

## Corporate Tax - Cyprus

### Tax regime: an overview

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The Cyprus taxation system was thoroughly overhauled in 2002 in preparation for EU membership. As a result, Cyprus benefits from a simple, modern tax system that is fully compliant with the requirements of the Organisation for Economic Cooperation and Development (OECD) and the EU. In a recent survey of tax professionals, Cyprus emerged as the most attractive tax regime in Europe on account of its combination of consistency in interpreting tax legislation, stability in resisting frequent changes to tax laws and comparatively low tax rate.

### Basis of taxation

The tax year for individuals and companies is the calendar year. Liability to Cyprus tax in any year of assessment is based on residence. For individuals, residence is determined by physical presence; for companies, it is determined by the locus of management and control.

### Income tax

#### *Individuals*

##### *Liability for tax*

Cyprus residents are taxed on the basis of worldwide income, irrespective of whether the income is remitted to Cyprus. Spouses are taxed separately.

Persons who are not resident in Cyprus are subject to income tax on income accruing or arising from sources in Cyprus in respect of:

- profits or other benefits from a permanent establishment situated in Cyprus or from any office or employment exercised in Cyprus;
- pensions in respect of past employment exercised in Cyprus;
- rent from property situated in Cyprus;
- consideration in respect of goodwill of a trade in Cyprus reduced by the cost of such goodwill; and
- the gross income derived by an individual from the exercise in Cyprus of any profession or vocation, the remuneration of public entertainers and the gross receipts of any theatrical, musical or other group of public entertainers.

Individuals are considered to be resident if they are present in Cyprus for more than 183 days in the relevant year. Days of departure and arrival are treated as follows:

- The day of departure from Cyprus counts as a day of residence outside Cyprus.

- The day of arrival in Cyprus counts as a day of residence in Cyprus.
- Arrival in and departure from Cyprus in the same day counts as one day's residence in Cyprus.
- Departure from and return to Cyprus in the same day counts as one day of residence outside Cyprus.

#### *Rates of tax*

Personal income tax rates are set out in the following table:

Income band	Tax rate
Below €19,500	0%
€19,500 to €28,000	20%
€28,000 to €36,300	25%
€36,300 to €60,000	30%
Above €60,000	35%

#### *Allowances and reliefs*

Relief is given for donations to approved charities, professional and trade union subscriptions, life insurance premiums and contributions to pension, social insurance and welfare funds. Relief may also be available under a [double tax treaty](#).

For the first three calendar years following the start of their employment, individuals taking up residence and employment in Cyprus will be entitled to an annual allowance of the lower of €8,550 or 20% of their remuneration. Alternatively, if income from employment exceeds €100,000 per annum, a 50% deduction is allowed for the first five years of employment.

A 20% deduction is allowed from rental income received to cover expenses. The full amount of interest paid on loans for the acquisition of the let property is also allowed as a deduction.

Subject to certain conditions, expenditure on maintaining buildings that are subject to a preservation order may also be deductible.

Annual writing-down allowances are available against plant, machinery and other assets used in a trade or profession.

#### *Expenditure disallowed for tax purposes*

The following are not tax deductible:

- contributions to the [Social Cohesion Fund](#);
- private motor vehicle expenses;
- immovable property tax;
- interest paid in respect of the acquisition of non-business assets or of private motor vehicles (even if used for business purposes); and
- business entertainment costs in excess of the lower of €17,086 or 1% of gross income.

#### *Relief for losses*

Losses incurred in a trade or profession may be offset against other income and any unrelieved balance may be carried forward for relief against income of future years for a maximum of five years. If the business is subsequently converted into a limited liability company, any unrelieved losses may be used by the company.

