

Examiner's report

F6 (CYP) Taxation

June 2016

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 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 are advised to work through the specimen questions and 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 syllabus, rather than attempting to question spot. The following two questions are reviewed with the aim of giving future candidates an indication of the types of questions asked, guidance on dealing with exam questions and to provide a technical debrief on the topics covered by the specific questions selected.

Sample Questions

Example 1

Mr Kypraios, a Cyprus tax resident person, owns the whole of Cyprus Friendly Ltd (CFL), a Cyprus tax resident company. For the year ended 31 December 2014, CFL made an accounting profit before taxation of €100,000, and had a tax adjusted profit of €120,000 for the tax year 2014. On 30 June 2015 CFL paid out all of its 2014 profits available for distribution as dividends.

What is the special defence contribution payable by Cyprus Friendly Ltd on the dividend paid to Mr Kypraios on 30 June 2015?

- A €14,450
- B €17,000
- C €17,850
- D €0

This question tested the special defence contribution payable by Cyprus Friendly Ltd on the dividend paid to a Cyprus tax resident individual, as a tax of the shareholder (only resident shareholders). Candidates must be able to estimate the corporation tax liability by multiplying the taxable profits with the relevant corporation tax rate. Moreover, candidates must be able to estimate the profits available for distribution by deducting the corporation tax from the profits before tax. As the company fully distributed the profits available for distribution, the whole profit after tax will be treated as a taxable dividend at 17% SDC.

The correct answer was A.

Example 2

A Cyprus value added tax (VAT) registered trader making wholly taxable supplies purchased goods from a trader registered for VAT in another EU member state. The goods purchased had a VAT exclusive price of €20,000 and would be classed as standard rated if they were supplied in Cyprus.

Which of the following statements correctly describes the VAT treatment of the purchase for both parties to the transaction?

- A** The EU trader will zero rate the invoice. The Cyprus trader will account for output VAT of €3,800 in his VAT return and can claim this €3,800 back as input tax on the same return
- B** The EU trader will zero rate the invoice. The Cyprus trader will account for output VAT of €3,800 but cannot reclaim any input VAT as it relates to an overseas transaction
- C** The EU trader will charge VAT at the Cyprus standard rate, so the invoice will show VAT of €3,800. The Cyprus trader can claim back the €3,800 VAT charged as input tax
- D** The EU trader will zero rate the invoice. The Cyprus trader has no output VAT to account for on this transaction, and cannot reclaim any input tax as the transaction is an overseas transaction on which €0 VAT was charged

This question tested the area of intra-community trade of goods and the performance on this question was mixed.

The intra-community supply of goods is treated as zero-rated EU dispatch, provided that the buyer is VAT registered in an EU member state and the seller shows the buyer's VAT registration number on the invoice, after he has verified the buyer's VAT registration number. Moreover, where a person registered for VAT in Cyprus receives goods from another EU member state supplied by a business registered for VAT in that country, he is liable to VAT in Cyprus on the acquisition of the goods. The rate of VAT due is that applicable to the supply of the same goods in Cyprus, i.e. 19%.

Hence, the correct answer was A.

Section B**Question One**

This 10-mark question covered the topics of the calculation of value added tax payable and the compulsory VAT deregistration.

Part (a) for 7 marks required candidates to calculate the amount of value added tax (VAT) payable by Charalambos for the quarter ended 30 September 2015. Candidates' performance was satisfactory on this question. Many candidates were able to confidently calculate both output and input tax in a timely way, and some scored full marks.

Where candidates did not score enough marks to pass, this tended to be because some candidates wrongly applied the reverse charge on the EU dispatches to an Italian VAT registered business, or because they wrongly applied the input VAT recoverability rules.

Part (b) for 3 marks required candidates to briefly advise Charalambos of the VAT implications of his ceasing to trade. Candidates' performance was unsatisfactory on this question. Many candidates were able to correctly identify the value added tax (VAT) treatment of the cessation of taxable supplies. However many candidates wrongly referred to voluntary deregistration rules,

rather than answering the question actually set. This was not what the question required and hence did not score any marks.

In addition some candidates wrongly mentioned the value added tax (VAT) treatment of the intra-community supplies of goods made from Cyprus to a taxable person registered in another EU member state. Again, this was not what the question required and hence did not score any marks.

Question Two

This 10-mark question covered the topic of capital gains tax calculation. Performance on this question was satisfactory.

Part (a) for 5 marks required candidates to calculate Rodoula's chargeable gain arising from the exchange of the plot in Nicosia with the villa in Peyia, claiming all available exemptions and reliefs. The majority of candidates identified and claimed both the roll-over relief and the general lifetime exemption. This part of the question was answered well by the majority of candidates.

