Answers

1

AN Accountant
Nicosia

1 June 2009

Mr Nemeas
Nemeas (Cyprus) Limited
Nicosia

Dear Mr Nemeas

Re: Overseas operations

With reference to our recent meeting in Nicosia, I set out below my response to the issues raised during the meeting.

(a) Taxes on income, capital gains and special defence contribution (SDC)

(i) I noticed that trading in Middle East countries is not carried out through a permanent establishment overseas. This means that profits from operations in these countries is taxed in Cyprus although at the same time no corporation tax is assessable in these countries. I would therefore suggest that a foreign branch or branches through which operations will be made, is set up in these countries. The effect of this, is that no corporation tax will be due in these countries on profits attributable to the branch(es), and such profits will also be exempt from corporation tax in Cyprus, as profits from foreign permanent establishments are specifically exempt from Cyprus corporation tax. Note, however, that the SDC liability of your company will not be affected by this move, as distributions/deemed distributions are made/deemed from accounting profits.

(ii) Regarding your planned operations in other EU countries, the following considerations are relevant:

- With the current mode of operation i.e. the use of warehouses, all profits will be taxed in Cyprus. As Cyprus has the lowest corporation tax rate in the EU, I would say that this would be the preferable option, as analysed in the following paragraphs.
- If a branch is formed in each EU country, the profits attributable to each branch will be taxed in the relevant country according to the local applicable corporation tax rate. As Cyprus has the lowest tax rate in the EU, the total taxation burden of Nemeas (Cyprus) Limited will be higher than if all profits were taxed in Cyprus, which is the case for the existing mode of operation
- Overseas subsidiaries offer more tax planning opportunities than overseas branches as Nemeas (Cyprus) Limited will be able to charge its connected companies with a reasonable profit margin, thus decreasing the tax exposure of its subsidiaries in other EU countries. This will mean that the overall tax burden will be less than if branches are used. You should note however, that transfer pricing rules vary from country to country and that advice should be sought from practising professionals in those countries as to the correct price structure. Also, withholding tax issues on the payment of dividends from overseas subsidiaries (no such issues are present in the other modes of operations) may also affect cash flow, as EU countries apply the Parent-Subsidiary directive regarding dividend withholding taxes differently.

(iii) By reference to Romania only, note that the factory itself will most probably be regarded as a permanent establishment in that country. Profits attributable to this permanent establishment will therefore be taxed in Romania irrespective of whether a partnership or a limited company is registered in Cyprus or Romania. This position is also re-enforced by the fact that the business will be managed from Romania (the management and control test).

The only issue which remains to be addressed, therefore, is the choice of business formation. As personal income tax rates are higher than corporate tax rates, a limited company will be more tax efficient than a partnership. This applies to both yourself and your Romanian prospective partner. In addition, a partnership is considered as a transparent tax entity. This will mean that if a partnership is formed, the Interest – Royalty EC Directive will not apply in the case of withholding taxes on royalty payments from Romania to Cyprus and therefore withholding taxes will be levied in Romania, which will not be the case where an associated (25% holding) limited company is formed.

(iv) As things stand at the moment, you will be assessed to capital gains tax in Cyprus on the profit on disposal of your shares in Nemeas (Cyprus) Limited to the extent of the increase in value of the immovable property owned by the company which is situated in Cyprus only. Any other profit attributable to the increase in value of immovable property situated overseas or to any other factor is not taxable. Care should also be taken in structuring shareholdings in any foreign subsidiaries in that the shares must be registered in the name of Nemeas (Cyprus) Limited and not in your own name. This is important, as if shares in foreign companies registered in your name are disposed of at a gain, such gain will be taxable in the foreign countries, whereas if registered in the name of Nemeas (Cyprus) Limited, no gains will be taxable in these countries, as no disposal of shares in foreign companies will take place (only indirect disposal of any interest through the disposal of Nemeas (Cyprus) Ltd shares).

