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European Company (SE) Taxation: The Cyprus Perspective

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Since its the accession on May 1, 2004, Cyprus has been widely considered to be the E.U. Member State with the lowest corporate tax rate (10 percent). Due to various other tax advantages, such as exemption possibilities for inbound and outbound dividend payments, no withholding taxes on interest for non-residents, a network of double taxation treaties, tax deductions in respect of borrowing costs, no thin capitalisation rules, narrow and flexible CFC legislation as well as group relief, to name just a few advantages, the island is generally recognised by tax experts as one of the more attractive locations for the establishment of a holding company in Europe. The availability for use of the SE statute since October 8, 2004 should have further increased Cyprus' attraction as a holding destination. However, such attraction will largely depend on the taxation of the SE in general and the tax advantages that may exist for an SE established in Cyprus.

This article will look first at tax aspects of an SE in general, illustrating some of its taxation problems which may currently exist in an E.U. high tax jurisdiction such as Germany. We then examine the tax situation in Cyprus and its specific application to an SE. In conclusion we provide a brief summary highlighting the advantages Cyprus presents as a place of registration of **an SE.**

I. General Tax Aspects of the European Company

A. General Rules on the Taxation of an SE

According to Article 9, Para 1 c) (ii) of the Council Regulation (EC) No 2157/2001 (the Regulation) on the Statute for a European Company (SE), the provisions of Member States' laws which would apply to a public limited liability company in that state apply to an SE with a registered office in that state in relation to matters not regulated by the Regulation. Note (20) of the Preamble to the Regulation clarifies that the Regulation does not cover, *inter alia,* taxation matters. Consequently, a European company is principally taxed according to Community law and the national laws of the Member State where It has its registered office. It is therefore necessary to consider relevant Community law, in particular the Merger Directive,[1] the Parent-Subsidiary Directive[2] and the Interest and Royalties Directive[3] as well as the national tax laws of the state where the SE will be established, when looking at the tax situation of an **SE.**

B. Important tax aspects of an SE

Various circumstances exist, where an SE may be subject to taxation. The main taxable situations are (Section I.C) the formation of an SE, (Section I.D) the running of the company, (Section I.E) the distribution of profits and (Section II.F) the transfer of its registered office.

C. Formation ofanSE

The Regulation provides for different ways of forming an SE: formation by merger;[4] formation of a holding SE;[5] formation of a subsidiary SE[6] (and separately, formation of a subsidiary SE by an SE[7]); and transformation of a public limited liability company into an SE.[8]

With regard the taxation of the formation of an SE, the greatest concern exists with respect to the disclosure of so called "hidden" reserves. The national tax laws of some Member States require such a disclosure in cases where a transaction has a cross-border nature.[9]

Although the E.U. Merger Directive provides, in cases of cross-border mergers, transfers of assets and exchange of shares (and in its amended form will be applicable to the formation of an SE by merger, the formation of a holding SE, the formation of a subsidiary SE and the transfer of the registered office of an SE[10]) for the avoidance of discrimination and disadvantage on a national tax level, the various Member States have yet to transpose the Merger Directive fully into national law.[11]

1. Formation by merger

In the area of mergers, the SE may be used for cross-border mergers and acquisitions and provide for a lean structure, cost effectiveness and facilitated corporate governance, when compared to the difficulties existing prior to the availability of an SE.

In principle, a distinction can be made between (a) merger by acquisition and (b) merger by creation of a new company. However, the Merger Directive defines, in Article 2 (a), both alternatives equally as "merger"; subsequently, the same rules concerning taxation and completion of depreciation, profits and losses are applied to both types of merger. If any national law makes a distinction between the various types of merger and applies different tax regimes thereto, the respective Member State would be in violation of the Merger Directive and, consequently, would have to amend its tax laws (or risk the intervention of the E.U. Commission and the direct application of the Merger Directive within Its territory).