#### *Exemptions and special cases*

The following exemptions are available:

- interest and dividends;
- lump sums received on retirement or commutation of pension or as a result of bodily injury or death;
- capital sums from approved life assurance policies and provident or pension funds;
- income from employment services provided abroad to a non-resident employer or an overseas permanent establishment of a resident employer for a period exceeding 90 days in the tax year;
- profit from the sale of shares (if the shares are of an unlisted company owning real estate in Cyprus, the gain may be subject to [capital gains tax](#));
- certain pensions, such as widow's pension;
- salaries of officers and crew of ships owned by a Cyprus shipping company that sail under the Cyprus flag and operate in international waters; and

- income from a qualifying scholarship, exhibition, bursary or similar educational endowment.

There is a separate, highly favourable **tonnage tax system** for international shipping and ship management activities.

Foreign pensions may be taxed either on the normal basis described above or on an alternative basis, under which the first €3,420 per annum of the foreign pension is free of tax and the excess over that amount is taxed at 5%. At current rates, the alternative basis results in a reduced tax liability on pensions above €24,860. The taxpayer may choose which basis to adopt in any particular year. Income from interest, dividends and rents is subject to a special defence contribution (SDC) which is described below.

#### *Payment of tax*

A self-assessment system is in place. Individuals must submit a provisional tax return for the year, accompanied by a remittance for half the estimated tax liability, by no later than July 31 each year. The taxpayer may amend the provisional return at any time during the tax year. The remaining balance must be paid by December 31. Taxpayers whose gross income from a trade or profession is less than €70,000 and who are consequently exempt from the requirement to submit audited financial statements to support their tax return must submit their final tax return, accompanied by a remittance for any tax due, within six months of the end of the tax year. Taxpayers whose gross income from a trade or profession exceeds €70,000 must submit audited financial statements to support their tax return. They must pay their final tax liability no later than August 1 following the end of the tax year and submit a final tax return no later than the following December 31.

Relief or credit may be available under a double tax treaty for tax paid abroad. Where no double tax treaty is in place, the Cyprus tax authorities normally allow unilateral relief for foreign tax paid.

#### **Companies**

The Income Tax Law of 2002 completely changed the system of company taxation and abolished the separate taxation system that had previously been available to international business companies (ie, companies incorporated in Cyprus owned by non-Cypriots and trading exclusively outside Cyprus). There is now:

- a single corporation tax rate of 12.5% for all companies resident in Cyprus;
- no geographical limitation on the exercise of a company's activities – income may be derived from any source, including Cyprus; and
- no restriction on the ownership of a company's shares.

#### *Liability for tax*

Liability to corporate income tax is based on residence. Cyprus-resident companies are liable to tax on worldwide income and non-resident companies are liable to tax on any Cyprus-source income.

For companies, the test for residence is the locus of management and control. A company is regarded as resident in Cyprus if it is managed and controlled in Cyprus. Mere registration or incorporation in Cyprus is not enough to render a company liable to tax in Cyprus. A majority of resident directors on the board establishes a *prima facie* rebuttable presumption of management and control being exercised in Cyprus.

The criteria for management and control have not been formally defined, but the following are generally accepted as the key factors determining whether the management and control of a company are exercised in Cyprus:

- Are a majority of the directors resident in Cyprus?
- Are all strategic decisions affecting the company demonstrably made in Cyprus by the board of directors?
- Does the company maintain its headquarters in Cyprus?
- Does the company operate an account with a bank in Cyprus?

A company should have economic substance in terms of staff, premises and equipment, and sufficient competence in Cyprus to make necessary business decisions. Finally, it should provide a service that is genuinely required by the group and not be devoid of an economic purpose. Otherwise, payment for such services could be viewed as an artificial transfer of profits from one company to another.

Cyprus branches of foreign companies are subject to tax on worldwide income if the locus of management and control of the branch is in Cyprus. If the locus of management and control is overseas, the branch is liable to corporation tax on profits accruing or arising in Cyprus.

Cyprus legislation defines a 'permanent establishment' in the same way as the OECD Model Tax Convention.