(v) You should however consider using a holding company, which will hold the shares of Nemeas (Cyprus) Ltd and any foreign subsidiaries; or hold the shares of Nemeas (Cyprus) Ltd and therefore, Nemeas (Cyprus) Ltd to hold the shares in all other foreign subsidiaries. The purpose of this is twofold. Firstly, when you retire, you will be disposing of the shares of the holding company, not the shares of Nemeas (Cyprus) Ltd. This means that the capital gains to be taxed in Cyprus

as referred to in paragraph (iv) above will not be taxable, as the holding company will not hold any immovable property directly. Note, however, that this restructuring will involve the transfer of ownership of your shares in Nemeas (Cyprus) Limited which may trigger a capital gains tax liability based on the value at the point of transfer. This liability may be avoided if an advance ruling is obtained on request of a free transfer of shares, which may be obtained if the director of the Inland Revenue is satisfied that this restructuring is not an attempt to avoid taxes. In this context, it would perhaps be preferable for the holding company to hold the shares in Nemeas (Cyprus) Ltd and all other foreign subsidiaries.

Secondly, dividend payments to yourself through the holding company and hence SDC payments at 15% on any dividend or deemed distribution, may be delayed for up to two years and they may also be reduced by 70% if this would be desirable. This is due to the fact that a payment of dividends between two Cypriot resident companies is exempt from SDC and as the deemed distribution rules refer to a distribution of 70% of the after corporation tax accounting profits, Nemeas (Cyprus) Ltd may thus pay 70% of its after corporation tax accounting profits as dividends to the holding company within two years of the relevant tax year and the holding company may pay 70% of the dividends received, to you, within two years from the end of the year during which dividends were received from Nemeas (Cyprus) Ltd.

(b) Value added tax (VAT)

Nemeas (Cyprus) Ltd is presumably already registered for VAT in Cyprus by reference to its local sales in Cyprus.

In relation to sales in other EU countries, provided you adopt my suggestion of maintaining the same mode of operation (paragraph (a)(ii)), as Nemeas (Cyprus) Ltd is responsible for the delivery of the goods in that country, the place of supply of goods is the country where the recipient of the goods belongs. As the recipients are consumers and therefore not registered for VAT in their countries, Nemeas (Cyprus) Ltd will be performing distance selling of goods. This means that your company may have an obligation to register in these countries by reference to their relevant registration thresholds and account for VAT in those countries through a VAT representative. These provisions do not apply to Romania, where a separate entity will operate. In this case, the separate entity may have an obligation to register for VAT in Romania and in other EU countries to which Romanian produced goods will be delivered.

I trust that I have covered all issues raised but should you have any further queries, please do not hesitate to contact me.

Yours faithfully

AN Accountant

2 MEMORANDUM

TO: TAX PARTNER
FROM: TAX SENIOR
RE: ANDREAS AND HIS BROTHER'S INHERITANCE
DATE: 30 APRIL 2009

I refer to the meeting I had with your friend Andreas, regarding the tax implications of his and his brother's plans relating to building land inherited from their late father. All tax issues are discussed below, as follows:

(a) Taxes on income, capital gains, immovable property and special defence contribution (SDC)

(i) Andreas and his brother will be subject to capital gains tax on the sale of the inherited property, based on the sales value of €5 million less the indexed January 1980 value of €350,000 (indexed from January 1980 until the month which precedes the month of actual disposal). The December 1996 value, which is the value at which their father inherited the property from his mother is irrelevant, as disposals on death are exempt from capital gains tax and therefore the deductible cost for capital gains tax will be the cost of acquisition by the initial bereaved relative or the 1 January 1980 value if acquisition took place earlier than this date.

(ii) If Andreas and his brother decide to exchange the property, then the exchange is a taxable event for capital gains tax purposes. In this case however, as the 1 January 1980 value of the property acquired is higher than the 1 January 1980 value of the property disposed of as part of the exchange, the whole of the capital gain arising will be rolled over. Such rolled over gain will be deducted from the cost of the property acquired for the purposes of any future disposal or part disposal.

(iii) Capital allowances at 3% per annum on qualifying expenditure will be deductible from rental income, provided the building is not more than 33 years old. Qualifying expenditure is determined as the cost of construction of the rented property (including the developer's profit margin). In addition a 20% discount of gross rental income (physical persons only) and bank loan interest to the extent that the loan relates to the part acquisition of the units rented out, will be deductible for income tax purposes. For SDC purposes the only deduction available is a general deduction of 25% of gross rental income.

