Strategic Professional – Options

Advanced Taxation – Cyprus (ATX – CYP)

Tuesday 4 December 2018

ATX CYP ICPAC

ATX – CYP

Time allowed: 3 hours 15 minutes

This question paper is divided into two sections:

Section A – BOTH questions are compulsory and MUST be attempted

Section B – TWO questions ONLY to be attempted

Tax rates and allowances are on pages 2–5

Do NOT open this question paper until instructed by the supervisor.

This question paper must not be removed from the examination hall.

Think Ahead ACCA

ΣΕΛΚ

The Association of Chartered Certified Accountants

The Institute of Certified Public Accountants of Cyprus

SUPPLEMENTARY INSTRUCTIONS

1. You should assume that the tax rates and allowances for the tax year 2017 shown below will apply for the foreseeable future unless you are instructed otherwise.
2. Calculations and workings need only be made to the nearest € unless you are instructed otherwise.
3. All apportionments should be made to the nearest month.
4. All workings should be shown.

TAX RATES AND ALLOWANCES

The following rates and allowances for the year 2017 are to be used in answering the questions

Income tax

€0 – €19,500	Nil
€19,501 – €28,000	20%
€28,001 – €36,300	25%
€36,301 – €60,000	30%
Over €60,000	35%

Corporation tax

All companies	12·5%

Special modes of taxation of certain kinds of income

Pensions of residents from services rendered outside the Republic (which exceed €3,420)	5%
Gross amount of royalties, premiums, compensation, etc	10%
Films rental, etc of non-residents	5%
Profits of non-resident professionals, artists, etc	10%
Widow's pension (in excess of €19,500)	20%

Capital allowances

Annual (wear and tear) allowances

Tractors, trenchers, excavators, bulldozers, transcavators, self-propelled shovels and loaders, drums, oil tanks	25%
Motor vehicles other than saloon cars	20%
Computer hardware and operating software	20%
Application software	
(a) if not exceeding €1,710	100%
(b) if exceeding €1,710	33·3%
Agricultural machinery and tools	
– acquired in the years 2012, 2013, 2014, 2015 and 2016	20%
– otherwise	15%
Other plant and machinery	
– acquired in the years 2012, 2013, 2014, 2015 and 2016	20%
– otherwise	10%
Hotel, industrial and agricultural buildings	
– acquired in the years 2012, 2013, 2014, 2015 and 2016	7%
– otherwise (maximum 25 years)	4%
Commercial and other buildings (maximum 33 years)	3%
Glass houses, metallic skeleton	10%
Glass houses, wooden skeleton	33·3%

Amortisation allowance

On the cost of purchase or development of intellectual property rights (from 1 January 2012 to 2 June 2016) – transitional provisions apply to 31 December 2016	20%

Interest and surcharge on unpaid tax

Interest on income and corporation tax assessments (Interest is calculated on the basis of completed months. The same rate applies to overpayments of tax.)	3·5% p.a.
Additional tax	5% of tax due
PAYE assessments	3·5% interest p.a. plus a surcharge of 1% per month

Special defence contribution

On dividends received (where applicable)	17%
On interest received	
– standard rate	30%
– reduced rate (applicable under specific circumstances)	3%
On rental income (on 75% of the gross rental income)	3%

Value added tax (VAT)

Registration limit	€15,600
Deregistration limit	€13,669
Standard rate	19%
Reduced rates	5%, 9%

Social insurance

Self-employed	14·6%
Employer	7·8%
Employee	7·8%
Maximum annual insurable income of employees	€54,396

Other contributions by employers

Social cohesion fund	2%
Redundancy fund	1·2%
Industrial training fund	0·5%
Central holiday fund (if not exempt)	8%

Capital gains tax

Rate	20%
Life time exemptions (maximum €85,430)	
– General	€17,086
– Farmer in respect of farm land	€25,629
– Residential dwelling	€85,430

Stamp duty

€nil for amounts up to €5,000
€1·50 for every €1,000 or part of €1,000 for amounts from €5,001 up to €170,000
€2·00 for every €1,000 or part of €1,000 for amounts exceeding €170,000 with a maximum amount of stamp duty of €20,000

Land transfer fees

€1 to €85,000	3%
€85,001 to €170,000	5%
Over €170,000	8%

Note:
For contracts concluded on or after 2 February 2011, no transfer fees will be payable when the immovable property to be transferred is subject to value added tax (VAT).