#### *Taxable income*

A company resident in Cyprus is taxable on its worldwide income derived or accruing from:

- gains or profits from any trade or business;

- interest earned in or closely related to the normal activities of the business;
- rents, royalties, premiums or other profits arising from property; and
- any other income (eg, a gain on sale of goodwill).

#### *Expenditure disallowed for tax purposes*

All expenses wholly and exclusively incurred for the production of the relevant income are deductible, with the following exceptions:

- private motor vehicle expenses;
- immovable property tax;
- interest paid in respect of the acquisition of non-business assets (with certain exceptions in relation to the acquisition of a 100% subsidiary) or of private motor vehicles (even if used for business purposes); and
- business entertainment costs in excess of the lower of €17,086 or 1% of gross income.

Where the income consists of both taxable and non-taxable income, expenses directly incurred in earning the non-taxable income are not allowed and indirect expenses are apportioned on the basis of the income earned.

#### *Rate of tax*

Tax is charged at 12.5% on the profits of a company's business and gains on trading in immovable property in Cyprus.

#### *Loss relief*

Trading losses may be offset against other income and any unrelieved balance may be carried forward for relief against income of future years for a maximum of five years.

For members of a group of companies, trading losses incurred by one group company may be offset against trading profits of another group company by way of group relief, provided that the losses and profits were accrued in the same year of assessment and both companies were resident in Cyprus and members of the same group for the whole of the tax year concerned. A subsidiary that is formed during a tax year (as opposed to an existing company that is acquired) is treated as being a member of the group for the whole tax year.

Two companies are deemed to be members of a group if one is the 75% subsidiary of the other or both are 75% subsidiaries of a third company. A '75% subsidiary' means holding at least 75% of the voting shares with beneficial entitlement to at least 75% of the income and 75% of the assets on liquidation.

#### *Exemptions and special cases*

The following exemptions are available:

- profit from the sale of securities;
- dividends;
- income of any company formed exclusively for the purpose of promoting art, science or sport and of certain educational and charitable companies;
- income of any approved pension or provident fund; and
- profits from a permanent establishment situated entirely outside Cyprus, unless the permanent establishment directly or indirectly engages more than 50% in activities which lead to investment income and the foreign tax burden is substantially lower than the tax burden in Cyprus.

Interest other than interest earned in or closely related to the normal activities of the business is not subject to corporate income tax, but is instead subject to SDC tax (currently 30%).

Royalties or any other payments to a non-resident for intellectual or industrial property rights are liable to a 10% withholding tax, subject to relief under any applicable double tax treaty. No tax need be withheld if the rights are used exclusively outside Cyprus.

Rental payments made to a person not resident in Cyprus in respect of films shown in Cyprus are subject to withholding tax at 5% of the gross amount.

There is a separate, highly favourable tonnage tax system for international shipping and ship management activities.

#### *Reorganisations*

Transfers of assets and liabilities can be made without giving rise to a tax liability within the framework of a reorganisation (including mergers, demergers, partial divisions, share exchanges and transfers of seat), and any tax losses can be carried forward by the receiving entity.

#### *Payment of tax*

No later than July 31 each year, companies must submit a provisional tax return for the year, accompanied by a remittance for half the estimated tax liability. The remaining balance must be paid by December 31. The final tax liability must be paid no later than August 1 following the end of the tax year and a final tax return must be submitted no later than the following December 31.

Relief or credit may be available under a double tax treaty for tax paid abroad. Where no double tax treaty is in place, the Cyprus tax authorities normally allow unilateral relief for foreign tax paid.

### Social insurance

Under the Social Insurance Scheme, the employer and employee each contribute 7.8% of the employee's earnings up to a current maximum of €4,533 per month (adjusted annually in line with inflation) – a total of 15.6%. The government pays a further 4.3%, making an aggregate of 19.9%.

A self-employed person contributes 14.6% on income within a lower and upper earnings threshold that varies according to the nature of the trade. The amount of the contributions is subject to a lower and a maximum limit, depending on the trade or profession.

