
Answers

Tutorial note: These model answers are considerably longer and more detailed than would be expected from any candidate in the examination. They should be used as a guide to the form, style and technical standard (but not length) of answer that candidates should aim to achieve. However, these answers may not include all valid points mentioned by a candidate and credit will be given to candidates making such points.

1 Kentavros Trust

MEMORANDUM

To: AN tax partner
From: AN tax manager
Date: 2 June 2008
Subject: Kentavros Trust

In relation to the above tax case, I hereby set out below my responses to the questions raised by the Trust's London tax consultants.

(a) Tax residence

The tax residence of a company is determined in Cyprus by the 'management and control' test. Although there is no definition of this term in the Cyprus tax law, the management and control of a company is determined if all of the following three criteria are met:

- the majority of the board of directors are Cyprus tax residents;
- directors' board meetings take place in Cyprus; and
- the management decisions of the company are taken in Cyprus.

(b) Basis of taxation: dividends and interest

Dividend income is assessable on the basis of entitlement of receipt, but specifically exempt from corporation tax. It will also be exempt from special defence contribution as the shareholdings in the Czech companies exceed 1% and the tax burden on the underlying profits is not considerably lower than at Cypriot tax rates (in fact it is higher).

Interest income whether treated as investment income or as trading income, will be assessable to corporation tax and special defence contribution on an accruals basis.

(c) Treatment of interest income

I believe it will be more beneficial to have two Cyprus companies in the structure, although using just one company may suffice in terms of how interest income will be treated by the Cyprus tax authorities. One company (the holding company) should hold the majority of the shares in the Czech companies and the other company (the finance company) should be the loan provider to the Czech companies. The finance company must hold at least 25% of the shares in the Czech companies, in order to take advantage of the provision for no taxes to be withheld at source on dividend and interest payments made by the Czech companies.

The main reason for having the two companies separately is to avoid any questions being raised by the Cyprus tax authorities as to how to treat the interest income received by the finance company, whose only activity will be obtaining and providing loan finance, as having only one company in the structure providing both equity and loan finance could raise questions as to whether the loan or part of it relates to the value of the acquired companies thus affecting the treatment of interest income. The treatment of interest receivable is important because if interest received is treated as trading income (in the hands of the finance company) it is subject to 10% corporation tax, after interest payable on the loans obtained is deducted as an expense. However, if the interest received is considered to be investment income, 50% of it will be exempt from corporation tax, thus creating a corporation tax loss after expenses, but it will also be subject to special defence contribution at 10%. This will create an unnecessary tax burden on the group because the dividend income (all received from the Czech companies) is also exempt from corporation tax leaving these tax losses unrelieved.

The effect of this is illustrated as follows. The loan obtained and granted is €30 million. Assuming 6% per annum interest receivable on the loan granted and 5% interest payable on the loan obtained, will give interest receivable of €1.8 million and interest payable of €1.5 million.

If this operation is treated as a trading activity, a trading profit of €300,000 will be taxed at 10% giving a corporation tax liability of €30,000 per annum (ignoring any other tax allowable expenses) as from the third year onwards. For the first two years withholding tax of 10% will be deducted at source and paid to the Czech tax authorities, thus covering any corporation tax liabilities, as the Czech withholding tax will be deductible as a credit from the Cyprus tax liabilities.

If on the other hand the interest receivable is treated as investment income, there will be a corporation tax loss of €600,000 (50% x 1.8 million – 1.5 million) per annum, but it will attract special defence contribution of €180,000 per annum (10% of 1.8 million), creating an additional tax burden of €150,000 (180,000 – 30,000) per annum as from the third year onwards. Withholding tax of 10% will be deducted at source and paid to the Czech tax authorities in the first two years, thus covering the special defence contribution liability (also imposed at 10%), as the Czech withholding tax will be deducted as a credit from the Cyprus tax liabilities.

Note that the above example is based on the assumption of no loan instalments being made which is stated to be the case for the first 18 months.