For contracts concluded on or after 16 July 2015, if the immovable property to be transferred is not subject to VAT the transfer fee will be reduced by 50%.

Retail Price Index For Capital Gains Purposes
Based on the Tax Department table of RPI

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1·1·80	67·15											
1980	67·99	68·53	69·14	71·51	70·56	70·70	72·12	72·16	73·41	74·00	74·50	75·21
1981	76·09	76·72	77·43	77·98	78·02	78·77	79·71	80·21	80·63	81·29	82·49	82·98
1982	82·94	83·70	83·48	84·60	84·40	83·81	83·44	83·99	84·89	85·23	86·22	86·80
1983	87·57	87·70	88·51	89·63	88·95	87·76	87·77	88·49	88·67	89·59	89·88	90·37
1984	91·16	91·78	92·31	92·92	93·73	93·83	94·92	94·41	94·13	95·33	96·81	97·77
1985	97·68	97·75	98·55	98·79	98·57	97·63	97·20	98·76	100·09	101·13	99·73	99·58
1986	100·22	100·12	100·33	99·53	98·44	98·36	99·39	99·37	99·34	100·65	101·92	102·39
1987	101·32	101·08	102·23	101·87	102·58	103·49	102·00	103·37	103·56	103·17	104·02	104·74
1988	104·61	105·44	106·05	107·16	106·06	105·11	104·39	105·09	106·30	107·51	108·92	109·12
1989	110·36	109·81	110·02	110·38	107·74	108·81	109·25	109·53	110·24	112·21	112·25	112·20
1990	111·80	112·84	114·04	115·72	116·19	115·32	114·27	115·11	115·48	116·78	117·16	118·70
1991	119·43	118·49	119·42	120·33	121·14	119·93	120·29	118·51	120·76	123·96	124·40	126·45
1992	127·91	126·18	127·76	129·79	127·72	127·15	127·93	127·18	128·77	130·44	132·09	134·65
1993	135·27	131·93	132·68	135·54	134·07	133·75	134·77	133·55	135·77	138·20	139·22	138·90
1994	138·52	135·29	138·64	139·99	140·23	141·13	141·68	139·57	144·27	146·90	146·57	146·14
1995	144·69	141·09	143·89	144·95	144·99	144·95	145·65	143·33	145·00	147·54	148·63	148·54
1996	148·32	144·76	148·61	149·23	149·68	149·58	150·06	148·10	150·64	151·97	152·04	152·26
1997	152·26	149·90	154·07	155·46	154·29	154·18	155·98	153·45	155·86	157·65	158·66	158·26
1998	155·27	155·06	156·03	157·95	158·20	158·87	158·10	159·15	161·66	161·07	160·35	159·70
1999	158·66	155·71	158·83	159·56	159·85	161·01	161·87	160·26	163·42	164·92	164·85	165·66
2000	165·52	163·60	166·72	167·40	168·05	167·16	167·12	166·74	168·78	169·81	170·68	170·92
2001	167·89	167·53	169·11	170·32	170·90	172·19	168·81	169·74	172·24	174·41	174·09	174·98
2002	172·43	172·05	173·11	174·83	174·93	175·69	174·42	176·15	178·11	178·79	179·06	180·13
2003	179·49	179·68	183·44	184·59	183·87	182·76	180·24	181·33	184·59	186·10	186·32	184·61
2004	182·74	183·03	184·18	185·48	186·61	187·87	186·18	187·13	188·97	190·81	191·88	192·36
2005	188·43	188·16	189·51	191·21	191·17	191·07	189·73	191·07	194·51	196·68	197·38	196·18
2006	193·03	193·26	195·55	197·16	197·33	197·58	195·01	196·12	198·29	199·45	199·87	199·75
2007	196·20	196·07	198·47	200·66	201·67	201·25	199·75	200·88	203·52	205·42	206·92	207·57
2008	204·70	205·73	207·80	209·93	211·64	212·26	210·99	211·74	214·37	216·17	214·02	211·93
2009	206·97	207·09	210·05	211·41	212·99	212·70	209·30	209·64	211·74	214·45	216·94	216·27
2010	212·01	213·04	215·08	216·58	216·41	216·83	214·68	216·44	219·23	220·98	220·17	219·82
2011	218·02	218·96	221·11	223·68	224·80	225·91	222·59	222·71	224·45	227·70	228·43	228·47
2012	224·82	225·72	228·56	230·58	231·43	229·91	227·43	228·66	230·10	231·66	231·18	230·98
2013	228·93	229·43	231·00	229·89	229·83	230·08	226·72	226·49	227·74	227·95	226·32	225·66
2014	222·32	223·51	225·72	226·22	226·70	227·35	225·39	224·86	225·66	226·83	225·97	222·36
2015	219·40	220·36	221·48	221·53	222·19	221·84	218·69	218·86	219·96	221·09	221·19	219·69
2016	216·16	214·43	215·87	216·22	217·57	217·26	217·68	217·50	218·62	218·80	218·67	219·68
2017	217·28	218·03	219·99	220·54	219·86	218·73	216·17	217·17	217·79	219·06	219·29	218·38