Employers must also pay 1.7% of their employees' earnings up to a maximum of €4,533 per month to the Industrial Training Fund and Redundancy Fund and 2% (with no upper earnings limit) to the Social Cohesion Fund, which is used to make social grants.

Contribution rates are reviewed at five-year intervals, with the next scheduled review due to take place in 2019.

### Special contribution by private sector employees, pensioners and self-employed

With effect from January 1 2012, a special contribution has been levied on remuneration and pensions paid to private sector employees. The special contribution was originally intended to be limited to two years, but was extended for a further three years until the end of 2016. In the case of an employee, the special contribution is borne by the employer and the employee in equal shares. The rates are set out in the following table:

Monthly remuneration	Special contribution
€0 - €1,500	0%
€1,501 - €2,500	2.5%
€2,501 - €3,500	3.0%
€3,501 and above	3.5%

### Special defence contribution

Special defence contribution (SDC) tax is payable by Cyprus-resident (determined in the same way as for income tax) individuals and companies on interest, dividend and rents received at rates set out in the following table:

Nature of income	Rate
Dividends	17%
Interest	30%
Rents	3% on the rent, discounted by 25%

#### Dividends

Dividends received by a resident company (or a permanent establishment of a non-resident company) from overseas are exempt from SDC tax in accordance with the EU Parent-Subsidiary Directive and domestic law. The only limitation to the exemption for overseas dividends is where:

- the investment income is more than 50% of the paying company's activities; and
- the foreign tax burden on the income of the paying company is substantially lower than the Cyprus tax burden.

Dividends received by one resident company from another are exempt from SDC tax. Dividends received by a foreign shareholder (individual or company) from a resident company are also exempt. This gives Cyprus a real advantage over other European holding company regimes, which generally impose a withholding tax – even when reduced by a double tax treaty – of at least 5% or make the exemption from withholding tax subject to meeting prescribed conditions.

Cypriot companies are generally required to withhold SDC at source from dividends paid and account for it to the tax authorities. Dividends paid to non-resident shareholders (whether directly or indirectly) are not subject to this requirement, subject to the company submitting a confirmation from its auditors or lawyers of the non-resident shareholders.

### *Interest*

Interest received in or closely related to the normal course of business is exempt from SDC tax. Other interest is subject to SDC tax at 30% on the whole amount received, with no deduction for the costs of earning the interest.

### *Rent*

Rent is subject to SDC tax at 3% on 75% of the gross rent, giving an effective rate of 2.25%. No deduction for expenses is allowed.

### *Deemed dividend distribution*

If a Cyprus-resident company does not distribute a dividend within two years of the end of a tax year, a 'deemed dividend distribution' is calculated, which is 70% of post-tax profits for that tax year, reduced by any dividends that have been paid out of those profits. SDC tax is charged only on the proportion of the deemed dividend distribution that is applicable to Cyprus-resident shareholders.

When an actual dividend is paid after the deemed dividend distribution, SDC tax is payable only on any dividend paid over and above the deemed dividend distribution.

Companies are generally required to submit an annual return on Form IR 623 for the purpose of calculating deemed dividends. Where the entire share capital of a Cyprus-resident company is ultimately owned by non-residents, the directors of the company may make a declaration to this effect, have it certified by the company's auditors or lawyers and forward it to the tax authorities. When the declaration has been accepted by the tax authorities, the company will no longer be required to make returns for deemed distribution purposes.

If part of the share capital is ultimately owned by Cyprus residents, an annual return must still be submitted, but the profits ultimately attributable to non-resident shareholders will be excluded.

### *Payment of SDC tax*

Any person or company paying a dividend or interest is required to deduct SDC tax and pay the SDC tax to the Inland Revenue department with a statement of tax deducted. SDC tax on deemed distributions must be paid within two years and one month of the end of the accounting year.

Companies, partnerships and national or local government bodies which pay rent to Cyprus-resident landlords are required to deduct SDC tax from rent payments and remit it to the tax authorities. The amount to be deducted and paid over to the tax authorities is 3% of 75% (ie, 2.25%) of the gross rental amount.