(d) Tax deductibility of interest on €30 million

Loan interest charged by the shareholder of a company on granting a loan to his/her company cannot be treated as a tax deductible expense for the borrower company, unless the loan is used by the company to finance its trading activities and the interest charged to the company is charged at an arm's length interest rate. Furthermore, interest on that part of the loan relating to a share capital subscription will not be allowed as it is considered as expenditure of a capital nature.

It is, therefore, imperative that the Cyprus finance company, which will in turn provide loans to its Czech subsidiaries/associated companies, is seen as using the loan to finance the operations of its Czech subsidiaries and is itself charged interest at the market rate (arm's length) by the lender – the Kentavros Trust.

It must be noted that in this situation, the Cyprus company will have to charge a reasonable margin on the loan itself which it will grant to the Czech companies under the arm's length principle.

(e) 'Transfer' of €5 million loan

JerseyCo should grant a loan to the Cyprus finance company either on the same terms or at a reasonable margin over the interest charged on the original bank loan, applying the arm's length principle which will ensure tax deductibility in Cyprus. This practice will not necessitate the early repayment and re-issue of the bank loan to the Cyprus company, a practice which may also entail further costs in terms of loan arrangement fees charged by the bank.

(f) Taxation of payments to the Kentavros Trust

Interest paid to non-Cyprus residents is not subject to any withholding tax in Cyprus. Dividends paid to non-Cyprus tax residents is also exempt from withholding tax. However, if any of the beneficiaries of the Kentavros Trust is or are Cyprus tax residents, special defence contribution at 15% will have to be withheld at source by the Cyprus company; and as far as interest is concerned, such Cyprus resident beneficiaries will have – through a Cyprus resident tax representative of the trustee (if the trustee is non-Cyprus resident) or the trustee (if the trustee is Cyprus resident) – to account for special defence contribution at 10% on a self assessment basis, and withhold this from the amount paid to the beneficiary and remit it to the collector of taxes in Cyprus.

(g) Stamp duty position

The transfer of shares will be subject to stamp duty only if the contract for the acquisition of the shares of the Czech companies is signed in Cyprus. If the contract is signed outside Cyprus no stamp duty is due, as the property transferred is situated outside of Cyprus.

In the case of the loan arrangement, if the contract is signed outside Cyprus between a Cyprus company and a foreign entity or person and the monies are never remitted in or through Cyprus, the transaction is not within the scope of Cyprus stamp duty. If however, the contract is signed in Cyprus, or the monies are remitted to or through Cyprus, then stamp duty will be due.

However, if in the contract it is stipulated that the Cyprus courts have jurisdiction over the contract, then stamp duty will become due in Cyprus irrespective of where the contracts will be signed or where the property is situated or whether the monies have been remitted to or through Cyprus.

In both cases, therefore, it should be possible in the current situation to avoid Cyprus stamp duty.

(h) Tax position on ultimate sale

The sale of shares in the Czech companies will most certainly be treated as a capital gain, mainly due to the length of ownership of the shares and the fact that these shares were held as an investment which had generated income. As the Czech companies will not get involved with immovable property situated in Cyprus, such gains will be exempt from capital gains tax in Cyprus.

Even if however the sale is treated as a trading transaction, which is unlikely to happen, such gains are specifically exempt from income/corporation tax.

Mr Andreas
Nicosia
Cyprus

2 June 2008

Dear Andreas

Re: Your proposed business venture

Further to my meeting with yourself and your prospective partners, Alkis and Jack, set out below is my advice on the various matters discussed.

(a) Introducer's fees

If a partnership is formed, Jack's introducer's fee of 10%, although an accounting expense, will not be treated as a tax deductible expense as it is a method of appropriation of profits. It will form part of Jack's share of taxable partnership profits.

If a limited company is formed, Jack's introducer's fee of 10% will be a tax deductible expense, as it is an expense incurred wholly and exclusively for the purposes of earning the profits. This fee will not be taxable on Jack in Cyprus, as he is not resident in Cyprus.