(iv) Andreas and his brother are also considering as an option to sell some units from the building acquired by exchange for the inherited property, the rest of the units being kept for rental generation purposes. Although many factors normally need to be examined to determine if these transactions are of a trading or capital nature (e.g. the badges of trade, method of acquisition, use of the disposal proceeds), given the circumstances such transactions will be treated as of a capital nature as the property was acquired mainly through the exchange of an inherited property. The deductible cost will most

probably be determined on the basis of the January 1980 value of each unit plus a portion of the cash consideration of €300,000 (€5·3 million minus €5 million) as allocated to each unit sold.

(v) Regarding the option of developing the land into residential accommodation, the project to be financed partly by the exchange of part of the land, the exchange of the land will be treated as a disposal for capital gains tax purposes. The basis of determining the capital gain will be the market value (€5 million) of the land less the indexed January 1980 value (as in paragraph (i) above) as adjusted on a *pro rata* basis for the part of the land disposed of through the exchange. As far as the developer is concerned, the market value of the part of the land acquired through the exchange, will form part of the consideration to be received for rendering the services of developing the land.

(vi) Regarding the option of parcellation into 30 plots, the total allowable cost will be the cost of the land (€350,000 as adjusted for general inflation) plus parcellation expenses. In this case, parcellation expenses will equal the estimated market value of the ten plots exchanged with the developer. Each plot will be allocated a *pro-rata* total cost based on the estimated selling value of each plot divided by the sum of the estimated sales values of all plots and therefore each plot will be allocated an estimated taxable gain based on its actual sales value less its allocated total cost. The taxable gain will be assessed in the tax year(s) of sale or exchange of the plots in question. As regards the six remaining plots, their deductible cost for future purposes will be the *pro-rata* total cost allocated to each one of them based on their estimated selling prices on commencement of the project.

(vii) Immovable property tax (IPT) will be imposed on Andreas and his brother by reference to the 1 January 1980 value of all owned properties as at 1 January of each year. Regarding option (1), if the land is sold during 2009, no taxable base will exist and therefore no IPT will be due. Regarding the exchange for the building (option (2)), if the exchange takes place during 2009, the taxable base will be €380,000 (the 1 January 1980 value of the whole building), as reduced by the 1 January 1980 value of any units sold during 2009. If the two brothers decide to develop the land (option (3)), the taxable base will be the 1 January 1980 value of all units erected on the land, when the project will be completed. As the project will not be completed before the end of year 2009, the taxable gain will be the 1 January 1980 value of the land. Finally, in the case of parcellation into 30 plots (option (4)), the taxable base will be the 1 January 1980 value of the 20 plots (ten plots exchanged) on completion of the project, less the 1 January 1980 value of any plots sold. As again the project will not be completed before the end of year 2009, the taxable gain will also be the 1 January 1980 value of the land.

(b) Value added tax (VAT)

The supply (transfer of ownership or possession) of buildings or parts thereof together with the building site, will in this case be liable to VAT at the standard rate of 15%.

The question whether the sale of a building plot and the construction and sale of a building thereon constitutes a single transaction or two separate transactions (one for the sale of land (not taxable) and one for the building (subject to VAT) is a matter which is decided according to the facts of each case. In order to decide on the VAT treatment of a transaction one must always take into account the real intention of the parties, the nature, the content and the character of the transaction as well as any other facts of the particular case, including:

- the time of the contract;
- the manner of presenting the case before the Department of Land and Surveys or the Department of Inland Revenue;
- the reason for the existence of two separate agreements;
- whether the construction of the building was done by the seller of the building plots or by some other person; and
- in the case of cancellation of the agreement for the sale of the land and the making of a new agreement, the time of cancellation, i.e. if the cancellation was preceded by a transfer of the land and/or the purchaser had already fulfilled his/her obligations under the contract.

The VAT treatment of transactions involving the transfer of land by a land owner to a land developer and the satisfaction of the agreed price of the land being transferred by the transfer to the land owner of certain building units (whether flats, offices, shops etc) of equal value is as follows:

(1) Where the owner of the land transfers the whole of the plot of land to the developer and in exchange the land developer gives to the land owner a building structure (house or flat) erected on the land being the subject matter of the development, then for VAT purposes there are two distinct transactions.