On June 30 and December 31 each year, the tenant must provide the landlord with a statement of tax withheld during the previous six months. Tenants must also submit a list of the landlords from which SDC was withheld with their annual tax return.

Persons or companies receiving rents are responsible for ensuring that the amount of SDC withheld is correct. They must pay any further SDC due (eg, in the event of under-deduction or on rents paid by individuals) by self-assessment on June 30 and December 31.

There is no requirement to withhold and account for SDC tax on rents paid to non-residents, subject to the landlord providing the tenant with the necessary confirmation of non-residence.

Relief or credit against SDC tax will be allowed in respect of any foreign tax paid, either under a double taxation treaty or by way of unilateral relief.

### **Capital gains tax**

Subject to certain exemptions and reliefs, net gains from the disposal of immovable property in Cyprus and of shares of unlisted companies owning immovable property in Cyprus are taxable at 20%. All other gains are exempt.

The following categories of disposals of real estate are exempt from capital gains tax:

- transfers by reason of death;
- gifts between relatives up to the third degree of kinship;
- gifts to family companies (limited companies whose only shareholders at the time of the gift and for the entire period of five years thereafter are members of the family of the donor);
- gifts by family companies to their shareholders, but only in cases where the property given was originally acquired by the company as a gift;
- gifts to charitable institutions or to the state;
- exchanges of immovable properties; and
- compulsory acquisitions.

In assessing the gain, the following will be deducted from the price received:

- the market value of the property at January 1 1980 or, if it was acquired after that date, the price paid or the consideration given for the acquisition of the property;
- the cost of any major improvements;
- the subsequent increase in the value of the property due to inflation, calculated by reference to the

Retail Price Index issued every month by the Department of Statistics; and

- expenses related to the acquisition and disposal of the property, such as transfer fees and legal costs.

Individuals may deduct from the resultant gain the following lifetime exemptions:

- in the case of sales of agricultural land by farmers, the first €25,629 of the sale price, provided that the farmer resided in the same area at the time of the sale;
- in the case of sales of property used as a residence by the vendor, the first €85,430 of the sale price, provided that the property has been used as the vendor's residence for at least five years prior to the sale; and
- in the case of any other disposal, the first €17,086 of the sale price.

Many of Cyprus's double tax treaties tax capital gains only in the country of residence of the company or individual disposing of the asset. The exemption from capital gains tax in Cyprus could therefore lead to complete elimination of any tax liability (eg, in the case of a capital gain made by a Cyprus-resident company from a sale of its foreign subsidiary's shares, which will be exempt from tax both in Cyprus and in the country where the subsidiary and the shares are based).

As the gain from a sale of goodwill is subject to corporate income tax at 12.5%, it is usually beneficial to transfer goodwill to a newly formed company and sell the shares of that company. Any capital gain on the sale of the shares (which will include the value of the goodwill) will be exempt from tax.

### **Double tax agreements**

Cyprus has a comprehensive network of double taxation agreements.<sup>(1)</sup>

All of the the treaties provide relief from double tax by applying the credit method to the taxation of dividends and interest. Cyprus residents' liability for Cyprus income tax and SDC is reduced by tax paid or payable in the other country, so that the taxpayer pays only the higher of the two rates of tax and is not taxed twice on the same income.

Even where there is no double tax treaty in place, the Cyprus tax authorities will allow unilateral relief in the form of a tax credit against Cyprus tax in respect of foreign tax on the same income charged in the country of origin.

### **Succession taxes**

The Estate Duty (Amending) Law of 2000 abolished any form of succession tax in respect of deaths taking place on or after January 1 2000.

### **Advance rulings**

The commissioner of income tax provides written replies on the interpretation of Cyprus tax law provisions. This practice is not incorporated in the Cyprus tax legislation and it is not an official ruling regime as used in other EU member states. Even so, the interpretations should be binding on the tax authorities if the full facts are disclosed on the ruling request. It is hoped that the advance ruling practice will be extended so that taxpayers can obtain binding advance decisions on the tax consequences of proposed transactions.