(b) Office rentals

If a partnership is formed, rent charged although an accounting expense, will not be treated as a tax deductible expense as it is a method of appropriation of profits. It will form part of Jack's share of taxable partnership profits. Jack will not be deemed as having rental income. He will, however, be entitled to capital allowances at a rate of 3% per annum on the cost of construction, which is $\frac{2}{3}$ of the acquisition cost, as his immovable property is an asset used in the business.

If a limited company is formed, rent charged will be a tax deductible expense as it is an expense incurred wholly and exclusively for the purposes of earning the profits, provided a rental agreement is signed and properly stamp dutied. As far as Jack is concerned, he will be taxed as receiving rental income at the gross amount of rent less 20%, less capital allowances calculated as above. As Jack is a non-Cyprus tax resident, his rental income will be exempt from special defence contribution.

(c) Interest on contributed capital

If a partnership is formed, interest on partners' capital, although an accounting expense, will not be treated as a tax deductible expense as it is a method of appropriation of profits. It will form part of each of the partners' taxable partnership profits. If a limited company is formed, the tax treatment will be the same as for a partnership except that your own interest will be tax deductible, as you will have taken a loan from a third party to invest in a private company, provided that the interest charged by this third party is at least 6% per annum.

Taking out a business overdraft would be preferable, as overdraft interest will be a tax deductible expense both in the case of a partnership and in the case of a limited company. The difference in taxable profits will be €3,300 (60,000 at 7.5% less 20,000 at 6%). It therefore makes sense to obtain a business bank overdraft.

(d) Tax efficient positions of the three partners

If a partnership is formed, you will have an annual taxable income of €59,833, taxed at 0% to 30% as your other income is dividends which are specifically exempt from income tax. If a limited company is formed, as a returning expatriate, you will have taxable salaried income of €34,000 taxed at 0% to 25% in year 1, €27,200 (34,000 less 20% exemption) taxed at 0% to 20% in years 2 to 4 and €34,000 from year 5 onwards. The rest of your share of corporate profits of €25,833 ($77,500 \times \frac{1}{3}$), will be taxed at an effective rate of 19.45% (10% corporation tax + 15% x 90% x 70% special defence contribution). This means that you will be better off with a limited company as your share of profits above your salary will be taxed at 19.45% instead of mostly at 30%.

If a partnership is formed, Alkis will have annual taxable income of €37,833, taxed at 25% to 30% as he also has other taxable income from employment of €30,000 (dividends are specifically exempt from income tax). If a limited company is formed, Alkis will have taxable salaried income of €12,000 taxed at 25% to 30%. The rest of his share of corporate profits of €25,833 ($77,500 \times \frac{1}{3}$) will also be taxed at an effective rate of 19.45% (as above). This means that Alkis is also better off with a limited company as his share of profits above his salary will be taxed at 19.45% instead of 30%.

If a partnership is formed, Jack's partnership annual taxable income will be €42,834 taxed at 0% to 30%. As Jack is a non-Cyprus tax resident the only income taxable in Cyprus will be income arising in Cyprus through a permanent establishment (in this case the partnership). If a limited company is used, Jack's taxable income in Cyprus will be rent of €4,600 ($12,000 \times 80\%$, less 5,000 capital allowances), taxed at 0% and his share of corporate profits of €25,833 ($77,500 \times \frac{1}{3}$) taxed at 10% on the company. His introducer's fees will not be taxed in Cyprus as this is not income arising from a permanent establishment he will use in Cyprus, and his actual or deemed dividend will be exempt from special defence contribution, as he is a non-Cyprus resident. It is clear therefore that from the Cyprus tax perspective Jack should be clearly in favour of using a limited company.

However, it must be noted that Jack's annual partnership income of €42,834 as compared with income arising from the company, i.e. rental income of €12,000 (before any allowances granted by USA tax law), introducer's fee of €10,000 and dividend of €11,625 ($77,500 \times 90\% \times \frac{1}{3} \times 50\%$), a total of €33,625 (before any allowances granted by USA tax law for rental income) will probably be taxable in the USA as he is resident there. Even so, he is better off with a limited company in Cyprus, as the total taxable income, and therefore Jack's tax liability, is lower than if a partnership is used. Proper professional advice must however be sought from the USA on this point.