Section A – BOTH questions are compulsory and MUST be attempted

1 You should assume that today's date is 1 December 2018.

Your firm has been approached by a potential new client, Gatos Ltd (Gatos). Your tax partner has prepared the following file notes after a meeting with John, the sole shareholder and director of Gatos.

John is aged 55 and is a Cypriot national, tax resident and domiciled in Cyprus.

Gatos was registered in 2003 and is a Cyprus tax resident company which has specialised in pet food distribution to the Cyprus market for many years.

Gatos faced serious financial difficulties and has been loss-making since 2013. John has been so preoccupied with the financial difficulties that the company's taxation matters have been overlooked. Since 2015, the company's business has improved and whilst John is keen to settle all overdue taxes, he is deeply concerned how these liabilities will affect the fragile cash flow of the company.

John anticipates that the amount of tax due will be small as the company has tax allowable losses from previous years. He is keen to find out how much tax is payable by the company for 2015, 2016 and 2017, if any, and how much tax is already overdue.

As agreed on completion of the meeting, an email was received from the accounting department of Gatos with the following information:

The unaudited results of the company for the last three calendar years were as follows:

	2015	2016	2017
	€	€	€
Accounting (loss)/profit	(20,000)	200,000	305,000
Tax allowable (loss)/taxable profit	(50,000)	190,000	295,000
Total borrowings	500,000	551,000	632,000
Interest expense included in both accounting and taxable profits	21,400	23,417	25,280

With reference to the above results, the following information is given in the email:

1. The purchase of a saloon car in January 2016 for €47,600 (including VAT) was treated as a commercial van for corporation tax and VAT purposes. Total running expenses for the saloon car included in the unaudited results above were €1,500 in 2016 and €3,800 in 2017. VAT claimed on these expenses was €150 for 2016 and €410 for 2017. The saloon car was used wholly for business purposes. Gatos depreciates all its cars for accounting purposes over seven years.
2. In 2004, Gatos bought shares representing a holding of less than 1% in TRX Ltd for €15,000. TRX Ltd is a portfolio investment company specialising in investments in other companies internationally and is listed on the Triland Stock Exchange. TRX Ltd is tax resident in Triland and has never held any assets in Cyprus. In November 2015, Gatos received a dividend from TRX of €2,000, which was paid into Gatos's bank account in Triland. In July 2017, the shares of TRX Ltd were sold for €50,000 and the proceeds were deposited in the same bank account in Triland.