   - a supply of the land by the land owner to the land developer which is an exempt supply; and
   - a supply of the house or flat which is subject to VAT at the standard rate.

(2) Where the land owner does not transfer the whole of the land, whether the erection of the house or flat given to the land owner consists of a supply of service by the land developer (which is taxable) or a supply of immovable property (which is exempt), depends on the terms of the agreement between the land owner and the land developer.

   The transaction in the above circumstances is treated as a supply of immovable property (and not a supply of services) if the following conditions are satisfied:

   - the land developer undertakes to supply to the land owner a specific property in accordance with plans and specifications which are the exclusive competence and responsibility of the land developer;
   - the appointment of architects, engineers and other consultants is the exclusive responsibility of the land developer
   - the supply of the immovable property subject matter of the transaction is erected as part of the total land development with an undivided share in the land and horizontal separation;

- the owner of the land maintains the ratio of the ownership in the land simply as a security for the materialisation of the agreement and in the end the balance of the rest of the share of ownership will be transferred; and
- the responsibility and the business risk for the development rests wholly on the land developer.

(3) Where any of the above mentioned conditions is not applicable and in particular where the land is not transferred in whole, the land developer is deemed to be supplying a construction service to the land owner. In this case there are two separate transactions.

- the part transfer of the land is an exempt transaction; and
- the construction of buildings on the land not transferred (remaining in the name of the land owner) is deemed to be a supply of taxable service by the land developer to the land owner.

3 (a) The types of investments which may be suitable for Loucas, are as follows:

- Fixed interest securities either in the form of Government development stocks or corporate bonds, generating interest income.
- Collective investments such as unit trusts, investment trusts and open ended investment companies, generating investment income.
- Equity investment in companies in the form of ordinary, preference and convertible shares, generating dividend income.
- Investment in immovable property, generating rental income.

(b) Interest income is exempt from income tax. It is subject to special defence contribution (SDC) at 10%, except for interest earned from Government development stocks, which is subject to SDC at 3%.

Income from collective investments is generally treated as dividend income. This is exempt from income tax but subject to SDC at 15%. Some unit trusts make interest distributions, which are again exempt from income tax but subject to SDC at 10%.

Income from equity holdings is dividend income, which is exempt from income tax but subject to SDC at 15%.

Rental income (less 20%; net of capital allowances and any bank loan interest) is aggregated with other income and taxed progressively at the relevant income tax rates. Gross rental income less 25% is also subject to SDC at 3%.

(c) As Loucas is a higher rate tax payer (30%) having taxable income of €48,000 before any new income generated from his possible investment of the €750,000 he is holding, he will be better off electing to be taxed on his overseas pension income under the special mode of taxation. Under this election, his overseas pension will be taxed separately as follows: the first €3,417 at 0% and the remaining pension of €24,583 at 5%. This will also mean that the income left to be taxed progressively at the normal income tax rates (UK rental income) will be reduced to €20,000.

(d) As the UK does not impose capital gains tax on disposals of UK assets by non-UK residents and as Cyprus only imposes capital gains tax on the disposal (direct or indirect) of immovable property situated in Cyprus only, Loucas could have avoided paying capital gains tax on his UK assets if he had become a Cyprus tax resident, before disposing of his UK assets.

4 (a) Group relief for trading losses in Cyprus, is granted through the surrender of losses of a loss making company against the profit of the same year of another company within the same group.

In order for companies to be considered as members of a group for loss relief purposes, all of the following must apply:

- the companies are Cyprus tax resident;
- the companies must have been members of a group for the whole of the relevant tax year; and
- one company must have a 75% interest in the share capital of another company or companies either directly or indirectly or two or more companies are owned to the extent of 75% by a third company.

(b) VAT payments will arise on intra-group trading, thus creating a temporary cash flow disadvantage, unless a VAT group is formed. It is possible to concentrate all exempt supplies (e.g. financial services) in one or two companies which can be left outside the VAT group. Companies making zero rated supplies (e.g. foodstuffs) can also be left outside the VAT group (or can form their own separate VAT group) and can make monthly repayment claims. In this way, VAT payments on intra-group transactions will be avoided and the 'zero-rated' companies will have a monthly cash inflow of input VAT.