(e) Sale of the business

In the case of a partnership, the sale of trading goodwill at a profit (in this case the profit will equal disposal value as cost is nil), will result in each of the partners being subject to income tax at the normal rates of 0% to 30% on their respective profit share.

In the case of a limited company transferring its business as a going concern i.e. selling its business, the profit on the sale of trading goodwill will be taxable income of the company subject to 10% corporation tax. In addition, after tax profits will be subject to special defence contribution at 15% on an actual or deemed distribution. As above, Jack will be exempt from special defence contribution as he is a non-Cyprus resident.

In the case of a transfer of shares in the company instead of a transfer by the company of its business, any trading goodwill included in the value of the company's shares will escape taxation as gains on the sale of shares are specifically exempt from income tax and in this case, outside the scope of capital gains tax, as the company will presumably not hold any immovable property.

(f) Value added tax (VAT)

No VAT will be charged as the transfer of a business as a going concern from one taxable person to another, is not a transaction that falls within the scope of value added tax.

I am at your disposal, should you require any further information.

Yours sincerely,

A N Accountant

Workings

1. If a partnership is formed:

Years 1–3 (per annum)

	Andreas €	Alkis €	Jack €	Total €
Salaries	34,000	12,000	0	46,000
Introducer's fees	0	0	10,000	10,000
Rent	0	0	12,000	12,000
Bank overdraft interest (60,000 at 7.5%)				4,500
Residue of profits	<u>25,833</u>	<u>25,833</u>	<u>25,834</u>	<u>77,500</u>
	59,833	37,833	47,834	<u>150,000</u>
Less: Capital allowances (250,000 at $3\% \times \frac{2}{3}$)	<u>0</u>	<u>0</u>	<u>5,000</u>	
Total taxable	<u>59,833</u>	<u>37,833</u>	<u>42,834</u>	

2. If a limited company is used.

Years 1–3 (per annum)	€
Profit	150,000
Salaries	(46,000)
Introducer's fees	(10,000)
Rent	(12,000)
Bank overdraft interest	<u>(4,500)</u>
Taxable on the company	<u>77,500</u>
Corporation tax at 10%	<u>7,750</u>
Deemed/actual distribution for special defence contribution purposes 77,500 less 7,750 at $70\% \times \frac{1}{3}$ per partner	<u>16,275</u>

3 Scandisure AB

- (a) The income of insurance companies engaging in life assurance and general insurance is calculated under a special mode of taxation, which includes a deduction of part of head office expenses where the head office is situated outside Cyprus as in this case. The deduction is capped at 3% of premiums arising in Cyprus net of re-insurances given, to companies engaging in the general insurance sector, whereas for companies engaging in life assurance, this deduction is capped at 2% of premiums arising in Cyprus net of re-insurances given. Any loss arising in a tax year not relieved within the same tax year may be carried forward and relieved against the first available profits of future years without any restriction. Interest receivable is treated as trading income and is subject to corporation tax but it is exempt from special defence contribution.

Profits are taxed at the normal rate of 10% corporation tax. However, in the case of life assurance activities, there is a minimum corporation tax liability of 1.5% of gross premiums.

(b) Taxable income and tax liabilities for the year 2008

	General insurance	Life assurance
	€'000	€'000
Gross premiums receivable	250	900
Interest receivable	50	0
Commissions receivable	10	0
Other income	5	0
Net investment income	0	120
Total income	315	1,020
Less: Expenses		
Deduction for head office expenses		
–3% x (250 – 117)	4	
–2% x (900 – 450)		9
Return of insurance premiums on cancellation	30	0
Premiums for re-insurance	117	450
Reserves for unexpired risks at 31 December 2008	50	120
Less: Reserves for unexpired risks at 1 January 2008	(0)	(0)
Net claims	60	150
Payments for policy surrenders	0	80
Branch overheads (excluding depreciation and social cohesion fund contributions)	50	100
Capital allowances	10	10
Total expenses	321	919
Net (loss)/taxable profits	(6)	101
Net taxable income (101 – 6)		95
Corporation tax at 10%	0	9.5
1.5% of gross premiums (1.5% x 900)		13.5
Corporation tax payable	0	13.5

No income is subject to special defence contribution.

