



CYPRUS TAX LEGISLATION ON COMPANIES  
**(THE FOREIGN INVESTORS' APPROACH)**

2013

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## **A. INTRODUCTION**

The Republic of Cyprus as from the 1/5/2004 is a full Member State of the European Union.

In view of its European Union accession, and in order to harmonies its domestic legislation with European Union Law and The European Code of Conduct and also in order to fulfill its commitment to OECD that it will eliminate harmful tax practices, the Republic of Cyprus in 2002 undertook a major tax reform. This reform had also to meet the requirement of keeping Cyprus as a competitive International Business Centre getting ready for a Global tax competition within internationally accepted boundaries. This was achieved, inter alia, by legislating a new Income Tax Law, a new Special Contribution for the defence of the Republic Law and major amendments to various other laws and other legislative measures.

This new tax legislation has been accepted by the European Commission and is in force as from 1<sup>st</sup> January 2003.

The new tax legislation is one of the major tax reforms world-wide and its outcome provides the international investor with highly interesting tax planning opportunities within limits accepted and respected by the international community.

## **B. THE TAX REFORM**

### I. General

With this publication, we outline the main provisions of those taxation laws that affect mainly international investors doing business through Cyprus as well as some international tax planning aspects that may be of interest to such international investors.

However, it is not intended to be legal or tax advice or opinion. Affected or interested companies and individuals are recommended to receive further professional advice based on their own particular case.

### II. Application of the Tax Law

The new taxation system applies only to:

- the worldwide income of **tax residents** of Cyprus and
- to the income that non tax residents of Cyprus derive in Cyprus – Cyprus source income

In effect:

- A Company or an individual are taxed in Cyprus only if they are **tax residents** of Cyprus. Tax residents are taxed on their worldwide income.
- Non – tax residents of Cyprus are not subject to any kind of Cyprus taxation, except for income that the non tax residents (company or the individual) derive from operations or a permanent establishment in Cyprus.
- There is no longer a distinction between local and offshore companies as the law provided in the past. All companies are treated in the same way.
- Companies and individuals as to taxation matters will be distinguished now as:-

- (a) Tax residents and
- (b) Non tax residents.

III. "Residence" and "Cyprus source income" - Conditions to be met before the taxation laws are applied to any company or individual

Since the new tax system applies only to tax residents of Cyprus or to the Cyprus source income of non - residents, the identification of:

- the residency status of the company or the individual and
- the Cyprus source income of the non – resident,

play the major role of the whole legislative tax structure, which will generate its application.

**Definition of tax resident**

- a) **In the case of an individual** – means an individual who stays in Cyprus for one or more periods exceeding, in aggregate 183 days in the year of assessment.
  
- b) **In the case of a company** – means a company whose "*management and control*" is exercised in Cyprus. The management and control of a company is exercised by its board of directors. The nationality or the residence of the shareholders is irrelevant. It is also irrelevant where the company was registered, whether in Cyprus or abroad. Incorporation in Cyprus is not sufficient to qualify the company as a resident of Cyprus.

There is no definition in the law of the meaning of "*management and control*". It is expected that the Commissioner of Income Tax will adopt the meaning that the court decisions of Commonwealth countries follow on this matter. As the residence issue is a factual matter, this is expected to be determined by considering a number of factors which will point to the central management and control of the company, that is:

- The place of directors' meetings, where Board decisions are taken. This factor is treated as being the most crucial;

- The residence of the directors or at least the majority of them;
- The degree of control exercised by the directors on company decisions. Where the general policy of the company is formulated. (It is important to point out that the issuing of a general power of attorney to a non-director, might be considered as an abdication of control and before issuing such a power of attorney, careful consideration must be given);
- Whether the directors think and decide the policy issues of the company and take their own decisions or blindly follow the instructions of a non-director or the shareholders or the beneficiaries;
- In which country the bank accounts are situated and who manages them (who the signatories of the accounts are);
- Where and whether the directors consider and there after sign the contracts / invoices the company is executing and issuing;
- Are the directors simply signing agency acting on instructions or they think and decide whether the particular contract to be signed or step to be taken is to the benefit of the company or not.

### **Our comments**

It is expected that the Cyprus Commissioner of Income Tax will more easily accept a company as being tax resident, rather than non tax resident. This is due to the fact that a tax resident company is liable to taxation, while a non tax resident is not liable to any taxation at all (except for income derived from within Cyprus).

If a company would like to be considered as a non tax resident it will be up to the company to submit such evidence proving that the management and control is outside Cyprus.