(c) A holding company may be formed to hold the shares in other companies of the group. Any immovable property may then be registered in the name of a subsidiary or subsidiaries. In this way, if the shares of the subsidiary are sold by the holding company, no capital gains tax will arise, which would have been the case where the subsidiary itself sold the immovable property.

(d) The disadvantages of a group structure can be summarised as follows:

- Assets transferred between the group may give rise to a charge to tax, either in the form of a balancing charge increasing trading profits, or in the form of a capital gain.
- Higher set-up and administrative costs.

- In cases where the parent company or subsidiaries are to be sold, tax liabilities may crystallise as the group would either have to:
  - sell the group and then buy back the required subsidiaries; or
  - reorganise the group which would need tax rulings for approvals and cause delays.

(e) The advantages of a divisional structure can be summarised as follows:

- automatic set-off of trading losses in respect of the various divisions;
- automatic set -off of capital gains and losses; and
- administration is simplified.

On the other hand, the disadvantages include:

- lack of incentive for divisional directors;
- difficulty in giving equity interest in a venture, although profit-related bonuses may be considered;
- it may be more difficult to find a prospective purchaser for the whole company, as such a purchaser may only be interested in some operations of the company; and
- no asset protection (one loss-making operation may affect the viability of the whole company, jeopardising the owner's capital).

5 **(a)** As Dina and Fani are higher rate (30%) tax payers by reason of their income from employment, it will be more tax efficient for them to trade through a partnership in the first two years of operations. This is due to the fact that it is expected that losses will arise in the first two years, and these can be aggregated with their employment income and therefore, relieved at tax rates of up to 30%. This will not be the case if a limited company is formed, as the company's losses may only be carried forward and relieved against its future profits. In addition, by reference to a deemed distribution relating to the fourth year onwards, losses of previous years are not taken into account when computing accounting profits for deemed distribution purposes (see below).

In the third year, the two partners will be tax indifferent between choosing a partnership and a limited company as no profits/losses are expected.

In the fourth year onwards, a limited company would be more tax efficient, as profits from it may be extracted with an effective tax rate (corporation tax plus SDC on dividend payments) of 19·45% to 23·5% (after all trading losses have been relieved), depending on the dividend payout ratio, as compared with their current personal income tax rate of 30%, if profits are all extracted from the company in the form of a dividend, as opposed to remuneration (directors' salaries).

(b) Social cohesion fund contributions at 2% of any salary paid from a company to Dina and Fani will be due and payable by the company (employer). Nothing is due in respect of partnership profits.

(c) If the business premises are registered in the company's name, the company's only deductions against its trading income, will be the cost of repairs and capital allowances at 3% p.a. of the cost of renovation expenses.

If the premises are registered in Dina's and Fani's names and a market value rent is charged to the company, the company will be entitled to deduct these rental payments from its trading income, thus saving taxes at the shareholders' level at 19·45% to 23·5% (corporation tax and SDC on dividends). At the same time, Dina and Fani will be taxed on the rental income received at a rate of 24% (30% x (100 – 20%)) and also be subject to SDC at 2·25% (3% less 25%), giving a total tax burden of 26·25%.

On balance therefore, it is *prima facie* more tax efficient to acquire the building in the company's name. However, the tax position on sale of the building must also be considered. If the building is sold by Dina and Fani, capital gains tax at 20% will be assessed on them. If on the other hand the company sells the building, in addition to the capital gains tax of 20%, the company will have to withhold 15% SDC on the dividend payout to Dina and Fani. As the value of the possible future capital gain is uncertain, one could say that it will be more prudent to register the property in Dina's and Fani's names.

If the building is a 'preserved' building, rental income will not be subject to income tax in the hands of Dina and Fani. Note, however, that such rental income will still be subject to SDC.

(d) The new business will be providing services electronically. As these services will be provided in Cyprus and overseas, and the business belongs to Cyprus, the business will have to register for VAT in Cyprus if the registration limit of €15,600 is exceeded.

