

# Examiner's report

## F6 (CYP) Taxation

December 2017

### General Comments

There were two sections to the examination paper and all of the questions were compulsory. Section A consisted of 15 multiple choice questions (two marks each) which covered a broad range of the syllabus topics.

Section B had four questions worth 10 marks each and two longer questions worth 15 marks each, testing the candidates' understanding and application of Cyprus Taxation in more depth.

The following paragraphs report on each section and focus on some of the key learning points.

### Specific Comments

#### Section A

It was very pleasing to see that almost all candidates attempted all of the questions. Candidates preparing for the next examination of F6 (Cyprus) are advised to work through the sample questions discussed here and to carefully review how each of the correct answers were derived.

Section A questions aim to provide a broad coverage of the syllabus, and future candidates should aim to revise all areas of the F6 (Cyprus) syllabus, rather than attempting to question spot.

The following question is reviewed with the aim of giving future candidates an indication of the types of questions asked.

#### Question 1

Eleni had the following income in the year 2016:

- Gross interest from bank deposits of €2,000
- A pension of €5,850
- Net dividend income of €2,400 from a Cyprus tax resident company

**What is the special defence contribution Eleni has to pay or recover for 2016?**

- A** €600
- B** €60
- C** €540
- D** €1,008

This question tested whether candidates were able to identify the income that was subject to special defence contribution and their ability to apply the reduced special defence contribution rate of 3% on interest income from bank deposits.

An individual whose total income does not exceed €12,000 is entitled to a refund of the special defence contribution withheld at source, following an application to the Tax Department, in order to have an effective reduced special defence contribution rate of 3%.

Therefore in this question, the individual was taxed at 30% withholding tax on interest income from bank deposits and is entitled to a refund of 27% (i.e. €540).

Option (A) €600, ignored the pension and the dividend income and applied a special defence contribution rate of 30% on interest income resulting to €600. This option did not take in consideration the total income of the individual which is below €12,000 and thus entitled to the reduced special defence contribution rate of 3%.

Option (B) €60, ignored the pension and the dividend income and applied a reduced special defence contribution rate of 3% on interest income resulting to €60. This option ignored the fact that a 30% special defence contribution has already been withheld at source and therefore the individual is entitled to a refund.

Option (C) €540, ignored the pension and dividend income. It calculated the 30% special defence contribution on interest income which was withheld at source of €600 and applied the reduced special defence contribution of 3% that the individual is entitled to, resulting to €60. Therefore, the individual is entitled to a refund of €540.

Option (D) €1,008, ignored the pension income and applied special defence contribution of 30% on the interest income and 17% on the dividend income.

The correct answer was C €540.

## Question 2

James had the following income in the year 2016:

- Gross employment income of €30,000
- Gross rental income of €7,200
- Expenses incurred for the rented property of €2,000

The value of the rented property (excluding the value of the land) is €250,000.

### What is James's chargeable income for the year 2016?

- A €25,920
- B €28,260
- C €27,660
- D €23,920

This question tested whether candidates were able to correctly calculate the chargeable income for an individual with more than one source of income. Candidates were expected to deduct the social insurance contributions applicable to the gross employment income, apply the deductions allowed for the rented property and to ignore the actual expenses incurred for the rented property.

Option (A) added the employment income €30,000 and the gross rental income €7,200, deducted €2,340 social insurance contributions, deducted 20% allowance for the rental income €1,440 and 3% wear and tear allowance of €7,500 calculated on the rented property value.

Option (B) added the employment income €30,000 and the gross rental income €7,200, deducted the 20% allowance for the rental income €1,440 and 3% wear and tear allowance of €7,500 calculated on the rented property value. This option ignored the social insurance contributions.

Option (C) added the employment income €30,000 and deducted only the social insurance contributions of €2,340. This option ignored the rental income and the allowable deductions.

Option (D) added the employment income €30,000 and the gross rental income €7,200, deducted €2,340 social insurance contributions, deducted the 20% allowance for the rental income €1,440 and 3% wear and tear allowance of €7,500 calculated on the rented property value. In addition, the actual expenses incurred of €2,000 were also deducted.

The correct answer was A €25,920.

## **Section B**

### **Question One**

This 10-mark question covered the topic of partnership profits.

Part (a) for 8 marks required candidates to calculate the partnership profits assessable to the three partners. Many candidates were able to answer this question very well and the majority of the candidates scored full marks.

Where candidates did not score enough marks, this was because they did not understand in full the requirements of the question. They wasted valuable time detailing the legal aspect of the partnerships, the particulars of the partnership agreement, and other information which were not required. This was a straightforward question which offered easy marks to the candidates.

Part (b) for 2 marks required candidates to briefly explain the procedures for declaring the taxable income from a partnership business to the Tax Department. The candidates were expected to write both the declaration of the chargeable profit in the partners' personal income tax return and the submission of the audited financial statements. Most candidates scored half marks on this part as the majority failed to mention the audited financial statements.