The national tax laws of a high tax jurisdiction (HTJ) may further distinguish between (i) an outbound alternative, *La,* the registration of the new SE abroad and (ii) an inbound

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alternative, i.e. the registration of the new SE within its territory, and be tempted to tax the various alternatives differently.

a. Outbound merger

In the event of registration of a new SE abroad, the national tax laws of a HTJ concerning the winding up or liquidation of a company, the transfer of its registered office or the transfer of management abroad and provisions regarding the remainder of the transferring national company as a domestic permanent establishment of the new SE may not apply.[12]

Regarding the disclosure of hidden reserves by companies or shareholders in the case of outbound mergers, the amended Merger Directive will apply to the SE and provide for tax neutrality (and consequently the non-disclosure of any reserves) of the merger under certain conditions.

In respect of transferring companies, Article 4 of the Merger Directive provides for the exclusion of any taxation of capital gains on the part of the transferring company regarding transferred assets and liabilities, if:

- those transferred assets and liabilities are, In consequence of the merger, effectively connected with a permanent establishment (PE) of the SE in the Member State of the transferring company;
- the transferred assets and liabilities play a part in generating the profits or losses of the PE in the Member State, where the PE of the SE is situated; and
- the receiving SE computes any new depreciation and any gains or losses in respect of the assets and liabilities transferred according to the rules that the transferring company would have applied.

Until now, unnecessary costs of cross-border mergers in the form of taxes on capital gains often occur due to the fact that different accounting standards and rules exist in the different Member States involved in a cross-border merger. It is *de facto* at times very complex and burdensome for a receiving company, *i.e.,* an SE, to comply with the obligation to compute new depreciation, gains or losses according to the same rules as the transferring company would have done, because the Member State where it is registered does not apply the same accounting rules and standards as the State where the transferring company was registered or does not foresee the application of the required computation method.

In respect of the shareholders of the transferring company, Article 8 of the Merger Directive provides for tax neutrality, *i.e.,* the absence of any taxation of the income, profits or capital gains of the shareholder, provided the latter does not attribute to the securities received a value for tax purposes higher than the securities transferred. "Value for tax purposes" means the value based on which any gain or loss would be computed for the taxation of the shareholder.

b. Inbound merger

In the event of the registration of a new SE within the territory of a HTJ, Article 7 of the Merger Directive provides for the tax-free accrual to the SE of any gains on the cancellation of its holding, provided the holding exceeds 25 percent (gradually lowered to 10 percent after the amendment of the Merger Directive) of the capital of the transferring company. Otherwise, the national tax law applying to the SE may provide for the taxation of such gains.[13]

In respect of the shareholders) of the transferring company, the merger will not lead to any tax liabilities, provided the conditions of Article 8 of the Merger Directive are met.

2. Formation of a holding SE

A holding SE may be a suitable instrument for a cross-border amalgamation of companies or the reorganisation of a company, for example, the restructuring of the European distribution channels of a non-E.U. holding company by way of creation of a European holding SE and the subsequent merger of the various distribution subsidiaries in different Member States into the SE.

Similar to the formation by merger, the formation of a holding SE may also be distinguished for tax purposes as (i) the formation of an Inbound holding SE, and (ii)the formation of an outbound holding SE.

The Merger Directive applies not only to mergers, but also to the "exchange of shares", defined as",. ,an operation whereby a company acquires a holding in the capital of another company[14]...." Thus, the formation of a holding SE shall be covered by the Merger Directive,

a. Inbound holding SE

The Merger Directive covers, In its Article 8, the avoidance of any taxation of the income, profits or capital gains of the shareholder of an acquired company, which may arise merely from the allotment of securities of the acquiring SE to such shareholder. Such avoidance of tax is conditional upon the shareholder not attributing to the securities received a higher value than the acquired shares had immediately before the exchange.