Services provided to non-EU countries are outside the scope of VAT in Cyprus, as the place of provision is where the recipient belongs. However, it should be noted that the business may have to register in these other countries based on their local requirements.

Services provided to other EU countries, although deemed as provided in those countries, triggers an obligation for registration in Cyprus. In addition, as the recipients of the services will be consumers and therefore not registered for VAT in their countries of residence, VAT at the standard rate will have to be charged in Cyprus and accounted for to the VAT authorities in Cyprus.

				Marks
1	(a)	(i)	No permanent establishment, profits taxed in Cyprus	1·0
			Set up overseas permanent establishment	1·0
			Overseas profits exempt overseas and in Cyprus	1·0
			No effect on SDC liability	1·0
				4·0
		(ii)	With current mode, all profits taxed in Cyprus	1·0
			Preferable as Cyprus has lowest corp. tax rate in the EU	1·0
			If branches formed, their profits taxed in countries of establishment	1·0
			As Cyprus has lowest tax rate, total tax burden higher	1·0
			Overseas subsidiaries offer more tax planning opportunities re: transfer pricing	1·0
			Tax exposure of subsidiaries in other EU countries reduced re: transfer pricing	1·0
			Subsidiaries' taxes lower than branches but complicated transfer pricing rules	1·0
			Use of subsidiaries may trigger withholding taxes on dividend payments	1·0
				8·0
		(iii)	Factory = permanent establishment in Romania	1·0
			Profits attributable to PE in Romania taxed there irrespective of where entity registered	1·0
			Taxability in Romania re-enforced by 'management and control' test	1·0
			Company more tax efficient with reasons	1·0
			Partnership not qualifying for EU directive	1·0
				5·0
		(iv)	Assessed to capital gains tax in Cyprus	0·5
			Explanation of tax basis	0·5
			Foreign subsidiaries not in own name	0·5
			Gains if shares in own name taxed in foreign countries	1·0
			If in Nemeas (Cyprus) Ltd name, no gain arising in foreign countries	0·5
				3·0
		(v)	On retirement sell share of holding company. No CGT in Cyprus as no direct ownership by holding company of immovables in Cyprus	1·0
			Transfer of ownership may trigger off CGT liability	1·0
			Tax liability avoided re: advanced tax ruling	1·0
			Delay dividend payout by two years	1·0
			Reduce dividend payout by 70%	1·0
			Explanation why delay and reduction above	1·0
				6·0
	(b)		Obligation to register re: local sales to Cyprus	1·0
			Place of supply in EU countries with explanation	1·0
			Distance selling of goods with explanation	1·0
			May have obligation to register in EU countries	1·0
			Account for VAT in EU countries through a VAT representative	1·0
			No distance selling in Romania with explanation	1·0
				6·0
			Format and presentation of letter	1·0
			effectivenss of communication	1·0
				2·0
			Total	**34·0**

				Marks
2	**(a)**	**(i)**	Andreas and brother subject to capital gains tax	0·5
			Explanation of how gain determined	0·5
			December 1996 value irrelevant, with reason	1·0
				2·0
		(ii)	Exchange of property is taxable event for CGT purposes	0·5
			1 January 1980 values comparison	0·5
			Roll over relief available	0·5
			Gain rolled over deducted from ‘cost’ of new asset	0·5
				2·0
		(iii)	Capital allowances deductible with explanation	1·0
			Definition of qualifying expenditure	0·5
			Other deductions for income tax purposes	1·0
			SDC deduction – 25% of gross rents only	0·5
				3·0
		(iv)	Decisive factors as to the determination of the type of transaction	1·0
			Treated as capital transaction with explanation	1·0
			Explanation of how deductible cost will be determined	1·0
				3·0
		(v)	Exchange of land treated as a disposal for CGT purposes	1·0
			Explanation of how the taxable base is determined	1·0
			Market value = developer’s consideration	1·0
				3·0
		(vi)	Explanation of total allowable cost	1·0
			Explanation of how parcellation expenses determined	1·0
			Plot allocated a cost and estimated gain, with explanation of basis	1·0
			Profit assessed in year of sale or exchange	1·0
			Explanation of how cost of remaining plots is determined.	1·0
				5·0
		(vii)	IPT imposed by reference to 1 January 1980 value	0·5
			If land sold in 2009 no taxable base	0·5
			Explanation of taxable base if exchanged with building	1·0
			Explanation of taxable base if land developed	1·0
			Explanation of taxable base if parcellation	1·0
				4·0
	(b)		Supply of buildings liable to VAT	0·5
			Single or two separate transactions depend on facts	0·5
			To decide need to consider, real intention, nature, content and character of transaction	2·0
			Other factors – 0·5 marks each	2·5
			Explain VAT treatment of exchange of land as consideration for development	1·0
			Explain VAT treatment where only part of land is transferred	1·0
			Conditions to be satisfied for the transaction to be considered as a supply of immovable property – 0·5 marks for each factor	2·5
			If above conditions not satisfied, two distinct transactions	1·0
			Explanation of the types of the two distinct transactions	1·0
				12·0
			Format and presentation of memorandum	1·0
			Effectiveness of communication	1·0
				2·0
			Total marks	**36**