Part (b) for 5 marks required candidates to calculate Rodoula's chargeable gain arising from the exchange of the agricultural land in Nicosia with the villa in Peyia, claiming all available exemptions and reliefs. This part of the question was also answered well by the majority of candidates. However, some candidates failed to identify the roll-over relief.

Question Three

This 10-mark question covered the topics of trade goodwill and income tax.

Part (a) for 3 marks required candidates to state the circumstances in which trading goodwill will be subject to either income tax or corporation tax. This part of the question was not answered well by the majority of candidates.

Many candidates failed to score marks because they made the following mistakes:

- Providing an explanation of how the trading goodwill shall be taxable. This was not what the question required and hence did not score any marks. Candidates should use their allotted reading time to read the question requirements carefully prior to writing anything.
- Failing to recognise the circumstances in which trading goodwill will be subject to either income tax or corporation tax.

Part (b) for 7 marks required candidates to calculate Pericles's total taxable income for the year 2015. The scenario contained various sources of income and candidates scored well on this part of the question, with some obtaining full marks.

Where candidates did not tend to score well this was because they failed to distinguish between trading and rental income. In addition some candidates estimated the income tax liability, this was not required and so would not score any marks.

Also some candidates mentioned that the personal trading income and the trading goodwill of Pericles shall be taxable under corporation tax.

Question Four

This 10-mark question covered the topic of special defence contribution. The question required candidates to calculate Farmers Ltd's deemed dividend distribution for the year 2015 and the related special defence contribution liability. Performance on this question was unsatisfactory.

Many candidates were unable to distinguish between the tax adjustments on accounting profits for income tax purposes and the tax adjustments on accounting profits for deemed dividend purposes. Candidates shall be aware that as from the year 2003, companies are deemed to have distributed in the form of dividends to their resident shareholders 70% of their after tax accounting profit as at the end of two years from the end of the year to which the profits relate, and account for special defence contribution to the Tax Department at the appropriate rate.

Many candidates failed to score marks because they made the following mistakes:

- Calculating the tax adjusted profit for corporation tax purposes, despite the fact that the tax adjusted profit was given.
- Calculating balancing adjustments in regards with the business assets disposed and including them in the deemed dividend distribution estimate.
- Calculating capital gains tax liabilities instead of special defence contribution liability on deemed dividends. Candidates again must answer the question.

Question Five

This 15-mark question was based on a self-employed individual, Christoforos, who commenced in business on 1 October 2014. This question tested the areas of income tax adjustments on accounting profits and capital allowances.

Part (a) for 3 marks required candidates to state the requirements for capital allowances to be granted in respect of an asset.

This part of the question was answered well by many candidates. However, some candidates did not always adequately state the requirements for granting capital allowances. In addition a minority of candidates misunderstood the requirement and instead of stating the requirements for granting capital allowances, they explained the procedure to be followed in order to estimate the wear and tear for each type of fixed asset.

Part (b) for 3 marks required candidates to state the effect (if any) on the wear and tear claim of the length of ownership of an asset and/or the length of the period of account. Performance on this question was mixed.

Many candidates provided an answer only for the first part of the requirement and they did not discuss the effect of the period of account.

For those candidates who understood what was required their explanations were often adequate, and some candidates scored full marks.

Part (c) for 9 marks required candidates to calculate the amount of trading profits to be assessed on Christoforos for each of the tax years 2014 and 2015. Performance on this question was satisfactory. It was pleasing that many candidates set their answer in a columnar format and again this seemed to help them to produce clear and concise answers. Many candidates performed

adequately on this part of the question, as they calculated correctly the capital allowances for both years. Where candidates did not tend to score well this was because of estimating full wear and tear claims for the three months accounting period to 31 December 2014.

Question Six

This 15-mark question was based on a Cyprus resident manufacturing company Innovative Business Solutions Ltd. The question tested the areas of corporation tax liability and group loss relief.

Part (a) for 7 marks required candidates to calculate Innovative Business Solutions Ltd's taxable profit and corporation tax liability for the year 2015. Performance on this question was satisfactory.

Very good answers were prepared by many candidates, demonstrating sound knowledge of the various adjustments to be performed to calculate the taxable income of Innovative Business Solutions Ltd. Many candidates were able to identify and make all necessary tax adjustments. Where candidates did not tend to score well this was because of lack of technical knowledge.

Part (bi) for 4 marks required candidates to briefly explain which companies will be regarded as members of Onesilos Limited's tax group for the year 2015. Performance on this question was satisfactory, and many candidates scored full marks.

Part (bii) for 4 marks required candidates to calculate Onesilos Limited's taxable profit and the corporation tax payable for the year 2015, taking into account any loss reliefs available. Performance on this question was mixed.

Many candidates were unable to claim correctly group loss relief and then estimate the corporation tax liability. In addition some candidates deducted the temporary tax paid from the taxable income even though it is a disallowed expense.