If the directors of the company are resident in Cyprus, the board meetings are held in Cyprus, the board decisions are taken in Cyprus, the directors are thinking and deciding the policy decisions of the company and contracts and other company documents are signed in Cyprus by the directors, then the "*management and control*" of the company will, most probably will be considered by the Cyprus tax authorities as being in Cyprus.

As the tax residency of the company is a matter which might have dual face, then this issue must always be considered from the aspect of the foreign law where the company is trading or where the shareholders reside. Special provisions are also included as to this issue in double tax treaties and their terms must always be considered.

For a detailed analysis of the management and control issue, please refer to our publication: ***Cyprus Tax Resident Companies Management and Control Test.***

### **Non tax resident companies/individuals**

A non tax resident company or an individual are taxable in Cyprus only if they derive income from within Cyprus and they are taxable only as to this "Cyprus source income".

It is important to note though, that the non tax resident company, on the one hand, will not be subject to Cyprus taxation (0%) but on the other hand, it will not be able to use the benefits of the double taxation treaties that Cyprus has signed with various countries, as these treaties apply only to tax residents of either contracting country.

### **Definition of Cyprus source income of a non tax resident**

A non tax resident company is subject to taxation only on certain Cyprus source income, namely:

- profits from a permanent establishment in Cyprus;
- rents, royalties, film rentals or other profit arising from a property in Cyprus;

- gains from trade goodwill arising from the disposition of a business with a permanent establishment in Cyprus;

A non tax resident individual apart from the above cases which might generate income to it in Cyprus is subject to taxation on Cyprus source income and on:

- gross receipts of theatrical, musical or other group of public entertainers, including football clubs and other athletic missions from abroad, derived from performances in Cyprus, irrespective of a permanent establishment in Cyprus;

## **C. TAXATION OF TAX RESIDENT COMPANIES**

### I. General Taxation on Companies

A Cyprus tax resident company is taxed on its worldwide income.

Net profits are taxed at company level with 12.5% corporation tax.

Particular type of income such as passive interest income, rents and dividends on certain remote conditions are taxed with Special Defence Contribution Tax as will be explained below.

#### **Taxable Income**

The categories of income applicable to companies, either with corporation tax or special defence contribution tax are:

- business profits (such as trading, manufacturing, industrial, farming, agriculture);
- interest and discounts;
- dividends (for defence contribution tax only, subject to certain conditions);
- rents, royalties, remuneration or other profits from property;
- gain in respect of trade goodwill;

Taxes paid abroad on the same income are credited against the Cyprus tax. Tax credit is given as this will be explained below.

Dividends, interest income, royalty income and profits from a permanent establishment abroad, are taxed under special rules as explained below.

Special status is also granted to ship owning and ship management companies as explained below.

The financial statements must be prepared in accordance with the International Financial Reporting Standards (IFRS).

The taxable profit is calculated by aggregating the taxable income from all categories listed, in the year of assessment and reducing this figure by allowable deductions which were incurred solely and in connection for the production of the taxable income. The net figure is subject to corporation tax.

Any prior year tax losses carried forward can reduce the final tax payable in the year.

### **Taxation of Interest**

The Law as before 1.1.2009 has employed a rather complicated procedure as to the taxation of Interest Income.

The complication though has been lifted by relevant amendment in the Law which applies as from 1.1.2009.

In effect now, we have two sets of rules governing the taxation of interest income. Those applicable before 1.1.2009 and those applicable after 1.1.2009.

The Law distinguishes in an indirect way between **trading** interest income and **passive** interest income. The following questions and their respective reply identifies the nature of the interest income:-

- a. Is the particular interest income acquired from the ordinary activities of the company?
- b. Is the particular interest income acquired from activities **closely connected** with the ordinary activities of the company?

If the answer to either of the above two questions is positive, then the interest is treated as **trading interest income** and if not, as **passive interest income**.

The trading interest income is subject to corporation tax at 12.5% taxation on net profits, if any.

If the answer to the above two questions is negative, then the interest is treated as **passive interest income** and is taxed only under Special Defence Tax at a rate of 30% on the interest income received or credited.

It is important to note that this taxation is imposed not only on the received interest but also on the credited interest to be received by the company at a future date.

For a more detailed analysis of the taxation of interest income kindly refer to our publication: **“Cyprus - Taxation of Interest income”**.