However, the Merger Directive does not exclude the provision by the national tax laws of a HTJ, in the case of the formation of an inbound holding SE, for the taxation, according to such national laws, of the sales price obtained by the transferring shareholder later on. This is particularly the case in all circumstances where the computation of the sales price will result in the realisation of a capital gain.[16]

b. Outbound holding SE

Similar to the situation in outbound mergers, the formation of an outbound holding SE may lead to difficulties where the national tax laws of the HTJ require that the foreign SE continues to compute the accounted depreciation, profits, losses, *etc.* of the exchanging domestic shareholder in order that the exchange of shares should be recognised by such national tax laws. The Member State where the holding SE is registered may simply not provide for the continuing computation of previously accounted values and tax neutrality of the transaction may therefore not be obtainable.[16]

Furthermore, the national tax laws of HTJ may provide for delayed taxation of the contributed shares, if the holding SE resells such shares within a certain period of time. The holding SE may therefore be restricted - at least temporarily - in its ability to freely dispose of the acquired shares.[17]

3. Formation of a subsidiary SE

A subsidiary SE may be used for the operation of a joint venture between companies of different Member States or for the reorganisation of a group of companies. It may either be formed by subscription for its shares through at least two legal bodies existing in two different Member States or be set up by an SE. The creation of the subsidiary SE can be realised by exchange of shares (provided less than 60 percent of the share

capital of the transferring company is exchanged) or by transfer of a branch of activity, *i.e.,* the transfer of assets, The transfer of a branch of activity can be accomplished by the transfer of a permanent establishment situated in another Member State or by the transfer of a permanent establishment situated in the Member State where the subsidiary SE is to be registered.

The Merger Directive applies principally to the formation of a subsidiary SE. With only a few exceptions In respect of the formation of a subsidiary SE, *I.e.,* regarding rollover relief, carry-over of tax exemptions and reserves and the take over of losses in the case of transfer of a branch of activity as well as rollover relief for shares received In the case of exchange of shares, it has been largely correctly implemented in the national tax laws.[1*] The taxation, *i.e.,* the tax neutrality of the formation of a subsidiary SE, should therefore not give cause for great concern.

4. Transformation of a public limited liability company into an SE

Community law does not regulate tax issues pertaining to the transformation of a public limited liability company ("pic") into an SE. The taxation of this situation is solely regulated by the national tax laws of the Member States.

It appears that there is no tendency within the Member States to tax the creation of an SE by way of transformation of an existing public limited liability company and no indication exists that this situation may change in the near future.[19]

Considering the fact that the institution of an SE has been created by the E.U, legislators, *inter alia,* in order to facilitate the transfer of the registered office of a company within the European Union, it appears obvious that the transformation of a public limited liability company into an SE may be in numerous cases a suitable first step to prepare for the transfer of the registered office of a pic.

D. Running the company

On a Community level, the operation of an SE is not (yet) subject to specific E.U. tax rules. Generally, an SE is treated at its place of registration like any other tax paying pic. normally with foreign subsidiaries and/or foreign PE (or, respectively, a foreign parent company).

Except for certain specific areas, such as sales taxes in the form of VAT, the European Union is still lacking a harmonised tax system, in particular with regard to company taxation, Different corporate tax rates may (and realistically will) lead to tax competition. Until E.U, harmonisation with regard to corporate taxes is achieved, companies will have to take into consideration, as one important cost factor, the tax rates offered by the different Member States when looking at the most suitable place for the incorporation of an SE.