### **Question Two**

Part (a) for 8 marks required candidates to determine the date which a sole trader is required to compulsorily register for VAT, state the action he must take to register and state the default surcharge in case his VAT return is not submitted on time. This was a straight forward question and I was happy to see that the majority of the candidates are confident with such VAT questions. The overall performance on this question was satisfactory.

Candidates were expected to identify the transactions that needed to be adjusted in order to determine the compulsory VAT registration threshold. The majority of the candidates that attempted this part of the question scored full marks.

Common mistakes made by candidates were:

- Many of the candidates ignored that the requirement was to state the surcharge for the late submission of the VAT return and listed all possible surcharges and interests for both VAT and income tax, thus losing valuable time.
- Some candidates stated the option for compulsory VAT registration, which was not a requirement and thus losing valuable time.

Part (b) for 2 marks required candidates to list any four types of goods or services for which no VAT input credit can be deducted. This straightforward 2 mark question appears to have confused the majority of the candidates that attempted this part, as they confused VAT input with VAT

output. The majority of the candidates listed exempt income items and items identified from Part (a) which were not relevant to the requirement.

### Question Three

This 10-mark question required candidates to calculate the capital gains tax payable arising from the disposal of a residential dwelling. The house was built on a piece of land with an area of 7,200 square meters. The candidates were required to calculate the capital gains in respect of the land and the capital gains in respect of the house as the residential dwelling exemption applies only to the gain accruing on the disposal of the principal dwelling house situated on a land not exceeding 1,500 square meters.

All of the candidates attempted this question with the majority scoring enough marks to pass.

Common mistakes made by candidates were:

- Ignoring that fact that the land exceeds 1,500 square meters.
- Not applying the lifetime exemption of €17,086 to the capital gain in respect of the land.
- Not allocating the agent's commission between the capital gain in respect of the land and in respect of the house.
- Not subtracting the lifetime exemption of €17,086 used in respect of the land from the residential dwelling lifetime exemption of €85,430.

### Question Four

This 10-mark question was focused on the temporary tax assessment system and was broken down into 4 parts.

Part (a) for 3 marks required candidates to briefly explain the purposes of the temporary tax assessment system. This requirement appears to have confused the majority of the candidates who listed the whole temporary tax procedure, the option to revise the temporary tax assessment and in general whatever they knew about the temporary tax assessment system. There were candidates who wrote a whole page detailing the temporary tax assessment system, thus losing valuable time, given the fact that they could only score a maximum of 3 marks for this part.

Part (b) for 3 marks required candidates to calculate the temporary tax payments of a company and indicate the due dates for payment. The majority of the candidates scored full marks for this part. Some candidates confused the due dates with the due dates for the submission of the income tax return.

Part (c) for 2 marks required candidates to state the circumstances in which interest will be imposed on a company's temporary tax payments. The majority of the candidates who attempted this part did not score full marks as they confused this with the 10% additional tax which is imposed in case of a low estimation of the temporary tax.

Part (d) for 2 marks required candidates to identify whether there was an overpayment or underpayment of corporation tax and to calculate the interest payable or refundable. The majority of the candidates who attempted this part were able to identify that there was an overpayment of corporation tax but they were not able to calculate the refundable interest.

### Question Five

Part (a) (i) for 6 marks required a calculation of the income tax payable or refundable by a Cyprus tax resident pensioner.

The majority of the candidates scored well in this question.

Common mistakes made by candidates were:

- Candidates failed to identify that the rental income was related to a plot of land therefore the 20% allowance and wear and tear deduction was not an allowable deduction.
- Candidates deducted the housing loan interest which is not an allowable deduction.

Part (a) (ii) for 5 marks required candidates to calculate the total special defence contribution payable by the pensioner.

The majority of the candidates attempted this part and all of them scored good marks.

Part (b) for 4 marks required candidates to calculate the income tax payable by a self-employed individual.

The majority of the candidates attempted this part and most of them scored good marks.

Common mistakes made by candidates were:

- Candidates added as an additional income the weekly income on which the social insurance contributions were calculated.
- Candidates did not deduct the temporary tax payment.
- Candidates did not add the 10% additional tax for low estimation of the temporary tax.

### **Question Six**

This 15-mark question required candidates to calculate the tax loss of a Cyprus tax resident company and state for how long the tax loss can be carried forward.

The majority of the candidates attempted this question and most of them were able to answer this question very well and have presented their answer in a professional style.

Common mistakes made by candidates were:

- The donation to an approved charity was not added back. Donations made whether to approved charities or not, cannot increase tax losses.
- Candidates did not add back the mortgage fees.
- The majority of the candidates failed to restrict the balancing addition to the capital allowances granted.
- Candidates did not add back the legal fees paid in respect of a share capital increase.

Some candidates who did not answer this question to a satisfactory standard, had listed all the items as given in the question, without specifying whether they should be added or deducted in an attempt to score easy marks.

The majority of the candidates who attempted this question answered it correctly stating that the loss can be carried forward for 5 years.