## II. Exempt Income

The following constitute exempt income under the tax legislation:

- a) Profits from activities of a permanent Establishment situated outside Cyprus under certain conditions;
- b) Profits from the disposal of titles (securities);
- c) Dividends;

d) Royalties – partial exemption

**a) Profits from activities of a permanent Establishment situated outside Cyprus: -**

The profits, which the tax resident Cyprus company may have from a permanent establishment outside Cyprus, shall be fully tax exempt (0%).

This exemption is not granted if:

- The permanent establishment, either directly or indirectly, is engaged by more than 50% in activities which lead to investment income

**AND**

- The foreign tax rate imposed on this income of the permanent establishment is substantially lower than the tax rate payable in Cyprus, by the company which is tax resident of Cyprus. Substantially lower has been interpreted to mean less than 5%.

**Meaning of investment income**

Investment income means an income, which is not acquired or received from any enterprise (trading or industrial business) or from salaried services, pensions or other annuities payable for or in respect of salaried services rendered.

## **Meaning of permanent establishment**

Means:

A fixed place of business through which the operations of the enterprise is wholly or partly carried on and, includes especially:

- a place of management,
- a branch,
- an office,
- a factory,
- a workshop, a building site or construction, or installation project or supervisory activities relating to such projects, provided they last for more than three months,
- a mine, oil well, source of light gas, quarry or any other place of extraction of natural sources of gas.

The following do not constitute a permanent establishment:

- The use of facilities for storage, display or delivery of goods.
- The keeping of stocks of goods for storage, display or delivery purposes.
- The keeping of stocks of goods for the purpose of processing by another person.
- The keeping of a fixed place of business solely for the purpose of purchasing goods or for collecting information for the business.
- The use of the services of an agent who is of an independent status.
- The keeping of a fixed base of business for preparatory or assisting work for the business.

## **b) Profits from the disposal of titles**

Profits from the disposal of titles i.e. shares, bonds, debentures, founders' shares and other titles of companies or other legal persons incorporated in Cyprus or abroad and rights thereon, are fully exempt from any corporation tax (0%).

Profits realised from the disposal of titles are also exempt from any capital gains tax except as to the disposal of shares of companies which own immovable property in Cyprus. Such

disposal is subject to capital gains tax at the rate of 20% according to the provisions of the Capital Gains Tax Law as amended.

As the above definition of titles was not clear, a circular was issued by the Income Tax Authorities listing the financial instruments that fall within the definition of “titles” as mentioned in the Income Tax Law. The legislation provides that any gain on the disposal of titles is exempt from income tax. The full list of financial instruments that fall within the definition is as follows:

- Ordinary shares
- Founder’s shares
- Preference shares
- Options on titles
- Debentures
- Bonds
- Short positions on titles
- Futures/forwards on titles
- Swaps on titles
- Depositary receipts on titles (ADRs and GDRs)
- Rights of claims on bonds and debentures (rights on interest of these instruments are not included)
- Index participations only if they result in titles
- Repurchase agreements or Repos on titles
- Participations in companies; Russian OOO and ZAO, US LLC provided that their profits are subject to taxes, Romanian SA and SRL and Bulgarian AD and OOD.
- Units in open-end or closed-end collective investment schemes that have been incorporated, registered and operate in accordance with the provisions of the relevant legislation of the incorporated country

Examples of such units are:

- Investment trusts, investment funds, mutual funds, unit trusts, real estate investment trusts
- International collective investment schemes - ICIS
- Undertakings for collective investments in transferable securities or UCITS

- Other similar financial institutions

The circular applies for tax years 2003 onwards. Cases that have already been settled shall not be re-examined. It is important to note that the circular states that tax returns submitted before the date of issue of the circular and which are not under objection will not be revised with regards to the tax treatment of titles as defined in the circular.

In cases where it is not certain whether a specific financial instrument falls under any of the above mentioned categories, a request for a ruling should be submitted to the Commissioner of Income tax.

### **Promissory notes – Not Titles**

Crucial to mention at this stage that promissory notes are NOT titles according to Cyprus tax law and any profit from the sale of promissory notes increases the taxable income of the company and on any resulting net profit of the company there will be 12.5% corporation tax.

For any *interest* received from the sale of promissory notes the considerations indicated above as to the ordinary or closely connected to the ordinary activities of the company apply. The taxation of the interest due or received is subject to the above classification.

### **c) Dividends**

Income in the form of dividends is exempted from corporation tax. There is also exemption as to Special Defence Contribution Tax under certain conditions explained below.