The existence of different company tax base calculation rules in different member states currently leads *de facto* to complex and costly tax base calculation processes and possibly unsatisfactory results for companies operating in different E.U. Member States. An SE registered in a HTJ with a large network of Double Taxation Treaties ("DTT"), operating a PE in another Member State, may face difficulties regarding the computation of PE losses in its home state. The DTTs may exempt the results of foreign PEs. Losses suffered by the PE. which regularly occur during the first years of establishment due to necessary (and often costly) Investment, may therefore not be used to lower the tax base of the SE at its place of registration in the HTJ.[20]

The taxation of PEs in the various Member States should not give cause for concern. Although PEs are often taxed differently than local companies, the same tax rate applies. Interest expense allocations to the PE in the case of a financed loan from the SE to the PE should be tax deductible for the PE either under the national tax law applicable at the PE's place of establishment or according to existing international tax treaties.[21]

The E.U. Commission has launched the idea of testing a common consolidated E,U. company tax base with an SE pilot scheme, which is under discussion. The Common Consolidated Base Taxation ("CCBT") would allow E.U.-wide operating companies to calculate their tax base on an E.U.-wide uniform tax base. The uniformly calculated consolidated profit of the company would then be distributed between the different Member States where the company is active and taxed according to the respective national tax laws. The CCBT may be developed from the E.U. Directives on annual account and on consolidated accounts, from the International Accounting Standards and the International Financial Reporting Standards as well as from common taxation principles.

E. Distribution of Profits

Profits may generally be distributed either through payment of dividends or in the form of interest or royalty payments.

In the case of interest or royalty payments between associated companies or companies and their PEs, the Interest and Royalty Directive is applicable to SE parent and subsidiary companies or the PE of an SE. Interest and royalty payments by the subsidiary or the PE to the SE in another Member State are thereby exempted from taxation at source. The proposed amendments to the Interest and Royalty Directive include the application of this Directive to the SE.[22]

The taxation of dividends may lead to difficulties and ultimately limit the acceptance of the SE as a suitable form of entity for European cross-border business. Various Member States apply different tax regimes to dividends depending on whether these are distributed by domestic or foreign companies. The taxation of dividends may therefore be looked at from three different points of view: a corporate direct Investor: a portfolio corporate shareholder; and an individual shareholder.

/. Corporate direct investor

A corporate direct investor holding at least 25 percent (after the amendment of the Parent-Subsidiary Directive in 2003 gradually to be lowered to 10 percent) of the dividend paying company may rely on the Parent Subsidiary Directive, which in its amended version applies to parent as well as subsidiary SEs.[23] The dividends received by a parent SE or a subsidiary SE from its respective subsidiary will either be tax free or fully credited for dividend withholding or foreign corporate taxes paid on the profits underlying the distributed dividends. Numerous national tax laws and DTTs will likewise provide for exemption or a full credit. Dividends paid by an SE to a foreign parent company holding at least 10 percent of its capital are exempt from withholding tax,

2. Portfolio corporate shareholder

Portfolio corporate shareholders generally own small amount of shares In the dividend distribution company. So far they have

often been entitled neither to exemptions under national tax laws nor to full tax credits for paid foreign withholding and corporate taxes; additionally, they were subject to foreign withholding taxes when receiving dividends from abroad.[24] It would be difficult to convince portfolio corporate shareholders to exchange their shares in a domestic company for shares in a foreign SE, if national tax laws were allowed to burden foreign dividends with unfavorable national taxes regimes and discriminate against them In favour of domestic dividends.

In this respect, the amended Parent-Subsidiary Directive will gradually bring relieve until January 2009, when the minimum shareholding percentage for the applicability of the Directive will have been lowered to 10 percent.[25]

Furthermore, similar considerations as currently applied by the E.U. Commission with regard to the taxation of dividends received by individuals have to apply to portfolio corporate shareholders.

3. Individual shareholders In the past, national tax laws have burdened individual shareholders receiving foreign dividends. Discrimination against foreign dividends existed and additional costs in the form of national taxes in the residence state of the shareholder applied. It was therefore necessary to tackle this issue at a Community level in order to create incentives for individuals to participate in foreign SEs.

In December 2003 the Commission issued a Communication on the dividend taxation of individuals.[26] In essence, the Communication made it clear that a Member State cannot discriminate against dividends from another Member State received by an individual and subject such dividends to taxation higher than on domestic dividends. Likewise, dividends paid to individuals have to be treated equally. Otherwise, cross-border investments might be restricted, resulting in fragmented capital markets in the European Union. The Commission threatened legal action against those Member States whose dividend tax rules would not comply with the Treaty.