   The bank account in Triland received €250 of interest in December 2017, which is tax free in Triland.

   Neither the dividend, nor the sale of the shares, nor the interest received were recorded in Gatos's books, accounting or taxable profits. Triland listed companies are exempt from tax in Triland.
3. Gatos signed a contract to sell a plot of land for €500,000 on 15 October 2017. The sale was made to a third party who paid an advance of €50,000 in cash to John on 1 October 2017. The balance of the proceeds will be collected by the bank directly, to repay the fixed mortgage it holds on the land. The sale, which will be taxed under capital gains, was not recorded in the books of the company and is not included in the results above as the transfer of the land at the Land Registry has not taken place yet. The plot of land was bought in June 2003 for €300,000. Transfer fees of €17,165 were paid in addition to the purchase price. The plot is sited in an industrial area and was acquired with the intention to build warehousing facilities for the company's use. This development did not take place and the land has remained unused throughout the period of ownership. Gatos has not sold any immovable property in the past.

4. John earns a gross salary of €28,000 per annum from Gatos. The social insurance and income tax due on his salary have been calculated correctly and paid on time through the company's payroll.
5. John used the €50,000 advance from the sale of the land considered in note (3), above, to settle a personal debt. He refunded the €50,000 to the company on 1 February 2018 and the balance of his director's current account returned to nil. No tax has been accounted for on this transaction by Gatos.
6. Gatos has not paid any dividends since 2013 and does not plan to do so for the next five years.
7. No provisional tax or special defence contribution was paid for the three years 2015, 2016 and 2017. All tax liabilities up to and including the tax year 2014 have been calculated correctly and paid on time.
8. Gatos's taxable losses brought forward from 2013 and 2014 were €70,000 and €55,000, respectively.

Required:

To assist the tax partner in her next meeting with John about Gatos Ltd, prepare a memorandum summarising all of the taxes payable by the company for 2015, 2016 and 2017 from the information provided.

You should include appropriate computations and summarise the results in a table showing the taxes due and overdue, and the due dates of payment.

The tax partner has asked you to include in the memorandum a note of ethical considerations which should be borne in mind before accepting an engagement with Gatos Ltd.

The following marks are available:

(i) Corporation tax. (8 marks)

(ii) Special defence contribution (SDC). (13 marks)

(iii) Capital gains tax. (3 marks)

(iv) Tax(es) on John's debt to the company. (5 marks)

(v) Ethical considerations. (2 marks)

Note: You should ignore interest and penalties on overdue taxes.

Professional marks will be awarded for the format and presentation of the memorandum and the clarity and effectiveness with which the information is communicated. (4 marks)

(35 marks)

2 You should assume that today's date is 3 December 2018.

Andri has contacted your firm for advice: she is a successful businesswoman from Greece, who wishes to become a tax resident of Cyprus and to relocate all of her business interests from Greece to Cyprus.

The following information has been obtained from emails and phone conversations with Andri.

Andri was born in Cyprus from Cypriot parents, in 1972. Her family moved to Greece in 1974 and still live there. Andri has previously visited Cyprus for occasional holidays since 1974 but has never stayed for more than two weeks per year. She is a graduate of Harvard Business School and is a skilled adviser to international venture capital investment managers. As a result Andri travels extensively for business purposes.

Andri is the sole director of Estia Ltd (Estia), a company set up and registered in Farland five years ago, which specialises in making investments in international property. The company is (and will always be) considered tax resident in Farland due to its registration there. Andri is involved in the day-to-day management of Estia and is the only signatory to the bank account, but she does not own shares in the company.