In effect the taxation on dividends is as follows:-

- **Income Tax – FULL EXEMPTION**

Dividends received from Cyprus companies (either resident or non-resident) or dividends received from overseas companies (foreign) do **not bear** any corporation tax.

- **Special Defence Contribution Tax**

1. Dividends received from another Cyprus resident company:

There is no Special Defence Contribution Tax in this case.

Any dividend paid from a Cyprus company indirectly after four years from the end of the financial year in which the profits that generate the relevant dividend were recognised, will not be exempt.

The Law provides for the deemed distribution of dividends every two years in case of tax resident shareholders. It further provides that these provisions however do not affect companies whose beneficial owner either directly or indirectly is not a resident of Cyprus.

It should be noted that the above will not apply in cases where the shareholders of the company are non-residents of Cyprus whether directly or indirectly.

2. Dividends received from a non-resident company:

Such dividend is exempt from Special Defence Contribution Tax. However, this **exception is not granted if**

(a) the company paying the dividend is engaged directly or indirectly by more than 50% in activities which result in investment income

**AND**

(b) the rate of the foreign taxation on the income of the company paying the dividend is substantially lower than the 12.5% payable by the recipient Cyprus resident company.

If the exception does not apply, the dividend income received from the non-resident company is taxed at the rate of 20%. After the 1<sup>st</sup> January 2014, the rate will be reduced to 17%.

If on any dividend income any foreign tax was paid, then unilateral tax credit is granted in Cyprus as explained in the preceding paragraph.

### **c) Royalty Income**

An 80% of "Royalty Profit" generated from any type of intellectual property right, patents and trademarks is exempt from corporation tax. The remaining 20% is subject to the normal corporation tax rate of 12.5%.

For the purpose of determining the "Royalty Profit" the law allows the deduction from the resulting royalty income of all expenses incurred wholly and exclusively for the production of royalty income.

It is important to stress that the favorable tax treatment also covers the profit from any future sale of the IP Right. This allows the owners of the IP Rights not only to enjoy tax benefits on the income generated from the use of such right but also provides for a tax efficient exit route in the future.

In addition to the above, the Cyprus Company holding the IP Rights is able to write off the capital expenditure made on the acquisition or development of such rights in the first five years of use. The company is able to receive capital allowances of 20% straight line starting from the first year of the use of the asset as well as the subsequent four years of usage. These capital allowances are considered of course tax deductible, which makes the tax benefits of the first five years for the Cyprus Royalty Company even more attractive.

### **III. Allowable Deductions to the income**

All expenses wholly and exclusively incurred for the production of the income are deductible, including:

- Expenses for repair of premises, plant, machinery and means of transport;
- Contributions to pension, provident and other insurance funds;
- Bad debts written off and provisions for doubtful debts, subject to conditions;

- Expenditures of a non – capital nature for specific research;
- Expenditures of a non-capital nature on patents or patent rights or royalties;
- Donations to approved charities;
- Any amount of interest in relation to the acquisition of business assets.

**The following are non – deductible expenses**

- Corporation tax and defence contribution;
- Any payments of a voluntary nature;
- Expenses for business entertainment up to EURO17.100 or 1% of the gross business income, whichever is the lower;
- Expenses in respect of private motor vehicles and interest applicable to their purchase costs.

IV. Allowable Tax Losses

Tax Losses can be carried forward for up to five years and can be set off against future profits.

V. Group relief

Group relief (set off of the loss of one company with the profit of another) is allowed provided both companies of the group are tax residents of Cyprus.

However, the requirement of the Income Tax Law that both companies must be tax residents of Cyprus in order to apply group relief, might be in conflict with the EU Law according to the decision of the European Court of Justice (ECJ), in the court case of MARKS & SPENCER PLC against the UK Inspector of Taxes where it approved that group relief within Member States is possible.

According to this judgement, foreign subsidiaries may transfer losses back to their parent company if the losses cannot be used for tax purposes in the country where they were made.

Two companies are deemed to be members of a group if: -

- One company is the 75% subsidiary of the other or,
- Both are 75% subsidiary of a third company.

A 75% subsidiary means a company whose holding company possesses either directly or indirectly at least 75% of its voting shares and beneficially entitled directly or indirectly to at least 75% of the income and 75% of the assets in case of winding up.

Group relief is available only when both companies belong to the same group for the whole financial year. A company incorporated by its mother company any time during a tax year will be considered as part of the group from the beginning of the year for group relief purposes. Losses incurred in one year can be set off only against profits of the same year.