### **Capital duty**

On incorporation of a Cyprus registered company, capital duty of €105 plus 0.6% of the authorised capital is payable to the registrar of companies. Any subsequent increase in share capital is liable to capital duty at 0.6%.

### **Annual levy on companies**

An annual levy of €350 is payable to the registrar of companies by all companies incorporated in Cyprus. The levy is payable by June 30 each year. Penalties are imposed in the event of late payment. If the levy is paid no later than two months after the due date, a penalty of 10% is imposed. If it is paid between two and five months after the due date, the penalty is 30%. Companies that have not paid five months after the due date may be struck off the register. They can be restored to the register only by paying an increased levy of €500 per year if they are restored within two years or €750 per year if they are restored after more than two years.

### **Stamp duty**

Stamp duty is payable on contracts relating to property or business in Cyprus. The rates are as follows:

- For transactions with a consideration up to €5,000, no stamp duty is payable.
- For transactions with a consideration in excess of €5,000 but not exceeding €170,000, stamp duty of €1.50 for every €1,000 or part thereof is payable.
- For transactions with a consideration in excess of €170,000, stamp duty of €2 for every €1,000 or part thereof is payable.

The maximum stamp duty payable on a contract is capped at €20,000. Where no amount of consideration is specified in the contract, the stamp duty is €35. For a transaction which is evidenced by several documents, stamp duty is payable on the main contract and ancillary documents are charged at a flat rate of €2. A number of categories of documents are exempt from stamp duty, including documents relating to corporate reorganisations (which are exempt from all forms of taxation) and ship mortgage deeds or other security documents.

Stamp duty must be paid within 30 days of the date of execution of the relevant documents or, if they are executed abroad, within 30 days of their receipt in Cyprus. If stamp duty is paid late, a surcharge of approximately 10% of the unpaid amount is payable if payment is made within six months of the due date; otherwise, the surcharge is twice the unpaid amount.

Documents that require stamping will not be accepted for registration by government departments or as evidence by courts unless they are stamped.

#### **Value added tax**

Cyprus's standard rate of value added tax (VAT) is 19% and reduced rates of 5% and 9% apply to certain goods and services. The VAT registration threshold is €15,600 per annum. VAT returns must be submitted quarterly and any tax due must be paid by the tenth day of the second month following the quarter-end date. If the amount of input tax is greater than output tax, the difference may be refunded or carried forward to the next return. Companies that do not have trading activities within the European Union need not register for VAT, but will be unable to recover input tax.

#### **Immovable property tax**

Immovable property tax is payable each year on the market value of all immovable property registered in the name of the taxpayer at the start of the year, with progressive rates of taxation being charged on each tranche of the total value. For years up to and including 2014, the tax was based on 1980 values and the rates for 2014 progressed from 0.6% on the first €40,000 to 1.9% on any amount above €3 million.

The government has recently concluded a revaluation of properties with the intention of revising the immovable property tax system, re-basing it on current values and adjusting the rates accordingly.

#### **Fees on transfer of immovable property**

The Department of Land and Surveys, which is responsible for property registration in Cyprus, charges a fee for the transfer of immovable property. The fee, which is generally payable by the transferee, is based on the purchase price or, under certain circumstances, on the current market value. No transfer fees are payable in respect of company reorganisations, and exemptions and reductions are available in respect of transfers between family members and between family members and family companies.

The first €85,000 is charged at 3%; the next €85,000 is charged at 5% and any excess above €170,000 is charged at 8%. Thus the transfer fee on a property priced at €250,000 will be €13,200 (€85,000 at 3% plus €85,000 at 5% plus €80,000 at 8%).

