

# THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2022

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## MODULE 2.03 – CYPRUS OPTION

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### ADVANCED INTERNATIONAL TAXATION (JURISDICTION)

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TIME ALLOWED – 3¼ HOURS

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This exam paper has **three** parts: **Part A**, **Part B** and **Part C**.

You need to answer **five** questions in total. You will **not** receive marks for any additional answers.

You must answer:

- **Both** questions in **Part A** (25 marks each)
- **The** question in **Part B** (20 marks)
- **Two** questions from **Part C** (15 marks each)

#### Further instructions

- All workings should be made to the nearest month and in Euros, unless otherwise stated.
- As you are using the online method to complete your exam, you must provide appropriate line breaks between each question, and clearly indicate the start of each new question using the formatting tools available.
- Marks may be allocated for clarity of presentation of your answers.
- The time you spend answering questions should correspond broadly to the number of marks available for that question. You should therefore aim to spend approximately half of your time answering Part A, and the other half answering questions in Parts B and C.
- There is no separate reading time, so you can start typing your answers as soon as the exam begins. However, we recommend that you set aside some time to thoroughly read each question and plan each of your answers.

## PART A

**You are required to answer BOTH questions from this Part.**

1. Alex is a citizen of Sweden, an EU member state. During 2021, Alex had the following income:
- Salary from X plc, a Swedish tax resident company for whom she acted as a financial consultant;
  - Salary from CypCo Ltd, a wholly-owned Cypriot subsidiary of X plc which was formed in early January 2021;
  - Non-executive director fees received from other Swedish tax resident companies;
  - Rental income received from tourist apartments which she had owned since 2012 in Ghana, a non-EU state (net of a 10% withholding tax);
  - Gains on the sale of shares held in Cyprus listed companies; and
  - Gains on the disposal of her tourist apartments in Ghana.

Alex was employed by CypCo Ltd in Cyprus, but also spent time in Sweden while remaining on X plc's payroll. She moved to Cyprus on 15 January 2021, but her family stayed behind in Sweden.

During the course of 2021, Alex spent a total of 200 days in Cyprus, 150 days in Sweden and six days on holiday in a third country. During the time spent in Sweden, apart from working for X plc, Alex also spent some time attending the board meetings of other Swedish tax-resident companies, as she had in previous years.

CypCo Ltd provided a house in Cyprus to Alex free of charge, at a cost to CypCo of €14,000, and leased a car which was at Alex's sole disposal, also for free, at a cost of €7,000. All fuel costs were paid by Alex.

Alex opened a bank account in Cyprus, into which her salary from CypCo Ltd was deposited. Her salary from X plc and her non-executive director fees from the other Swedish companies were paid into her Swedish bank account. The disposal proceeds of the Ghana tourist apartments were remitted to Alex's bank account in Cyprus.

According to the domestic tax legislation of Sweden, Alex will be treated as a tax resident of Sweden for 2021.

You may assume that Cyprus has a double tax agreement (DTA) with Sweden, whose provisions are identical to the OECD Model Treaty, and that Cyprus does not have a DTA with Ghana.

**You are required to:**

- 1) **Discuss Alex's tax residency position.** (12)
- 2) **Explain the tax treatment in Cyprus and Sweden of each income item received by Alex, according to the domestic tax legislation of Cyprus and the DTA between Cyprus and Sweden. What exemptions or reliefs may be available to Alex in Cyprus?** (13)

Total (25)

2. You recently had a meeting with Mr Taras, the 96% shareholder in Super Ltd. Super Ltd controls 60% of Sikma Ltd; with the remaining 40% of Sikma Ltd belonging to three minority shareholders.

Mr Taras has recently agreed with Ms Makis, the 99% owner of Fail Ltd, to merge his group with Ms Makis's company. He also agreed with the three minority shareholders of Sikma Ltd for Super Ltd to acquire the Sikma Ltd net assets, through an exchange of shares and a small payment in cash.

Fail Ltd has accumulated tax losses in recent years. All three companies own immovable property, situated mostly in Cyprus. Sikma Ltd is involved in the wholesale distribution of home appliances and furniture, while the other two companies are involved in the retail distribution of the same commodities. Sikma Ltd also operates outside Cyprus, through overseas branches.

The current balance sheets of the three companies are as follows:

|                                      | Super Ltd (€)  | Sikma Ltd<br>- Cyprus (€) | Sikma Ltd -<br>overseas<br>branches (€) | Fail Ltd (€)    |
|--------------------------------------|----------------|---------------------------|---|-----------------|
| Immovable property at net book value | 250,000        | 70,000                    | 25,000                                  | 60,000          |
| Other assets                         | 80,000         | 40,000                    | 25,000                                  | 30,000          |
| <b>Total assets</b>                  | <b>330,000</b> | <b>110,000</b>            | <b>50,000</b>                           | <b>90,000</b>   |
| Share capital                        | 100,000        | 50,000                    |   | 20,000          |
| Profit and loss account              | 170,000        | 40,000                    | (20,000)                                | (80,000)        |
| <b>Share capital and reserves</b>    | <b>270,000</b> | <b>90,000</b>             |   | <b>(60,000)</b> |
| Liabilities                          | 60,000         | 20,000                    | 70,000                                  | 150,000         |
| <b>Capital and liabilities</b>       | <b>330,000</b> | <b>110,000</b>            |   | <b>90,000</b>   |