A partnership transferring business into a company can carry forward tax losses into the company for future utilisation.

#### VI. Mergers, reorganisations, de-mergers of companies

Any profits or gains made by reason of reorganisations, the transfer of property, and the transfer of shares in exchange for shares in another company are exempt from income tax.

Reorganizations include merger, de-merger, transfer of assets and exchange of shares between resident and / or non – resident companies in Cyprus.

- **A merger is:**

- One or more companies at their dissolution without liquidation, transfer their total net assets and liabilities to a pre – existing company in exchange for shares granted to their shareholders and possibly with cash consideration, not exceeding 10% of the nominal value of the shares, or in the absence of nominal value the accounting value of the shares.

- Two or more companies transfer at dissolution without liquidation, their total net assets and liabilities to a new company they incorporate in exchange for shares granted to their shareholders and possibly with cash consideration not exceeding 10% of the nominal value of the shares, or in the absence of nominal value the accounting value of the shares.
- A company transfers at dissolution without liquidation, its total net assets and liabilities to its 100% holding company.
- **A de - merger is:**
  - A company at dissolution without liquidation, transfers its total net assets and liabilities to two or more existing or new companies in exchange for shares granted to its own shareholders and possibly with cash consideration not exceeding 10% of the nominal value of the shares or in the absence of nominal value the accounting value of the shares.
- **A transfer of net assets** takes place when a company at its dissolution without liquidation, transfers the whole or one or more of its divisions / activities to another company in exchange for shares in the capital of the recipient company.
- **Exchange of shares** means an act by which a company (first company) acquires controlling participation in the capital of another company (second company) in exchange for shares of the first company, granted to the shareholders of the second company, and possibly with cash consideration not exceeding 10% of the nominal value of the shares or in the absence of nominal values the accounting value of the shares.

## **D. TAXATION OF SPECIAL CATEGORIES OF COMPANIES – LEGAL BODIES - TRUSTS**

### I. Ship Owning Companies, Charterers and Ship Management companies

Eligible Cyprus ship owning companies, charterers and ship management companies, once they meet the requirements of the Merchant Shipping (Fees and Taxing Provisions) Law 44(I) of 2010, may pay only Tonnage Tax according to the provisions of the relevant Law.

In such a case eligible Cyprus ship owning companies, charterers and ship management companies are fully exempted (0%) from any taxation on:

- Profits from Shipping Operations;
- Dividends paid directly or indirectly out of such profits or from the Sale of a ship;
- Interest earned on funds used as Working Capital or for the Financing, Operation or Maintenance of the Ship;
- Profits from Sale of a Ship or the Ship-owner Company Shares.

Also remuneration of a Cyprus Ship Crew is Tax Exempt.

Eligible Ship-owners of Cyprus ships by default enter into the Tonnage Tax System contrary to eligible Ship-owners of EU and Non-EU Ships, Charterers and Ship managers, who may enter the Cyprus Corporate Tax System but once they elect to be taxed according to the Tonnage Tax System then they must remain in the Tonnage Tax System for 10 Years.

Cyprus ship owning companies, Charterers and Ship Management companies once they do not meet the requirements of the Merchant Shipping (Fees and Taxing Provisions) Law 44(I) of 2010, to be taxed according to the favourable Tonnage Tax System or if they meet them but elect not to follow it, they pay taxation according to the general provisions of the Income Tax Laws or any other taxation law.

## II. Taxation of Partnerships

A partnership is not a legal entity. It does not have legal personality and in this respect is not taxable as an entity. The partners who establish the partnership are those to be taxed for the profits of the partnership. If they are residents in Cyprus, they are taxable according to the regular rates. If they are not residents, no tax shall be levied in Cyprus on the distribution of profits to the partners of such partnership.

## III. Taxation of Collective Investments schemes – Mutual Funds – International Collective Investment Schemes

Beneficial tax provisions are in place for such type of legal bodies.

Generally they will be subject to taxation in Cyprus at the regular rates, applicable to tax resident companies – 12.5% on their net profits.

It is important to mention that according to the law, there is full exemption on the taxation of profits from the sale of titles i.e. shares, etc.

Since such type of legal bodies are mainly engaged in the trading of titles, there is no tax on profits from these operations. In effect, their taxation has been reduced to 0%.