In order to stimulate the market for new properties, the government has announced temporary waivers and reductions of transfer fees. The transfer fee on a sale of property on which VAT is payable will be waived provided that the sale agreement is deposited with the Department of Land and Surveys by December 31 2016. For a first-time sale of a new property which is not subject to VAT (which is the case if the building permit was obtained prior to May 1 2004), the transfer fee is halved.

#### **Levy on credit institutions**

Credit institutions operating in Cyprus are required to pay a levy of 0.095% on their customer deposits as at December 31 of the preceding year. Inter-bank deposits are not subject to the levy. The levy is payable by:

- Cyprus banks in respect of their banking activities in Cyprus (overseas branches and subsidiaries are not subject to the levy);
- the Cyprus operations of foreign (EU and third-country) banks and credit institutions; and
- cooperative credit institutions.

The levy is not deductible for the purpose of calculating taxable profits, but it will be taken into account in calculating profits subject to deemed dividend distribution.

The declaration of taxable deposits on the preceding December 31 must be made by March 31 each year and the levy is collected in four equal instalments at the end of each quarter, starting March 31.

The levy is limited to 20% of taxable profits for the year in respect of which it is paid. The tax authorities must issue final income tax assessments within six months of the date on which the corporate income tax return is submitted and any overpayment above the 20% limit must be refunded within a month of the issue of the final income tax assessment.

#### **Taxation of international shipping and ship management activities**



The Merchant Shipping (Fees and Taxing Provisions) Law of 2010 (the Tonnage Tax Law) gives qualifying Cyprus-resident shipping and ship management companies the option to be taxed on the basis of the tonnage of the vessels they operate, simplifying and reducing the tax burden. It widens the range of exempt gains to include profits on the disposal of vessels, interest earned on funds and dividends paid directly or indirectly from shipping-related profits, in addition to profits from shipping operations.

Qualifying persons are tax-resident owners or charterers of Cyprus ships, of EU ships or of fleets of ships comprising EU and non-EU ships, and ship managers providing technical or crewing services or both. Ship managers must maintain a functioning office in Cyprus staffed by a sufficient number of appropriately qualified personnel. At least 51% of onshore personnel must be citizens of the European Economic Area (EEA – comprising the European Union together with Iceland, Liechtenstein and Norway), and at least two-thirds of the total tonnage under management must be managed within the EEA.

For owners or charterers of Cyprus ships, the tonnage tax scheme is mandatory. Other owners or charterers and ship managers may opt for taxation based on profits or tonnage tax, but having opted for the tonnage tax scheme, they must remain within it for 10 years unless the vessel is sold or a charter or management agreement is terminated. For a fleet to qualify for the scheme, at least 60% of its tonnage should comprise of EU ships. If this requirement is not met, the non-EU vessels may still qualify if certain criteria are met, but surcharges may be payable.

For owners and charterers, qualifying activities are maritime transport of goods or people between Cyprus ports and foreign ports or offshore installations or between foreign ports or offshore installations, including towage, dredging and cable laying. For ship managers, qualifying activities are the provision of services under a written agreement to a ship owner or bareboat charterer in relation to crew management, technical management or both. A qualifying vessel is a sea-going vessel that has been certified in accordance with international principles and legislation of the flag country and is registered in the register of a member country of the International Maritime Organisation and International Labour Organisation.

The Tonnage Tax Law replaces taxes based on profits with a tax calculated on the net tonnage of the vessels concerned.

For owners and charterers, the tax exemption covers profits from the use of a qualifying vessel, dividends paid out of those profits at all levels of distribution and interest income relating to the financing, maintenance or use of a qualifying vessel and the related working capital, excluding interest on capital used for investments. Profits from the disposal of a qualifying vessel or any share or interest in it and profits from the disposal of shares in a ship owning company are also exempt from tax. In order to qualify for the exemption, at least 25% of the net tonnage of vessels subject to tonnage tax must be owned or bareboat chartered. The percentage can be reduced, but not for more than three consecutive years. The qualifying percentage is reduced to 10% if all vessels of the charterer are registered or managed in the EEA.