The ECJ has considered, in various cases, the issue of different tax regimes applicable to foreign and domestic dividends with regard to the fee movement of capital provisions. In principle, such discriminatory treatment was declared incompatible with these provisions.[27]

In essence, dividends paid by a foreign SE to individual or portfolio corporate shareholders cannot be taxed more highly than domestic dividends received by such shareholders. Any national tax rule to the contrary is in contravention of existing Community law.

F. Transfer of the Registered Office

One of the most significant aspects of the SE is surely its ability to transfer its registered office from one Member State to another without the need to wind up and re-register the company. However, the taxation regimes of various Member States will have to be adjusted in order to enable the SE to accomplish on a tax level what has been guaranteed by the Regulation solely on a company level.[2*] Until now, some Member States still request the disclosure of all hidden reserves and levy an exit tax upon the migration of a domestic company.[29]

With regard to individuals, exit taxes have just recently (in the case of *Lasteyrle du Saillant*[30]) been declared incompatible with E.U. law. The judgment applies to individuals in the case of migration of the individual, How far this judgment could be applied to companies may be subject to discussion for some time.

An SE may transfer its registered office and either migrate from or move to a HTJ, thereby incurring various tax related difficulties.

1. Migration from a HTJ

The migration from a HTJ may have different tax consequences for (i) the migrating SE and (ii) the remaining shareholder(s).

a. *Tax consequences for the migrating SE*

The company may be obliged to disclose all hidden reserves and be subject to some sort of migration tax according to the national tax laws of a HTJ. However, such migration tax (and disclosure of hidden reserves) should not apply, if the HTJ did not have the right to levy taxes before the migration[31] or does not lose its taxation right after the migration.

It should be noted that the proposed amendments to the Merger Directive in the new Article 10a, applicable to the transfer of the registered office, provide for tax neutrality of assets and liabilities of the transferring company, if those remain effectively connected with a remaining FE of the SE and any new depreciation, gain or loss in respect of those assets and liabilities is computed on the previously applied basis. As a result, the assets and liabilities of the transferring company may be carried forward in the remaining PE,

b. Tax consequences for the remaining shareholder(s)

The tax consequences may depend on the applicable national tax law and vary from one Member State to another. However, if a DTT applies, a provision under Article 13, Para 5 OECD-Model Convention[32] would give the taxation right to the shareholder's resident state.

2. Moving to a HTj

The SE would become subject to the national tax laws of the HTJ and would be fully liable to taxes levied in the HTJ. It would also have to comply with accounting standards applied in that state and may have to compute any new depreciation, gain or loss according to the rules applicable in such state, Questions may arise with regard to the evaluation of assets newly transferred into the HTJ, In the event that a PE had already been established prior to the migration, the assets, profits and losses of such PE will presumably be carried forward and computed according to the previously applied rules.

There should be no significant consequences for the shareholders of the SE, in particular in cases where an existing DTT gives the taxation right to the shareholder's resident state.[33]

In the future, the amended Merger Directive will apply to the transfer of the registered office of an SE as explicitly provided for in its amended Article 1 (b).

II. The Taxation of an SE in Cyprus A.

Taxation of companies in Cyprus

Companies In Cyprus are (with the exception of International Business Companies, which have opted for a transitional period ending 2005 to be taxed according to the previously applicable tax rate) all subject to the same tax regime, irrespective of whether they are established as public limited or as private limited companies. An SE established in Cyprus will

therefore be taxed according to the rules generally applicable to companies.

A company established in Cyprus will be subject to corporation tax. This tax Is charged on the worldwide income profits of the company's business and gains on trading investments in Cypriot real property, if the company is resident in Cyprus. A company is considered a resident company for Cypriot tax purposes, if its management and control are exercised in Cyprus. A flat corporate tax rate of 10 percent is applied. Business income of non-resident companies is generally only taxed if accruing to a permanent establishment in Cyprus.[34] Exceptions apply to ship and aircraft operating companies.