In addition to the above, these types of legal bodies enjoy other tax benefits such as:

- Interest income received by such legal bodies will only be subject to Income tax as trading income and not as interest income and such income is specifically exempted from Special Defence Contribution Tax;
- The holder of a unit in such legal bodies is classified as shareholder;
- Profits on disposal of units or other ownership interests in such legal bodies are specifically exempted from Income tax as they are regarded as “titles”;

- Deemed dividend distribution to Cyprus tax residents due to their holding interest in such legal bodies is taxed under Special Defence Contribution Tax at 3% only instead of 20% which is the normal rate for companies' Cyprus resident shareholders. Deemed dividend distribution provisions are not applicable to non Cyprus tax residents;
- Redemption of a Unit or other interest in such legal bodies is not considered as reduction of capital and in such a case the amount received by the unit holder is not liable to Special Defence Contribution Tax ;
- In case of dissolution of such legal bodies profits of the last 5 years not distributed to Cyprus resident shareholders will be taxed with Special Defence Contribution Tax 3% instead of the 20% applicable standard rate in case of companies. Non Cyprus tax residents are exempted from this taxation altogether.

#### IV. Taxation of International Cyprus Trusts

The new law has not affected the taxation of the income of international trusts belonging to non-resident persons. The International Trust Law (Law no. 69/92) as amended specifically provides in section 12 that *"the income and gains of an international trust derived or deemed to be derived from sources within or outside the Republic shall be subject to all taxes imposed in the Republic in case the beneficiary of the trust is a resident of the Republic"*

In the case where a beneficiary is NOT a Cyprus resident, income and profits of a Cyprus International Trust which are gained or deemed to be gained from sources outside the Republic are exempt from taxes imposed in the Republic.

If however the income and profits of a Cyprus International Trust which are gained or deemed to be gained from sources within the Republic are subject to such taxation which is imposed in the Republic irrespective of the fact that the beneficiary is not a Cyprus resident.

## E. WITHHOLDING TAXES

### I. Withholding taxes on Dividends, Interest and Royalties

- There are no withholding taxes on payments to non – residents in respect of dividends and interest. There are also no withholding taxes on royalties arising from sources outside Cyprus. Royalties arising from the use of an asset in Cyprus are subject to 10% withholding tax.
- Rentals on films shown in Cyprus are subject to 5% withholding tax.
- Income of non tax resident professionals, entertainers and athletes from activities in Cyprus is subject to a 15% withholding tax

## F. SPECIAL DEFENCE CONTRIBUTION TAX

Special Defence Contribution Tax is imposed **only** on income earned by Cypriot tax residents. Non-tax residents of Cyprus are exempted from this taxation.

The following apply in addition to the above main rule:

- Dividends received by a Cyprus tax resident company as explained above under certain conditions and dividends paid to non tax residents are not subject to special defence contribution tax;
- There is a 30% special defence contribution tax on certain types of interest income subject to double taxation treaties and unilateral tax credit, as will be explained below;
- There is a 20% Special Defence Contribution tax on dividend income received by tax resident **individuals**. (From 1st January 2014 the rate will be reduced to 17%)
- There is 3% Special Defence Contribution tax on rents which is imposed on the gross rental income reduced by 25%

- Other special provisions are in force for particular items of income, but are outside the scope of this report as they do not affect non tax residents.

## **G. SPECIFIC MATTERS RELATING TO TAXATION**

### **Double taxation treaties – Unilateral tax credit relief**

#### I. Double tax treaties

The Double taxation treaties that Cyprus has signed apply in full and resident companies may use their provisions and claim the relevant benefits. Tax credit is available according to the provisions of each particular treaty. The law adopts the credit method for the avoidance of double taxation.

The Law contains extensive provisions dealing with the methodology and the procedure to be followed in case credit will be granted to a person liable to taxation in Cyprus.

#### II. Unilateral tax credit relief

Apart from the tax credit under any relevant double tax treaties there is as well unilateral tax credit relief which is now available in respect of any foreign tax paid by the company, in any foreign country with which Cyprus does not have a Double Tax Treaty. Both the credit under the relevant double tax treaties, as well as the unilateral tax credit, will equally apply in respect of corporation tax and / or to special defence contribution tax.

It follows that, if a company receives any income or dividends which under the new tax regime might be taxable in Cyprus or if it earns any interest from abroad, any rentals from outside Cyprus or otherwise and if on any such type of income it pays any tax outside Cyprus the amount of such tax paid shall be deducted from any Cyprus tax which would have otherwise been payable on such type of income.

