self-employed. Eleni will be paid after each software development project has been completed satisfactorily.

Provision of equipment

If the individual provides the tools and equipment to carry out the work, this would suggest the individual is self-employed. Eleni will use her own equipment.

Financial risk

If the individual has economic risks with regards to the work to be performed, this would suggest the individual is self-employed. Eleni has to complete a software development project in order to get paid.

Insurance

If the employer does not take out professional indemnity and/or public liability insurance for the worker, this would suggest the individual is self-employed. There is no indication that Eleni will be entitled to such benefit.

Service contract/Contract for services

A self-employed individual works within the framework of a contract for services, with all the associated risks.

		Marks
(ii) Income tax for 2012		
	€	€
Business income		
Income from software development projects		50.000
Less: Allowed expenses		
Use of office – room in flat (€5.000 x ½)	(2.500)	
Telephone bill (excess cost incurred for business purposes)	(500)	
Capital allowances – computer (€2.000 x 20%)	(400)	
		(3.400)
Trading income		46.600
Less: Personal allowances		
Social insurance contributions payable	(3.000)	
		(3.000)
Restricted to 1/6th of net income ($1/6 \times €46.600 = €7.767$)		
Taxable income		43.600
		4
		30

2 Alasia Ltd

(a) Tax adjusted trading profit for 2012

	€	€	
Business income			
Accounting profit		612.660	
Add: Disallowed expenses			
Depreciation	54.200		1/2
Loss on disposal of a saloon car (Note 1)	5.000		1/2
Gifts and donations (Note 2):			
Gifts to customers (promotional expenses)	0		1/2
Donation to AKEL (recognised political party)	5.200		1/2
Donation to Nicosia Municipality (local authority)	0		1/2
Bad debts (Note 3):			
Trade debts written off	0		1/2
Loan to a director written off	4.100		1/2
Professional fees (Note 4):			
Accountancy and audit fee (revenue item)	0		1/2
Legal fees – acquisition of a plot of land (capital item)	1.100		1/2
Legal fees – debt collection (revenue item)	0		1/2
Salaries (Note 5):			
Gross salaries	0		1/2
Contributions to approved funds	0		1/2
Unpaid salaries and contributions	20.000		1/2
Repairs and renewals (Note 6):			
Replacing the roof of a factory building (revenue item)	0		1/2
Extending the factory building (capital item)	100.700		1/2
Repairs to plant and machinery (revenue item)	0		1/2
Other expenses (Note 7):			
Entertaining expenses (€15.000 – €13.000)	2.000		1
Maximum allowed is the lower of:			
– €17.086, and			
– 1% of the turnover (1% x €1.300.000) €13.000			
Interest payable (Note 10) – no restriction applies as the private assets are older than seven years	0		1 1/2
		192.300	
Deduct: Exempt income			
Profit from disposal of furniture (Note 1)	(2.000)		1/2
Profit from disposal of factory building No. 2 (Note 1)	(188.100)		1/2
Trade bad debts recovered from previous years (Note 3)	0		1/2
Profit from disposal of shares (Note 8)	(10.000)		1/2
Interest received (Note 9):			
On loan to a customer	(11.360)		1/2
From bank deposits	(1.000)		1/2
		(212.460)	
Deduct: Allowed expenses/charges not included in the financial statements			
Old assets (Note 1):			
Machines (purchased in 2007: €10.000 x 10%)	(1.000)		1/2
Saloon car (purchased in 2004: not eligible for capital allowances)	0		1/2
Furniture (purchased in 2000: fully allowed asset)	0		1/2
Computer hardware (purchased in 2008: €2.000 x 20%)	(400)		1/2
Factory No. 1 (purchased in 2000: (€320.000 – 150.000) x 4%)	(6.800)		1/2
New assets (Note 1):			
Furniture (purchased in 2012: €10.000 x 20% increased rate)	(2.000)		1/2
Extension of the factory building No. 1 (Note 6)			
(Constructed in 2012: €100.700 x 7% increased rate)	(7.049)		1/2
Disposals (Note 1) – balancing adjustments			
Furniture – balancing charge (W1)	1.400		2 (W1)
Saloon car – no balancing adjustment	0		1/2
Factory No. 2 – balancing charge (W2)	51.408		2 1/2 (W2)
		35.559	
Tax adjusted profit		628.059	

Workings:

(1) Balancing adjustment – furniture (Note 1)

	€	
Cost	8.000	
Less: Capital allowances claimed (2004–2011) (10% x €8.000 x 8 years)	(6.400)	1
Tax written down value (TWDV) 1 January 2012	1.600	1/2
Deduct from disposal proceeds	3.000	
Balancing charge	1.400	1/2
		<u>2</u>