The following comments on Cypriot tax matters relating to an SE focus on the issues discussed in the first part of this article.

B. Cypriot rules on SE relevant taxation issues

The most critical taxation issues relevant to an SE have been discussed above. Cyprus could become a sought-after destination for the registration of SEs, if these issues are in principle covered by Cypriot tax law. In light of its accession to the European Union, Cyprus had to implement substantial changes to its tax regime. In the course of these changes, Cyprus has adopted the various E.U. Regulations and Directives, in particular the Merger Directive and the Parent-Subsidiary Directive. Various issues, which may be of concern for an SE in some of the other (particularly older) Member States, may already be taken care of by the current reformed tax system, which came into force on January 1, 2003.

C. Formation of an SE in Cyprus

7. Formation by merger

The Cyprus Income Tax Law (CITL) has, to a large extent, adopted the Merger Directive, including the definitions therein contained. The introduction of the Merger Directive into the national tax system did not present a great difficulty, as basically no conflicting provisions existed previously. The old Cypriot tax system did not contain any comparable rules on company reorganisations.

With regard to mergers, the CITL does not discriminate between resident and non-resident companies. The term "merger" also expressly includes the cases of acquisition and creation of a new company.

In the case of outbound mergers, a Cypriot company transferring assets and liabilities into a foreign SE is not liable to tax on profits. It can transfer all balance sheet values, whereby provisions and reserves are specifically mentioned. The problem of having to disclose hidden reserves should not appear. Although the CITL provides in section 26 para (2) for the continuation of the book values of the transferred assets, liabilities, provisions and reserves by the receiving SE, the tax neutrality of the transferring company, which is regulated in section 26 para (1), has not been made conditional upon the book value continuation.

Accumulated losses of a transferring Cypriot company or foreign company with a Cypriot PE may be carried forward to the new Cypriot SE or foreign SE with a Cypriot PE.[36]

The shareholders of the transferring company are not liable for tax with regard to shares received in exchange for the shares representing the capital of the transferring or acquired company. The CITL contains in section 29 a provision similar to Article 8 of the Merger Directive (note: only paras 3 and 4 of Article 8 of the Merger Directive have not been adopted).

As regards inbound mergers into Cyprus, section 28 of the CITL contains a provision similar to Article 7 of the Merger Directive and provides for a tax-free accrual of any profits to the new Cypriot SE, if it had a holding in the transferring company and the profits accrue on the cancellation of the holding. Interestingly, no minimum holding requirements exist for the new Cypriot SE to benefit from the provision.

2. Formation of a holding SE

As the Merger Directive had been adopted during the course of the Cypriot tax reforms, the most relevant tax issues pertaining to the formation of inbound and outbound holding SEs are covered by the Cypriot tax laws.

a. Inbound holding SE

Section 29 of the CITL has implemented the provisions of Article 8 of the Merger Directive, excluding the taxation of the profits or benefits of the shareholder of an acquired company merely on the allotment of shares of the acquiring SE. Although the CITL has, in principle, also transposed the provisions of the Merger Directive concerning the taxation of profits arising out of the subsequent transfer of shares, profits from the sale of securities (which in accordance with the law's definition include shares) are, as with income from dividends in Cyprus, generally tax exempt-

Furthermore, no capital gains tax is payable in Cyprus because of a transfer of chargeable assets *[i.e.,* immovable property in Cyprus or shares in a company owning immovable property in Cyprus). However, In the case of later sale of chargeable property the original base cost will be used, *i.e.,* taxation will not be avoided, but just postponed.[37]

b. Outbound holding SE

The tarnation of an outbound SE should not create a problem for any Cypriot company involved in such a transaction from a Cypriot law perspective. Balance sheet values, similarly to the case of an inbound merger, can be carried over without creating any tax liability for the transferring company. Likewise, losses may be carried over, provided the receiving foreign SE has a permanent establishment in Cyprus,[34]

Provided no chargeable property is disposed of, the re-selling of transferred shares by the foreign SE does not lead to any delayed taxation issues as the transfer of shares is generally tax exempt in Cyprus.