## H. SUMMARY OF THE PROVISIONS OF THE TAX LEGISLATION ON COMPANIES

- There is no distinction between local companies and offshore companies. Companies for Tax purposes will be identified as tax resident and non tax resident.
- A Company, irrespectively of where it is registered, is taxed only if it is a tax resident of Cyprus. A Company is considered as tax resident of Cyprus if its management and control is in Cyprus.
- A non tax resident company is not subject to any tax in Cyprus on any income derived from sources outside Cyprus (0%), but is taxed on its profits arising from within Cyprus.
- The taxable net profits of all tax resident companies (i.e. having their management and control in Cyprus) whether incorporated in Cyprus or not, will be liable to corporation tax at the rate of 0% - 12.5%, depending on the type of income.
- There is no tax (0%) on profits from the sale of titles i.e. shares, bonds, debentures, founders' shares and other titles of companies or other legal persons, incorporated in Cyprus or abroad and options thereon.
- There is no **corporation tax** (0%) on dividends received by a tax resident company. There are also very wide exemption criteria from Special Defence Contribution Tax for such dividend income.
- Royalty Profits receive an 80% tax exemption and can enjoy significant capital allowances deductions
- There is no tax (0%) on profits from a permanent establishment abroad (under certain conditions).
- Passive Interest Income as is taxed only under Special Defence Contribution Tax at 30%.

- Trading Interest Income is taxed only under corporation tax at 12.5%.
- There is no withholding tax (0%) on payments to its non tax resident shareholders in respect of dividends, or interest or royalties arising from sources outside Cyprus. Royalties from the use of an asset in Cyprus are subject to 10% withholding tax.
- Tax losses can be carried forward for five years and can be set-off against future profits.
- Group relief is allowed. Tax losses of one company in the same group are set-off against the profits of another company of the group in the same tax year.
- Reorganizations (mergers, de-mergers, transfer of assets and exchange of shares) are exempt from income tax (0%).
- Eligible Cyprus ship owning companies, charterers and ship management companies, once they meet the requirements of the Merchant Shipping (Fees and Taxing Provisions) Law 44(I) of 2010, may pay only Tonnage Tax according to the provisions of the relevant Law.

In such a case eligible Cyprus ship owning companies, charterers and ship management companies are fully exempted (0%) from any taxation on:

- Profits from Shipping Operations;
- Dividends paid Directly or Indirectly out of such profits or from the Sale of a ship;
- Interest earned on funds used as Working Capital or for the Financing, Operation or Maintenance of the Ship;
- Profits from Sale of a Ship or the Ship-owner Company Shares.

Also remuneration of a Cyprus Ship Crew is tax exempt.

- Eligible Ship-owners of Cyprus ships by default enter into the Tonnage Tax System contrary to eligible Ship-owners of EU and Non-EU Ships, Charterers and Ship managers, who may enter the Cyprus Corporate Tax System but once they elect to be taxed

according to the Tonnage Tax System then they must remain in the Tonnage Tax System for 10 Years.

- Double tax treaties signed, continue to apply to tax resident companies, which may invoke their provisions and be benefited accordingly.
  
- Unilateral tax credit relief is granted. Any amount of tax paid for any income taxable in Cyprus, in any foreign country, irrespective of whether a double taxation treaty has been signed or not, is given as a tax credit in Cyprus and the tax due in Cyprus is reduced accordingly.

## **I. CONCLUSION**

The tax legislation of Cyprus has been designed to balance the future competitiveness of Cyprus as an International Business Centre and its commitments towards the European Union.

The result created a European jurisdiction where advantageous tax planning structures can be achieved.

The Cyprus Company has the lowest taxation in Europe and at the same time has acquired the European "*stamp of respectability*". Compared to other offshore jurisdictions which have unstable future, that are or will be under attack unless they affect structural changes in their systems, Cyprus has made the move and the final result is here, known and now in practice.

The Cyprus Company, with its European diversion and acceptability opens the gates to Europe for those valuing respect.

## **J. DISCLAIMER**

This publication has been prepared as a general guide and for information purposes only. It is not a substitution for professional advice. One must not rely on it without receiving independent advice based on the particular facts of his/her own case. No responsibility can be accepted by the authors or the publishers for any loss occasioned by acting or refraining from acting on the basis of this publication.