- (c) All companies in Cyprus are required to submit a temporary assessment of tax on 1 August of the year of assessment, 1 August 2008 in this case; and pay tax provisionally in three equal instalments on 1 August, 30 September and 31 December.

If the actual tax liability exceeds the provisional tax paid, the difference is payable by self-assessment by 1 August, following the year of assessment, 1 August 2009 in this case.

The tax return for a year of assessment must be submitted by 31 December following the year of assessment.

- (d) There is no obligation nor right to register for value added tax (VAT) as insurance services are specifically exempt from VAT (Schedule 7) and persons providing only exempt supplies cannot register for VAT.

4 Martine

- (a) Where a Cyprus tax resident company is the recipient of film rental income, its income from film rentals derived from other European Union (EU) countries will be exempt from withholding taxes in those countries if the Cyprus company (beneficial owner of the income) is an associated company of the paying companies (or permanent establishments of those companies) which are resident in the other EU member states; or if the Cyprus company has permanent establishments in the other EU member states where such income represents a deductible expense under the provisions of the tax laws of those EU member states for such permanent establishments.

A company (the first company) is deemed to be an associated company with another company (the second company) if either:

- the first company has a direct minimum holding of 25% of the share capital of the second company; or
- the second company has a direct minimum holding of 25% of the share capital of the first company; or
- a third company has a direct minimum holding of 25% of the share capital of both the first and the second companies.

- (b)** Since Martine will be carrying out duties on behalf of the Cyprus company overseas, she can receive remuneration for these duties, thereby reducing the taxable profits of the Cyprus company while avoiding paying personal taxes in the UK in respect of all or part of this salary, provided she does not remit it to the UK.

It must, however, be noted that Martine's remuneration from the Cyprus company must be determined at arm's length, otherwise, the commissioner will deem this practice as an attempt to avoid the payment of taxes by the company. Furthermore, the employment contract must be properly executed and stamp dutied.

- (c) (i)** If a Cyprus tax resident company is used to acquire the house in London and Martine occupies the house rent free, then there is an assessable benefit in kind on Martine on the basis of the cost to the employer. However, as Martine is a non-Cyprus tax resident, the Cyprus tax authorities will not be able to tax her. It must be noted, however, that it is possible that the UK tax authorities may be in a position to assess this benefit in kind on Martine if the Cyprus company has activities in the UK, and she is deemed to be an employee in the UK. Proper professional advice must be obtained from Martine's London accountant on this issue.

As far as the company (who is the legal owner of the house) is concerned, it will not be able to claim any expenses in respect of the property, if it has no other income or activity. However, if Martine uses the same company for film production and ownership of the house, part of the expenses relating to that part of the property used for business purposes may be claimable against the company's profits. Alternatively, if two companies are used, the property owner company may charge a reasonable amount as office rent (applying the arm's length principle) to the film producing company, in this way making it possible to recover that part of the expense relating to ownership of the property.

If Martine pays rent to the owner company, then provided that she pays a market rent, no benefit in kind will be assessable on Martine.

The company on the other hand will be receiving taxable rental income determined per its audited accounts and assessed to Cyprus corporation tax. In addition such rental income less 25% will be assessable to special defence contribution at 3%.

It must also be noted that as the income arises from immovable property situated in the UK, the Cyprus company may have to account for corporation tax in the UK. In this case, any tax paid in the UK will be deductible as a credit from the Cyprus tax liabilities of the company.