3. Formation of a subsidiary SE in Cyprus

The formation of a subsidiary SE in Cyprus, like the formation of a holding SE, should not lead to any difficulties as the Merger Directive has been implemented in Cyprus. As far as possible within the boundaries set by the Directive, the Cypriot tax reform has created a tax environment which is more favourable than the one foreseen as a minimum standard by the Merger Directive. In particular, the tax neutrality of transferred book values explicitly extends to provisions and reserves, and the continued computation of profits and losses in respect of the transferred assets and liabilities, although mentioned in the law. is not directly formulated as a condition for the application of such tax neutrality.

4. Transformation of a Cypriot pic into an SE

The mere change of company form is, as in the other Member States, not subject to taxation. Furthermore, Cypriot Income Tax Law does not distinguish between private and public

companies. In fact, the new Cypriot Income Tax Law has abolished the previously existing notion of a "Public company", It therefore appears that the tax authorities in Cyprus would not tax the transformation of a public limited company into an SE.

D. Running of a Cypriot SE

Any SE incorporated in Cyprus will benefit from the favourable corporate tax rate of 10 percent.

In addition, a Cypriot SE will, of course, be able to benefit from all the tax advantages usually accruing to a Cypriot-resident company. For example, Cyprus has signed a large and further growing number of double taxation treaties. Generally, these treaties provide for the taxation of PEs at the place where they are established. In most cases of foreign PEs of a Cypriot SE, any applicable treaty would most likely provide for a full credit of taxes paid abroad.

Losses from any business carried on outside Cyprus through a permanent establishment of the SE are allowed as a deduction from the SE's income from other sources for the same year.[30]

In essence, the new Cypriot tax laws have been designed to provide for an excellent holding environment.[40] An SE registered in Cyprus would, of course, fully benefit from all tax benefits that exist on the island.

E Distribution of Profits of a Cypriot SE

Dividends received by either an individual or a corporate shareholder from a company registered in Cyprus or abroad are taxable income, but exempt from income tax in Cyprus.[41]

Dividends received by a Cypriot-resident individual or company from any company, whether in Cyprus or abroad, are subject to a Special Defence Contribution at 15 percent on the gross dividend.

In the case of foreign source dividends, credit relief is given In respect of the foreign tax.

Inter-cornpany dividends between a Cypriot SE and its Cypriot subsidiary are tax-exempt. Dividends from foreign E.U. subsidiaries paid to a Cypriot SE are tax-exempt, provided the Cypriot SE has at least a 1 percent holding in the subsidiary. As Cyprus has the lowest corporate tax rate in the European Union, CFC rules do not apply (for Cyprus to apply CFC rules, the tax burden at the source must be substantially lower than in Cyprus).

It should be noted that problems of discrimination against portfolio corporate shareholders or individuals receiving foreign dividends do not occur in Cyprus. Corporate shareholders are treated equally; domestic and foreign dividends are submitted to the same tax regime.

F. Transfer of the registered office

The Cypriot tax reform did not bring any changes with regard to taxation in the case of migration. Cyprus so far has not known any exit taxes and it is unlikely that the authorities would try to tax a Cypriot SE transferring its registered office to another Member State.

Any SE transferring its seat to Cyprus would become subject to Cypriot tax laws and would be liable to Cypriot tax with its worldwide income, provided management and control of the SE are exercised in Cyprus. The SE would obviously be able to benefit from the tax advantages already mentioned.

III. Conclusion

The SE has been created to further the development of the internal market and to facilitate the carrying on of business on **a** Community scale. It is supposed to be a tax neutral vehicle and not privileged or discriminated against in comparison with other Member States' public limited companies. The various E.U. Directives have been amended to include the SE and to achieve the above goals.