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**K. COMPARATIVE TABLE ON TAXATION RATES AND OTHER RELEVANT MATTERS AS TO TAX AND NON TAX RESIDENT CYPRUS COMPANIES**

<b>Type of income and type of taxation</b>	<b>Tax Resident Companies (Management and Control in Cyprus)</b>	<b>Non Tax resident Companies (Management and Control outside Cyprus)</b>
Corporation tax on net profits	12.5%.	0% (unless they have income from within Cyprus then are taxed only for that income with normal rates).
Profits of a permanent establishment abroad	0% - on conditions.	0%
Profits from sales of shares (titles)	0%	0%
Corporation tax on Dividends received from a tax resident/Cyprus company	0%	0%
Corporation tax on Dividends received from a non tax resident/foreign company	0%	0%



<b>Type of income and type of taxation</b>	<b>Tax Resident Companies (Management and Control in Cyprus)</b>	<b>Non Tax resident Companies (Management and Control outside Cyprus)</b>
Special defence Contribution on dividends paid from one tax resident Cyprus company to another tax resident Cyprus company	0% (some conditions may apply)	0%
Special defence contribution on dividends paid from non tax resident company to Cyprus resident company	0% The exemption is not granted if the income of the non tax resident company paying the dividend is more than 50% as investment income <b>AND</b> the foreign tax rate payable for the income of the company paying the dividend is substantially lower than 12.5%. If the exemption is not granted then the dividend income is taxed at the rate of 17%	0%
Royalty Income	80% exemption so that the maximum effective rate of corporation tax is 2.5%	0%
Interest Income	Passive Interest : 30% as Special Defence Contribution tax.  Trading Interest: 12.5% as Corporation Tax.	0%



<b>Type of income and type of taxation</b>	<b>Tax Resident Companies (Management and Control in Cyprus)</b>	<b>Non Tax resident Companies (Management and Control outside Cyprus)</b>
Withholding taxes on dividends or interests payable to non tax resident persons or companies	0%	0%
Withholding Taxes on Royalties	0% if arising from sources outside Cyprus – if arising from the use of assets situated in Cyprus then there is 10% withholding tax	0%
Ship owning companies	Only Tonnage Tax once they meet certain conditions otherwise normal rates	0%
Charterers	Only Tonnage Tax once they meet certain conditions otherwise normal rates	0%
Ship management companies	Only Tonnage Tax once they meet certain conditions otherwise normal rates	0%
Cyprus International Trusts.	0%	Not applicable (Not possible to set up an International Cyprus Trust without a resident Cypriot trustee)
Collective investment Schemes – Mutual Funds	Normal rates BUT special provisions apply for various items- see above.	0%
Partnerships	0%. Partners are taxed	0%
For Reorganizations (mergers, de-mergers, transfer of assets and exchange of shares)	0%	0%



<b>Type of income and type of taxation</b>	<b>Tax Resident Companies (Management and Control in Cyprus)</b>	<b>Non Tax resident Companies (Management and Control outside Cyprus)</b>
Tax Losses	Can be carried forward for five years and can be set off against future profits	Not applicable
Group relief	Group relief is possible, i.e. the loss of one company is set off against the profits of another in the same group in the same tax year.	Not applicable
Double Tax Treaties	Apply	Do not apply. Benefits can not be claimed
Tax Credit	As provided in Double Taxation Treaties.  Also Unilateral Tax credit for non-treaty countries is granted. Any Tax paid to the foreign country is applied as Tax Credit	Not applicable. Benefits of Double Tax Treaties can not be claimed

## Our Firm

**Kinanis LLC**, a law and consulting firm, is one of the leading and largest business law firms in Cyprus and advises for over 30 years the international investor and private clients on all aspects of law, tax and accounting.

Kinanis LLC absorbed the business of its shareholders which are in the legal and consulting profession since 1983, with local and international dimensions.

Experience and practice over the years brought forward the need for transformation from a traditional law firm to a more innovative multidisciplinary firm providing a full range of services combining law and accounting with the extensive expertise in corporate and tax advice to ensure that our clients will obtain the best possible spherical advice adopting the principle as to the services offered "All in one place", so that the client will find a quick, correct and efficient solution to its daily legal, accounting and tax issues in a trustworthy environment.

This combination of legal, accounting and tax services through our well qualified personnel and our involvement and participation in international transactions over the years, have established our firm as one of the key players in the field. Our involvement in international financial transactions has also provided us with the extensive expertise in representing groups, corporations, funds as well as the private client.

The firm is staffed with around 80 young, energetic and ambitious professionals, including lawyers, accountants and administrators who provide prompt, efficient and high quality services and who are capable of meeting the current demanding challenges of the local and international business environment.

We always look to give solutions in a simple and as possible quick way focusing on the needs of each client trying to anticipate the issues before becoming a problem.

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