(2) Balancing adjustment – factory No. 2 (Note 1)

	€	
Cost (€137.100 – €30.000)	107.100	
Less: Capital allowances claimed (2000–2011) 4% x (€137.100 – €30.000) x 12 years	(51.408)	1
TWDV 1 January 2012	55.692	1/2
Deduct from disposal proceeds	250.995	
Balancing charge – restricted to capital allowances claimed	51.408	1
		<u>2 1/2</u>

Tutorial notes:

- Salaries for which social insurance contributions have not been paid by the due dates specified by the law are not tax deductible.
- Interest deemed to be attributed to the acquisition of saloon cars or to the acquisition of any other private asset is not tax deductible. The restriction applies for seven years, starting from the year of the acquisition of the relevant asset. However, both the saloon car (note 1) and the shares (note 8) were purchased more than seven years ago and, as a consequence, the restriction is not applicable.

(b) Taxable profit and tax payable for 2012

	€	
Tax adjusted profit	628.059	
Less: Group loss relief (Loss of Ledra Ltd)	(46.800)	1
Taxable profit	581.259	
Corporation tax liability at 10%	58.126	1/2
Less: Temporary tax paid	(30.000)	1/2
Corporation tax liability balance	28.126	
Add: 10% Additional tax (estimate lower than 75% of €58,126)	2.813	1
Corporation tax payable	30.939	
		<u>3</u>
		<u>25</u>

Tutorial note: Group relief is available because Alasia Ltd and Ledra Ltd form a group for group relief purposes as Alasia Ltd owns more than 75% of the share capital of Ledra Ltd; and in cases where a company is incorporated by its parent company during the tax year, the subsidiary company is deemed to be a member of the group for the whole of that tax year.

3 Aristos Kyrios

(a) (i) Principal dwelling house exemption

The principal dwelling house exemption can be given if the following conditions are satisfied:

- the capital gain has been derived from the disposal of the individual's principal dwelling house; 1/2
- the house was used by the owner exclusively for his own habitation for a total period of at least five years; 1/2
- the house is situated on land not exceeding 1 1/2 decares (1.500 m²); 1/2
- the gain in respect of any excess over the 1 1/2 decares is taxable; 1/2

			Marks
– the exempt amount cannot exceed €85.430 during the lifetime of the specific taxpayer;			½
– the own habitation time limit is extended to ten years in the case of the disposal of a dwelling house for the second or more times;			½
– no exemption is given where the disposal takes place after the lapse of one year from the cessation of the owner's own habitation; and			½
– in the case of joint ownership, the exemption is restricted to the percentage of ownership.			½
			<u>4</u>
(ii) The principal dwelling house exemption is not available as the house was let out from 2001 onwards, so the disposal took place after the lapse of one year from the cessation of Aristos' own habitation of the property.			<u>1</u>
(b) Chargeable gain on the exchange of the old family house with a new flat			
	€	€	
Disposal proceeds 31 March 2012 (market value of the house at the exchange date)		265.000	1
Less: Acquisition cost			
Cost of the house (acquired before 1 January 1980, therefore, market value on 1 January 1980)	(26.500)		1
Add: Indexation allowance €26.500 x (117,52/34,96)	(62.581)		1
		(89.081)	
Less: Additions			
Structural alterations	(25.000)		1
Add: Indexation allowance €25.000 x (117,52/82,71)	(10.522)		1
		(35.522)	
Less: Incidental expenses			
Commission paid to a non-approved agent		0	1
Add: Capital allowances claimed (2001 to 2010: 10 years)			
Original cost: €20.000 x 3% x 10 years	6.000		1
Additions: €25.000 x 3% x 10 years	7.500		1
		13.500	
Capital gain		153.897	
Less:			
Roll-over relief			
Market value of property received – flat	150.000		½
Less: Indexed cost of property given – house			
Original cost (as above)	(89.081)		½
Alterations (as above)	(35.522)		½
Gain reinvested	25.397		
Relief available		(25.397)	½
General lifetime exemption (not used in the past)		(17.086)	1
Chargeable gain		111.414	
Restated value of the new flat for capital gains purposes (150.000 – 25.397 (gain reinvested))		€124.603	1
			<u>12</u>
(c) Compliance obligations			
Aristos must submit a self-assessment declaration of disposal of property (form 401) in respect of the disposal and pay the tax due by 30 April 2012 (within one month from the date of disposal).			1½
If no return is submitted, the Director of Inland Revenue may issue a best judgement assessment on the basis of the information available to him.			1
Also, interest at the rate of 5% per annum will be payable on the tax due for each day of delay.			½
			<u>3</u>
			<u>20</u>