You have also received the following information:

- It is expected that Sikma Ltd's Cyprus operations will continue to be profitable, but most of the overseas branches will continue to incur losses for the next three years, after which all overseas operations are expected to become profitable.
- Although Ms Makis has already agreed to the merger through an exchange of shares, she insists on receiving cash with respect to the value of the company's accumulated tax losses. Mr Taras and Ms Makis disagree upon how this value should be determined, as Ms Makis insists on attaching both a Corporate Income Tax and a Special Defence Contribution element to this value.
- Fail Ltd's operations are expected to turn profitable after one year, as Mr Taras anticipates the negotiation of lower prices on the purchase of merchandise, better payment terms and a reduction in overheads as a result of the merger.
- Accumulated accounting losses as above, equal tax losses.

**You are required to:**

- Describe the methods under which the merger of the three companies may be achieved, explaining the pre-requisites that must be fulfilled for such a merger to qualify for tax exemptions under a 'scheme of re-organisation', and which tax exemptions will be available in this case. (10)**
- Describe the steps that will need to be taken to facilitate the proposed merger, assuming that no new company will be formed. (4)**
- Provide a recommendation as to how the value of Fail Ltd's tax losses may be determined, stating any limitations on the amount of the cash payment and any personal tax implications for Ms Makis. (5)**
- Advise as to how the overseas operations may be structured in order to become more tax efficient in the future, with reference to future profitability expectations. (6)**

Total (25)

**PART B**

**You are required to answer THIS question.**

3. Kenneth is domiciled in the United Kingdom, where he has lived and worked for most of his life. He recently moved permanently to Cyprus, after selling his home and some other immovable property in the UK.

As of 15 December 2021, Kenneth owns the following immovable property in the UK and Cyprus:

| <u>Description</u>   | <u>Market value (€)</u> | <u>Cost (€)</u> | <u>1 Jan 1980 value (€)</u> |
|--|-------------------------|-----------------|-----------------------------|
| Freehold shop in the UK<br>(acquired on 20 January 2013)   | 800,000                 | 420,000         | 110,000                     |
| Plot in Nicosia (acquired on 2 February 2013)  | 600,000                 | 300,000         | 180,000                     |
| Agricultural land in Pafos<br>(acquired on 20 November 2018)   | 320,000                 | 260,000         | 50,000                      |
| Agricultural land in Lythrodontas<br>(a gift from Kenneth's mother on 20 June 2013, then valued at €160,000, originally acquired on 13 January 1975) | 280,000                 | 20,000          | 40,000                      |

Kenneth intends to acquire a villa in Cyprus from a land developer, which he expects to use as his main residence for a number of years before selling it, as he plans to move back to the UK at a future date, when his children are ready to go to university. However, Kenneth has not ruled out the possibility of retaining the villa and renting it out when he and his family return to the UK.

The value of the villa is €600,000 including VAT (the 1 January 1980 value was €100,000). Kenneth is seeking to exchange one or more of his existing properties for the villa, and has proposed the following options to the land developer:

- a) Kenneth sells the UK shop to the Cyprus developer, in return for the villa plus €200,000 in cash;
- b) Kenneth purchases the villa from the developer in exchange for his plot in Nicosia; or
- c) Kenneth purchases the villa in exchange for the two pieces of agricultural land.

Kenneth has not previously sold or exchanged any immovable property in Cyprus.

**Ignoring any VAT implications, you are required to answer the following questions:**

- 1) **What is Kenneth's exposure to Capital Gains Tax, under the three property exchange options described above? You should consider all available exemptions and reliefs, and support your answer with appropriate computations, assuming a 30% indexation allowance where applicable.** (11)
- 2) **For each of the three exchange options above, on what value will the deductible cost be based in a future disposal of the villa? Are any further exemptions or reliefs available, and what conditions will have to be met to qualify for them?** (6)
- 3) **If Kenneth decides not to sell the villa when he moves back to the UK, will the rental income generated from it be subject to Income Tax, Special Defence Contribution or General Healthcare System (GeSY) contributions in Cyprus?** (3)

Total (20)

**PART C**

**You are required to answer TWO questions from this Part.**

4. **You are required to briefly explain the scope and objectives of the OECD/G20 BEPS Project, by also referring to its EU tax law consequences. Explain the statutory measures that Cyprus has taken in response to the BEPS Project.** (15)
5. **How is domicile determined in the context of Cypriot tax legislation? What are the tax implications for a non-domiciled individual who is a tax resident of Cyprus?** (15)
6. A trust was founded in Cyprus in 2021 under the International Trust Law 20(I)/2012, with both Cyprus and non-Cyprus resident beneficiaries.

**You are required to explain how the trust's income and gains will be treated for Income Tax, Capital Gains Tax, Special Defence Contribution and Stamp Duty purposes.** (15)

7. "The profits of life insurance and non-life insurance undertakings, as defined in the Law on Insurance Services and other Related Issues Law (Law 35(I)/2002 as amended), are taxed under a special taxation regime."

**You are required to:**

- 1) **Briefly describe how insurance companies are assessed for Income Tax purposes, and demonstrate how taxable profits are calculated.** (11)
- 2) **Calculate the Income Tax payable by a life insurance company recording gross premiums of €1.8 million and taxable income of €212,000 in 2021.** (4)

Total (15)