- (ii)** On the sale of the property, any capital gain arising is exempt from Cyprus capital gains tax as the immovable property is situated outside of Cyprus (it will also be exempt in the UK, as stated in the question). There is a possibility that the commissioner in Cyprus will deem this transaction as trading (isolated transactions rules), it is however unlikely that such practice will succeed based on the length of ownership and the fact that the property was held as an investment, generating taxable income for a number of years. In addition, on distribution of the gain to Martine, no special defence contribution is payable, as Martine is not a resident of Cyprus. It will also not be taxable in the UK unless the dividends are remitted there. Separate advice should, however, be obtained with regard to the US tax position, if Martine intends to return to the USA before she receives the dividend or to receive the dividend from this company in a year of assessment in which she is tax resident in the USA or in any country other than the UK.

5 Exxonmore Limited

- (a)** The expenses that are tax deductible are as follows:

- The gross salaries of the five employees listed in the question.
- The employer's contributions to the social insurance and other funds that the company is obliged by law to contribute to, except for contributions to the social cohesion fund.
- The air tickets, accommodation and meals overseas in respect of Elli and Nicos.
- The cost of accommodation for Boris.
- The business part of the air tickets, accommodation and meals of Mr Exxon.

- (b)** Mr Exxon is not a Cyprus resident individual and his salary mostly relates to duties performed overseas and will, therefore, mostly be exempt from income tax in Cyprus. He will be assessed in Cyprus only on the part of the salary relating to his attendance at the board and shareholders' meetings.

Nicos is a tax resident of Cyprus and his salary is assessable in Cyprus. However, as he spends more than 90 days per annum at a permanent establishment of his Cyprus resident employer overseas, the part of his salary that relates to the duties performed overseas will be exempt from income tax in Cyprus. Nicos will not be taxed on the benefit of the air tickets, accommodation and a reasonable amount for meals provided overseas as these expenses are incurred wholly and exclusively for the purposes of exercising his duties, but he will be assessed on the car benefit on the basis of the percentage of private use of the car and the cost to the employer.

Elli is also a tax resident of Cyprus and her salary is assessable in Cyprus. Although she spends more than 90 days per annum overseas, as these duties are not provided to a permanent establishment of her Cyprus resident employer overseas, the whole of her salary will be subject to income tax in Cyprus. Elli will not be taxed on the benefit of the air tickets, accommodation and a reasonable amount for meals provided overseas, as these expenses are incurred wholly and exclusively for the purposes of exercising her duties. She will however be taxed on the amount of her daughter's tuition fees paid by the company, as although these do not relate to her personally, they relate to one of her dependent relatives.

Boris and Alice are also both tax resident in Cyprus and will be taxed on their salary (as well as any other worldwide income) in Cyprus. In addition, Boris will be taxed on the benefits of accommodation and meals on the basis of the cost to the employer.

- (c) Mr Exxon is not ordinarily resident in Cyprus, as he spends a very limited time in Cyprus and will, therefore, be liable to neither social insurance nor social cohesion fund contributions. The same principle applies to the employer.

Nicos and Elli are ordinarily resident in Cyprus and are liable to both social insurance and social cohesion fund contributions on the whole of their salary (despite the fact that part of Nicos's salary is exempt from income tax due to application of the 90 day rule) as well as on the value of their benefits in kind. The same principle applies to the employer.

Alice, although not ordinarily resident in Cyprus, is a European Union citizen and is liable to both social insurance and social cohesion fund contributions on her salary. The same principle applies to the employer.

Boris is not ordinarily resident in Cyprus; he is a citizen of a third country (non-EU) and therefore exempt from both social insurance and social cohesion fund contributions. The same principle applies to the employer.