4 Petroulas Sports Ltd

(a) Value added tax (VAT) for the three months to 31 December 2012

	€	€	
Output VAT			
Sales (€19.500 x 17%)		3.315	½
Less: Sales returns (€1.100 x 17%)		(187)	½
		<u>3.128</u>	
Understatement of sales on last return (€1.000 x 17%) (Note 6)		170	1
		<u>3.298</u>	
Input VAT			
Purchases (€9.500 x 17%)	1.615		½
Purchase returns (€500 x 17%)	(85)		½
Bad debts written off (€500 x 15%)	75		½
Salaries (not taxable)	n/a		½
Customer entertaining (not recoverable)	0		1
Staff entertaining (€500 x 17%)	85		½
Car fuel charge (€585 x 30% x 17/117)	26		1
Other expenses ((€2,400 – €500) x 17%)	<u>323</u>		1
		<u>(2.039)</u>	
VAT payable		<u>1.259</u>	½
Due date of payment: by 9 February 2013			<u>1</u>
			<u>9</u>

Tutorial note: If input tax is reclaimed in full on petrol (business and private), then the business must account for output VAT on the car fuel charge. Hence it is beneficial for the business to claim the input tax only on the business part.

(b) Treatment of items

(i) Bad debt relief (Note 4)

VAT bad debt relief can only be claimed if:

- the debt has been written off as a bad debt, and
- at least 12 months has elapsed since the due date of the payment.

The debt written off satisfies these conditions as it was originally due on 28 February 2011. 1

(ii) Invoice omitted in error in the previous quarter (Note 6)

Errors on VAT returns can be amended in a current return by voluntary correction if:

- the understatement of output tax on the previous return did not exceed €1.709; and
- the correction is made within three years.

Therefore, the error made in the previous quarter can be corrected in the quarter ended 31 December 2012; also, any additional tax, penalties and interest will be avoided.

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(c) Importance of the tax point

The tax point is the deemed date of supply and determines the VAT period in which output VAT must be accounted for, and/or credit for input VAT allowed. 2

The tax point also determines the applicable VAT rate, relevant if there is a VAT rate or a VAT category change. 1

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5 Perikles Wise

(a) Income tax, special defence contribution (SDC) and social insurance contributions (SIC)

(i) Additional director's remuneration

	€	€	
Director's salary (€40.000 + €50.000)		90.000	1/2
Less: Personal allowances			
Social insurance contributions payable (maximum €53.304 x 6,8%)	(3.625)		1/2
	<u>(3.625)</u>		
Restricted to 1/6th of net income ($1/6 \times €90.000 = €15.000$)		(3.625)	1/2
Taxable income		<u>86.375</u>	
Tax liability			
€0–€19.500 at 0%		0	
€19.501–€28.000 at 20%		1.700	
€28.001–€36.300 at 25%		2.075	
€36.301–€60.000 at 30%		7.110	
€60.000–€86.375 at 35%		<u>9.231</u>	
Total tax liability		<u>20.116</u>	1/2
– Perikles' additional income tax liability for 2012 will be €16.047 (€20.116 – €4.069 deducted under PAYE system).			1
– The additional employee's SIC will be €905 ((€53.304 – €40.000) x 6,8%).			1
– The additional SDC is nil as salaries are outside the scope of SDC.			1/2

(ii) Dividend

– Perikles' additional income tax liability for 2012 will be nil as dividends are exempt income.			1
– Perikles' additional SIC for 2012 will also be nil as dividends are not subject to SIC.			1/2
		€	
Gross dividends (€50,000 x 100/80)		<u>62.500</u>	1/2
SDC liability at 20%		<u>12.500</u>	1/2
			<u>7</u>

(b) Additional employer's SIC due by Alpha Ltd

(i) Additional director's remuneration

– The additional employer's SIC will be €905 ((€53.304 – €40.000) x 6,8%).			1/2
– The additional employer's social cohesion fund will be €1.000 (€50.000 x 2%, no upper limit restriction for the social cohesion fund).			1
– The additional employer's redundancy fund will be €160 ((€53.304 – €40.000) x 1,2%).			1/2
– The additional employer's industrial training fund will be €67 ((€53.304 – €40.000) x 0,5%).			1/2

(ii) Dividend

– Employer's additional SIC for 2012 will be nil as dividends are not subject to SIC.			1/2
			<u>3</u>
			<u>10</u>