Estia Ltd owns immovable property in many countries, including Farland and Cyprus. In Cyprus, it owns a block of flats purchased three years ago from which it earns rental income of €50,000 per year. All of the flats are rented to physical persons. All the profits of Estia are reinvested. There is no double tax treaty between Cyprus and Farland.

Marios, who is domiciled in Cyprus and a Cyprus tax resident, owns 10% of the share capital of Estia but all the other shareholders are non-Cyprus tax residents. Marios is not related to Andri in any way.

Andri has registered a new company in Cyprus, Inelixis Ltd (Inelixis). Andri is the only director of Inelixis and holds 100% of the share capital. Inelixis will engage Andri, along with other professional individuals, to provide venture capital investment advice to local and international clients.

Apart from her employment income, Andri receives dividends on a regular basis from her personal portfolio of investments in various companies worldwide.

Andri is keen to become a Cyprus resident as soon as possible as she believes that this will allow her to save a significant amount of tax in Greece, where tax rates have escalated in recent years. She has informed you that she will require a Cyprus tax residency certificate for the Greek tax authorities.

Required:

(a) Discuss the options available to Andri to become a Cyprus tax resident and how soon her Cyprus tax residency can be arranged. (8 marks)

(b) Describe how Andri's dividend income will be taxed in Cyprus once she becomes Cyprus tax resident. (4 marks)

(c) Explain why Estia Ltd will be considered Cyprus tax resident when Andri relocates to Cyprus, and detail the Cyprus tax and special defence contribution implications for Estia Ltd of becoming a Cyprus tax resident. (13 marks)

(25 marks)

Section B – TWO questions ONLY to be attempted

3 Stefanos, a Cyprus tax resident and domiciled individual, is a self-employed dentist working since 2000 out of a dental surgery he owns in central Nicosia. He files his tax return as a self-employed person every year and pays all his taxes on time; he pays social insurance on the same basis.

Stefanos is not registered for VAT because dental services are an exempt supply. However, Stefanos is planning to start selling tooth care products in his surgery, all of which will be taxable under VAT at either 5% or 19%. He plans to register for VAT voluntarily before he starts to sell these products.

Stefanos expects sales of tooth care products to grow steadily and reach €60,000 a year, with an annual profit of €30,000. This will increase his current turnover from €60,000 to €120,000. His taxable income currently stands at about €45,000 per year.

Stefanos urgently needs to buy a new tooth drill which a local supplier will sell to him for €3,000 plus VAT. Alternatively, a supplier in Austria will sell him an equally suitable drill for the same price, including delivery to Cyprus.

Required:

(a) Describe the income tax and social insurance implications for Stefanos of the sale of tooth care products and the purchase of the tooth drill, including filing deadlines and payment dates. (7 marks)

(b) Discuss the VAT implications of Stefanos starting to sell tooth care products. (5 marks)

(c) Advise Stefanos whether he should delay purchasing the drill until after he is VAT registered. Given he needs to buy the drill urgently, explain whether it would make any difference if Stefanos were to buy it from the Austrian supplier.

Note: Austria is a member of the European Union (EU). (5 marks)

(d) In December 2018, Stefanos received a tax assessment for 2014 showing tax payable of €4,000, even though he filed his tax return and paid all the tax due on time.

Required:

Consider why the tax department may have raised a tax assessment and explain the options available to him. (3 marks)

(20 marks)

4 Evi, a Cyprus tax resident and domiciled businesswoman, owns and is a director of XS Ltd (XS), a very successful energy drinks import and distribution company in Cyprus. XS owns a large warehouse in Limassol out of which it operates. The land was purchased in 1974 for €70,000 and the warehouse was constructed over a period of months in 1980, at a cost of about €200,000. The current market value of the warehouse is more than €3 million.

Evi currently owns 100% of the issued share capital of the company, comprising 10,000 ordinary shares with a nominal value of €1 each. Evi acquired 5,000 shares at the time of registration of the company for €1 each and inherited the other 5,000 from her father five years ago when the market value of each share was €340 each.