			Marks
3	(a)	Fixed interest securities, types and type of income	1·5
		Collective investments, types and type of income	1·5
		Equity investments, types and type of income	1·5
		Investment property and type of income	0·5
			5·0
	(b)	Interest income exempt from income tax	0·5
		Subject to SDC at 10%	0·5
		Government development stocks interest subject to SDC at 3%	0·5
		Income from collective investments – dividend treatment	0·5
		Exempt from income tax	0·5
		Some unit trusts make interest distributions	0·5
		Dividends exempt from income tax, subject to SDC at 15%	0·5
		Rental income net of deductions aggregated with other income	1·0
		Rental income less 25% subject to SDC at 3%	0·5
			5·0
	(c)	Loucas is a higher rate tax payer	0·5
		Elect for special mode of taxation of pension income	1·0
		Explanation of the special mode of taxation	1·0
		Numbers illustrating the effect	0·5
			3·0
	(d)	UK not imposing CGT on UK assets of non-residents and Cyprus imposing CGT on disposal of assets in Cyprus only	1·0
		Loucas should have become Cyprus tax resident before disposing of UK assets	1·0
			2·0
		Total marks	**15**
4	(a)	Explanation of group relief	0·5
		Conditions to be satisfied – 0·5 marks each	1·5
			2·0
	(b)	Intra-group company VAT avoided by group registration	0·5
		Concentrate exempt supplies in one–two companies outside VAT group	1·0
		Concentrate zero-rated supplies in one–two companies outside VAT group	1·0
		Monthly VAT repayment claims	0·5
			3·0
	(c)	Form holding company to hold shares of other group companies	0·5
		Register immovable property in subsidiaries' names	0·5
		No CGT on sale of subsidiary companies shares	1·0
			2·0
	(d)	Possible tax due on transfer of assets	1·0
		Higher costs/administration	0·5
		Crystallisation of gains on partial break up	1·5
			3·0
	(e)	Advantages – 1 mark each	3·0
		Disadvantages – 1 mark each maximum 2 marks	2·0
			5·0
		Total marks	**15**

			Marks
5	**(a)**	Partnership preferable in first two years with explanation	2·0
		Limited company in first two years disadvantageous with explanation	1·0
		In fourth year onwards limited company better with explanation	2·0
			5·0
	(b)	SCF at 2% if salary paid from company	1·0
	(c)	If in company's name, deductions for cost of repairs and capital allowances	1·0
		If in Dina's and Fani's name, rent is a deductible expense, tax relief at 19·45–23·5%	1·0
		Dina and Fani taxed at 26·25%	1·0
		But on sale of building SDC at 15% in addition to CGT at 20%	1·0
		Explanation of tax treatment of 'preserved' building rental income	1·0
			5·0
	(d)	Company providing services electronically	0·5
		Obligation to register in Cyprus if registration threshold exceeded	0·5
		Services to non-EU outside Cyprus VAT scope with explanation	1·0
		May have to register in those non-EU countries	0·5
		Services to EU countries triggers obligation to register in Cyprus	0·5
		As customers not VAT registered in home countries charge VAT in Cyprus	1·0
			4·0
		Total marks	**15**