	<i>Marks</i>
1 Kentavros Trust	
(a) Refer to the 'management and control' test	0·5
Define 'management and control' (3 x 1/2)	<u>1·5</u>
	<u>2·0</u>
(b) Dividend income on an entitlement to receive basis	1·0
But exempt both corporation tax and special defence contribution, with reasons	2·0
Interest income on an accruals basis, both corporation tax and special defence contribution	<u>1·0</u>
	<u>4·0</u>
(c) More beneficial to use two Cyprus companies	1·0
Explanation of two company structure to adopt	1·0
The finance company must hold at least 25%	1·0
Identify treatment of interest receivable as key issue	1·0
Explain alternative treatments (2 x 1)	2·0
Identify additional tax burden/unrelieved loss	0·5
Illustration:	
Trading income years 1 and 2	0·5
Withholding tax effect year 3 onwards	1·0
Investment income years 1 and 2	0·5
Withholding tax effect year 3 onwards	<u>0·5</u>
	<u>9·0</u>
(d) Conditions necessary for deductibility in the case of intra group loans (2 x 1)	2·0
Interest on portion of loan to subscribe for share capital not deductible, with reason	1·5
Application in this case:	
Kentavros Trust/Cyprus finance company	0·5
Cyprus finance company/Czech company	<u>1·0</u>
	<u>5·0</u>
(e) Loan by JerseyCo on same or different terms as original bank loan	<u>1·0</u>
(f) Position of non-residents (2 x 1/2)	1·0
Identify specific issue re resident beneficiaries of the Kentavros Trust	1·0
Explain effect:	
– re dividends	0·5
– re interest	<u>1·5</u>
	<u>4·0</u>
(g) Share transfer subject to stamp duty only if contract signed in Cyprus, with reasons	1·5
Loan arrangement not subject to stamp duty if signed outside Cyprus, with reasons	2·0
Exception if Cyprus courts stipulated as having jurisdiction	1·0
Conclude in this case	<u>0·5</u>
	<u>5·0</u>
(h) Sale treated as capital gain, with reasons	1·5
Exempt from capital gains tax, with reason	1·0
If transaction treated as trading, then specifically exempt income/corporation tax.	<u>0·5</u>
	<u>3·0</u>
Presentation and format of the memorandum	1·0
Effectiveness of communication	<u>1·0</u>
	<u>2·0</u>
Total	<u>35</u>

	Marks
2 Andreas, Alkis and Jack	
(a) Partnership: not tax deductible expense, with reason	0·5
Part of Jack's share of taxable partnership profits	0·5
Limited company: tax deductible expense, with reason	0·5
Not taxable on Jack in Cyprus, with reason	0·5
	<hr/> 2·0
(b) Partnership: not a tax deductible expense, with reason	0·5
Part of Jack's share of taxable partnership profits	0·5
Jack will not be deemed as having rental income	0·5
Entitled to capital allowances, with reason	0·5
Basis of capital allowance claim	1·0
Limited company: tax deductible expense, with reasons	1·0
Explanation of Jack's income tax position	1·0
Exempt from special defence contribution, with reason	1·0
	<hr/> 6·0
(c) Partnership: as for rent (above)	0·5
Limited company: as for a partnership	0·5
Andreas's interest tax deductible, with reasons	1·5
Business overdraft preferable, with reasons	1·0
Calculation of difference in taxable profits, €3,300	0·5
	<hr/> 4·0
(d) Workings/computations:	
Partnership:	
Residue of profits	1·0
Allocation of income to partners	1·0
Capital allowance (Jack)	0·5
Limited company:	
Taxable income/tax payable	0·5
Deemed/actual distribution	0·5
Explanations with reasons:	
Andreas:	
Partnership	1·0
Limited company: salary	2·0
share of profits	1·0
Conclusion	0·5
Alkis:	
Partnership	0·5
Limited company: salary	0·5
share of profits	0·5
Conclusion	0·5
Jack:	
Partnership	1·0
Limited company: rent	1·0
share of profits	0·5
introducer's fees	1·0
deemed dividend	0·5
Conclusion	0·5
Consideration of Jack's US tax position and need for advice	1·5
	<hr/> 16·0

	Marks
(e) Partnership: taxable on partners according to profit share	1·0
Limited company transfer as a going concern:	
Corporation tax	1·0
Distribution: general	0·5
Jack	0·5
Transfer of shares in company:	
Income tax	0·5
Capital gains tax	0·5
	<u>4·0</u>
(f) No VAT, with reason	<u>1·0</u>
Presentation and format of the letter	1·0
Effectiveness of communication	1·0
	<u>2·0</u>
Total	<u>35</u>