One of XS's main suppliers, Apre Ltd, is keen to buy 80% of the shares of XS from Evi. Apre Ltd is a producer of energy drinks, is tax resident in France, and has incurred losses for tax purposes in recent years. They have commissioned an independent valuation for the company which shows a value of €400 per share which includes the value of the immovable property of the company.

After the valuation, Apre Ltd has written a letter to Evi stating that by buying a share of XS Ltd as it stands today at the value of €400 per share, they will be investing indirectly in immovable property in Cyprus which is something they do not want to do. They have made another offer, to buy 80% of the shares for €120 per share but without the immovable property. They have suggested that the immovable property could be transferred outside XS, either to Evi or to another company which belongs to Evi. In either case, XS would continue to use the warehouse and pay rent to the new owner of the warehouse, at the market rate.

Required:

(a) Explain what taxes, if any, Evi will have to pay on the sale of her shares in XS Ltd to Apre Ltd.

Note: You are NOT required to make calculations for this part. (4 marks)

(b) In view of the fact that Apre Ltd is loss-making, explain how the sale of shares to Apre Ltd could affect the future corporation tax and special defence contribution (SDC) liabilities of XS Ltd, assuming XS Ltd has been profitable since 2012.

Note: France is a member of the European Union (EU). (5 marks)

(c) Explain the tax implications for XS Ltd and Evi of transferring the immovable property to Evi and renting it.

Note: You are required to consider all relevant taxes. You are NOT required to make calculations for this part. (7 marks)

(d) Discuss whether it would be possible to use either the 'partial division' or the 'transfer of assets' type of re-organisation scheme to separate the immovable property from XS Ltd without XS Ltd being liquidated. (4 marks)

(20 marks)

5 Axonas Ltd (Axonas) is a Cyprus tax resident and VAT registered company, which sells spare car parts from a scrap yard in Larnaca, Cyprus. George, who is a mechanic by profession, owns 100% of the share capital of the company; he is also the only director. George is tax resident and domiciled in Cyprus.

On average, Axonas makes accounting profits of €100,000 per year, and this is expected to continue for the foreseeable future. Taxable profits are equal to accounting profits. Two years after the end of a year, Axonas pays dividends equal to the minimum required by the provisions of the special defence contribution (SDC) legislation.

George's gross salary has been €12,000 per year for several years. Income tax and social insurance payable on the salary is deducted and paid on a regular basis through the company's payroll. The company has exemption from contributions to the central holiday fund for all its employees. Other than his salary and dividends from Axonas, George has no other income or personal allowances.

Axonas has an agreement with Tsiao, a retired engineer who lives in Japan, who visits suppliers in Japan to inspect used parts Axonas is interested in buying and importing to Cyprus. Tsiao invoices for his services on a piece-by-piece basis. The amount he invoices ranges from €5,000 to €20,000 per year. Tsiao is not registered for VAT and does not charge VAT on his invoices. Due to the very good relationship he has with George, Tsiao's invoices are always paid immediately and in full.

Tourists who visit Cyprus for holidays come to Axonas's yard in Larnaca to buy spare parts for rally cars, which Axonas sells at competitive prices. Customers often say they should not pay VAT on their purchases because they will export the parts to their home countries, outside Cyprus. To make sales more attractive, George is keen not to charge VAT on sales to tourists who bring good business to the company.

Required:

(a) Explain how an increase in George's salary to €21,000 per year will reduce the total tax liabilities payable by Axonas Ltd and George. Support your explanation with calculations, and note any non-tax advantages to George of drawing a salary of €21,000 per year. (10 marks)

(b) Explain the Cyprus VAT and income tax implications of Tsiao's services. (4 marks)

(c) Explain the VAT treatment of local sales to tourists. Suggest if there is a way for VAT on these sales to be reduced or avoided. (6 marks)

(20 marks)

End of Question Paper