Ship managers may elect to pay tonnage tax at one-quarter of the rates applicable to ship owners and charterers, in which case profits earned from the provision of technical and crewing services are exempt from tax in respect of qualifying vessels, together with dividends paid out of those profits at all levels of distribution.

Profits from commercial management are not covered by the tonnage tax scheme and remain taxable under corporation tax.

Section 46 of the Tonnage Tax Law contains an 'all or nothing' provision. Qualifying owners, charterers and ship managers opting to enter the tonnage tax system must include all qualifying ships. If a company which is part of a Cyprus tax resident group of companies enters the tonnage tax scheme, then all other qualifying members of the group must simultaneously enter the scheme. The Tonnage Tax Law contains ring-fencing provisions to prevent exemption being gained in respect of ineligible activities. Separate accounts must be maintained in respect of qualifying and non-qualifying activities and transactions with related parties that are not in the tonnage tax system must be made at arm's length.

Tonnage tax is charged on a sliding scale on net tonnage. The initial rates charged to owners and charterers are set out in the following table:

<b>Tonnage</b>	<b>Rate per tonne</b>
First 1,000 tonnes	€0.3650
Next 9,000 tonnes	€0.3103
Next 15,000 tonnes	€0.2008
Next 15,000 tonnes	€0.1278

Each tonne above 40,000	€0.0730
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By way of example, the annual tonnage tax on a ship of 50,000 tonnes would be €8,816.70. Cyprus-flag ships are also subject to an annual registry maintenance fee of €300. For ship managers, the rates are one-quarter of those set out in the table above.

### IP box

In 2012, Cyprus introduced a package of incentives and tax exemptions relating to income from IP rights, aimed at stimulating investment in research and development. A number of other countries have introduced similar schemes, which have come to be known as an 'IP box'.

Four-fifths of the profit earned from the use of intangible assets (including any compensation for improper use) is disregarded for tax purposes. In addition, four-fifths of any profit resulting from the disposal of relevant intangible assets is disregarded for tax purposes.

The net effect of the scheme is that the rate of tax on income from the exploitation of intellectual property is 2.25% or less. Since there are no taxes on dividends paid to non-resident shareholders, a Cyprus-resident company can be used to generate royalties under licensing or similar arrangements with third parties and distribute profits to its shareholders by way of dividends with minimal tax leakage.

Cyprus's effective tax rate of 2.25 or less on income from the exploitation of intellectual property compares favourably with the competition:

- The United Kingdom's patent box regime gives an effective rate of 10% on relevant income.
- The Irish scheme is more complex and it is not possible to directly compare rates, but it will generally produce an outcome close to the UK rate; and
- The Luxembourg and Netherlands schemes give an effective rate of 5.76% and 5% respectively, more than double the Cyprus rate.

Further, the Cyprus exemption scheme applies to a wider range of assets and includes fewer restrictions and limitations than other schemes.

The tax regime provides attractive opportunities for structuring the exploitation of IP assets through Cyprus and in particular through the use of Cyprus-resident IP owners, especially in the context of Cyprus's extensive network of double-tax treaties under which foreign withholding taxes on royalty income are either eliminated altogether or substantially reduced.

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### Endnotes

(1) As of January 1 2015 double tax agreements were in operation between Cyprus and Armenia, Austria, Azerbaijan, Belarus, Belgium, Bosnia, Bulgaria, Canada, China, Czech Republic, Denmark, Egypt, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, India, Ireland, Italy, Kuwait, Kyrgyzstan, Lebanon, Lithuania, Malta, Mauritius, Moldova, Montenegro, Norway, Poland, Portugal, Qatar, Romania, Russia, San Marino, Serbia, Seychelles, Singapore, Slovakia, Slovenia, South Africa, Spain, Sweden, Syria, Tajikistan, Thailand, UK, Ukraine, United Arab Emirates, the United States and Uzbekistan. Treaties are under negotiation, or awaiting ratification, with a number of other countries.

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