3 Scandisure AB

(a) Special mode of taxation,	0·5
Deduction for head office expenses where situated outside Cyprus	0·5
Limits to deduction (2 x 1/2)	1·0
Treatment of losses	0·5
Treatment of interest receivable	1·0
Minimum corporation tax payable for life assurance business	0·5
	<u>4·0</u>
(b) Gross premiums receivable	0·5
Interest/commissions receivable	0·5
Other income/net investment income	0·5
Deduction of head office expenses (2 x 1/2)	1·0
Return of insurance premiums/premiums for re-insurance	0·5
Reserves for unexpired risks at 31 December 2008	0·5
Reserves for unexpired risks at 1 January 2008	0·5
Net claims/payments for policy surrenders	0·5
Branch overheads/capital allowances	0·5
Net taxable income/loss offset	0·5
Tax payable – minimum basis	1·0
No income subject to special defence contribution	0·5
	<u>7·0</u>
(c) Requirement to submit temporary assessment, including due date	0·5
Provisional tax payable in three equal instalments, including date	0·5
Balance of actual tax liability payable by self-assessment, including due date	0·5
Tax return due date	0·5
	<u>2·0</u>
(d) Cannot register for VAT	1·0
Insurance services exempt supply	1·0
	<u>2·0</u>
Total	<u>15</u>

	Marks
4 Martine	
(a) Necessary conditions (2 x 1)	2·0
Definition of 'associate'	1·0
	<u>3·0</u>
(b) Identify payment of remuneration as best strategy	0·5
Explain Cyprus tax consequences	0·5
Explain UK tax consequences	0·5
Identify and explain tax avoidance risk	1·0
Employment contract must be properly executed and stamped	0·5
	<u>3·0</u>
(c) (i) Martine occupies the house rent free:	
Assessable benefit in kind	0·5
In practice Cyprus tax authorities will not be able to tax her	0·5
Possible UK tax liability, with reason	0·5
No claim for expenses if no other income or activity	0·5
Availability of claim for part expenses re business use	0·5
Alternative methods of achieving deduction (2 x 1/2)	1·0
Martine pays rent to the owner company:	
Market rent, no benefit in kind	0·5
Rental income taxable on company (2 x 1/2)	1·0
Possible UK tax liability	0·5
Double tax relief available	0·5
	<u>6·0</u>
(ii) Capital gain exempt, with reason	0·5
Possibility transaction deemed as trading	0·5
Unlikely to succeed, with reasons	1·0
No special defence contribution on distribution, with reason	0·5
Refer to non-Cyprus tax position and need for advice	0·5
	<u>3·0</u>
Total	<u>15</u>

5 Exxonmore Limited		Marks
(a)	Gross salaries of all five employees	0.5
	Employer's contributions except social cohesion fund.	1.0
	Air tickets, accommodation and meals overseas re Elli and Nicos	0.5
	Cost of accommodation for Boris.	0.5
	Business part of the air tickets, accommodation and meals for Mr Exxon.	0.5
		<u>3.0</u>
(b)	Mr Exxon:	
	Not tax resident, with reasons	1.0
	Assessed only on part of salary relating to attendance at board and shareholders' meetings	0.5
	Nicos, Elli, Alice and Boris are all tax resident in and assessable to tax in Cyprus	1.0
	Nicos:	
	Exempt on part of salary that relates to duties performed overseas, with reason	1.0
	Not taxed on benefit of air tickets, accommodation and a reasonable amount for meals provided overseas	0.5
	Assessed on car benefit	0.5
	Elli:	
	Whole of salary subject to income tax in Cyprus	0.5
	Not taxed on benefit of air tickets, accommodation and a reasonable amount for meals provided overseas	0.5
	Assessed on daughter's tuition fees	1.0
	Boris:	
	Taxed on benefits of accommodation and meals	0.5
		<u>7.0</u>
(c)	Position with reasons:	
	Mr Exxon	1.0
	Nicos and Elli	1.5
	Alice	1.0
	Boris	1.0
	Same principle applies to employer in each case	0.5
		<u>5.0</u>
Total		<u>15</u>