Through the efforts made prior to its E.U. accession, Cyprus has already put in place a tax regime that allows companies and businesses to carry out trading and investment activities on a European scale. Due to its fully E.U. compliant tax regime and a simple and flexible definition of the term "company" in the CITL, Cyprus should be able to further establish itself as a prime location within the European Union for holding companies in general and as a home state for SEs in particular.

The E.U. Commission's initiative on a common consolidated E.U. company tax base and its possible success should help to increase rapidly the acceptance of the SE as a suitable form of company amongst existing companies doing business In Europe.

1 Council Directive 90/434/EEC
2 Council Directive 90/435/EEC, amended by Council Directive 2003/123/EC
3 Council Directive 2003/49/EC
4 Article 2 Para 1 Council Regulation (EC) No 2157/2001
5 Article 2 Para 2 Council Regulation (EC) No 2157/2001
6 Article 2 Para 3 Council Regulation (EC) No 2157/2001
7 Article 3 Para 2 Council Regulation (EC) No 2157/2001
8 Article 2 Para 4 Council Regulation (EC) No 2157/2001
9 Article 8 b KStG (Germany), for Instance, contains a disclosure requirement in the case of an outbound merger
10 Amendment to Merger Directive proposed by Council Proposal 503PC0613
11 International Bureau of Fiscal Documentation (IBFD), Survey on the SE, September 2003, p. 38 If,
12 Example: Articles 11 and 12 KStG (Germany), which are not applicable in the case of an outbound merger of a German company
13 Article 8 b KStG (Germany), *i.e.,* merger profits may be subject to 6 percent corporate tax
14 Article 2 (d) of the Merger Directive 90/434/EEC
15 Article 20 Para 4 UmwStG (Germany)
16 Articles 17 and 3 No 40 EStG (Germany)
17 Article 26 Para 2 UmwStG (Germany) provides for delayed taxation for a period of seven years
18 IBFD, Survey, September 2003, p. 32 ff.
19 IBFD, Survey, September 2003, p. 38
20 As Is the case, for example, in Germany after deletion of the former Article 2 Para 3 EStG (Germany), which provided under certain conditions for tine possibility to apply for the recognition of losses incurred abroad till 1999.
21 European Federation of Accountants (FEE) Position Paper on Tax Treatment of the European Company, November 2003, p. 10
22 Proposal COM (2003) 841 for an amendment to the Interest and Royalty Directive
23 Council Directive 2003/123/EC
24 FEE Position Paper, November 2003, p. 8
25 Article 1 No. 3 (a) of Council Directive 2003/123/EC
26 Commission Communication COM/2003/810

27 Case C-36/98 Verkooijen [2000] ECR1-4071

28 IBFD, Survey, September 2003, p. 37

29 For example Germany, Article 12 Para 1 KStG (Germany)

30 ECJ *"Lasteyriedu Saillant",* March 11, 2004, Rs. C-9/02 ; *Tax Planning International: European Union focus,* BNA International, September 2004, p. 17ff.

31 Article 8 Para 2 KStG (Germany)

32 OECD-Model Convention with respect to taxes on income and on capital, 2003

33 Article 13 Para 6 OECD-Model Convention

34 Sec. 5(2)(a) Cyprus Income Tax Law (CITL)

35 Section 27, CITL

36 Section 8 Para 22 CITL

37 Law 119(1)2002 (Capital Gains Tax (amendment) Law)

38 Section 27, CITL

39 Section 13 Para 9 CITL

40 *Tax Planning International: European Union Pocus,* BNA International, July/August 2004: International Tax Aspects of the Cypriot Holding Company

41 Article 5 Para 1 (c), Article 8 Para 20 CITL

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See also, "The Arrival of the European Company: The Vehicle of the Future?^ EUF (October 2004).

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