



## Cyprus Tax Update – Year 2015

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On 9 July 2015, the House of Representatives enacted into laws a number of significant tax law proposals which were published in the Cyprus Government Gazette on 16 July 2015.

The amendments to the Cyprus Tax Legislation are in an effort to modernize the framework of the Cyprus tax system and improve Cyprus' competitiveness in attracting foreign investments.

We briefly outline below the main provisions with respect to the various tax law amendments.

- Income Tax Law
- Capital Gains Tax Law
- Special Contribution for Defence Law
- Department of Lands and Surveys (Levy and Duties) Law

### INCOME TAX LAW

#### Introduction of Notional Interest Deduction on “Qualifying” Equity

The Income Tax Law (ITL) has been amended to introduce a Notional Interest Deduction (NID) on equity.

According to the amended Law, companies resident in Cyprus and companies not resident in Cyprus which maintain a permanent establishment in Cyprus are entitled to a NID on equity, which is effectively a tax allowable deduction against the taxable profits of the company.

The NID is calculated by multiplying the “new equity” held and used by the business in the carrying on of its activities with the “reference interest rate”

For the purpose of the Law:

- “Reference interest rate” is the yield of the 10 year government bond of the state in which the new equity is invested plus a 3% premium, having as a minimum rate the 10 year Cyprus government bond yield as at 31<sup>st</sup> December of the tax year preceding the relevant tax year, plus a 3% premium.
- “New equity” is the equity introduced in the business on or after 1<sup>st</sup> January 2015 in the form of issued share capital and share premium (provided that these are fully paid) and does not include amounts that have been capitalised and which were derived from revaluation of movable or immovable property.

It is provided that any new equity that has been introduced in a company on or after 1<sup>st</sup> January 2015 which directly/indirectly emanates from reserves existing as at 31<sup>st</sup> December 2014 but does not relate to the financing of new assets used in the business, is not deemed as new equity.

The NID granted on new equity cannot exceed 80% of the taxable profit as calculated before allowing the NID. It is further provided that in the case of a loss such deduction is not granted.

A company may in any given tax year elect to claim the whole or part of the amount of the NID available.

#### Anti-abuse measures

In the case where the new equity of a Cyprus tax resident company or a non-Cyprus tax resident company which maintains a permanent establishment in Cyprus, is derived directly/indirectly from the new equity of another Cyprus tax resident company or a non-Cyprus tax resident company which maintains a permanent establishment in Cyprus, the NID on the new equity is available only to one of the two respective companies.



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In the case where the new equity emanates directly/indirectly from loans on which interest expense deduction is claimed, the NID on the new equity is reduced by the amount of the interest expense deduction claimed.

In the case where equity is contributed in the form of assets in kind, the amount of equity for the purposes of NID may not exceed the market value of the assets at the date of their introduction into the business, and their market value must be substantiated by the Commissioner's judgement.

In the case where reorganization is carried out without generating profits subject to taxation, the NID on equity is calculated as if the reorganization has not taken place.

The Commissioner may not grant the NID, if in his judgment actions/transactions have taken place without substantial economic or commercial purpose or the new equity on which the NID is claimed emanates from equity that existed prior to 1<sup>st</sup> January 2015 and is presented as new equity through actions/transactions with related parties, with the aim of claiming NID.

### Effective Date

The above provisions have come into effect on 16 July 2015, which is the date they were published in the Official Gazette.

### **AuditPro View**

*These new provisions which allow companies to fund their operations from own equity/capital and obtain a tax allowable deduction (NID), have been introduced to encourage the introduction of new equity into Cyprus tax resident companies and thus promote the development of the Cyprus economy. With a corporate tax rate of 12.5% and depending on the level of capitalization of a company the effective tax can be reduced to as low as 2.5%.*

## **SPECIAL CONTRIBUTION FOR DEFENCE LAW**

### **Introduction of "Domicile" concept in the Special Contribution for Defence Law**

The Special Contribution for Defence (SDC) Law is amended by introducing the new term of "domicile".

For the purposes of the SDC Law, an individual has a "domicile in the Republic" if he/she has a domicile of origin in Cyprus based on the provisions of the Wills and Succession Law (WSL) (i.e. domicile of the father at the time of birth), except for:

- i) an individual who has acquired and maintains a domicile of choice outside Cyprus based on the provisions of the WSL (i.e. factual concept - an individual permanently lives and intends to live in another country), provided that he/she has not been resident in Cyprus as defined in accordance with the provisions of the ITL for any period of at least 20 consecutive years prior to the relevant tax year, or
- ii) an individual who has not been resident in Cyprus as defined in accordance with the provisions of the ITL for a period of at least 20 consecutive years prior to the entry into force of the provisions of this Law.

It is provided that regardless of the domicile of origin, any individual who is resident in Cyprus, as defined in accordance with the provisions of the ITL for at least 17 out of the last 20 years prior to the relevant tax year, will be deemed domiciled in Cyprus for the purposes of this Law.

### **Anti-abuse measures**

Furthermore, the amended Law introduces an anti-abuse measure which provides that in the case where any person domiciled in Cyprus transfers assets to a relative up to third degree kindred who is



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not domiciled in Cyprus, and in the Commissioner's judgment the main purpose of the transfer was to avoid paying SDC, the income arising from these assets is subject to SDC.

### Effective Date

The above provisions have come into effect on 16 July 2015, which is the date they were published in the Official Gazette

### **AuditPro View**

*The new term is introduced in an effort to attract expatriates and high net worth individuals to reside in Cyprus. Under the "non-domicile" rules, Cyprus tax resident individuals who are not domiciled in Cyprus are exempt from SDC on dividend, interest and rental income. Hence, the amendment makes the holding of investments in dividend/interest earning assets e.g. shares, bonds by non-Cyprus domiciled individuals more attractive*

## Taxation of Dividends

An anti-abuse provision has been introduced in the SDC Law in relation to the taxation of dividends when these are paid to Cyprus resident companies beneficially owned indirectly by Cyprus resident and domiciled individual(s).

In case where actual dividend is received by a Cyprus company which is owned indirectly by Cyprus tax resident and domiciled individual(s) and the Commissioner considers that the interposition of this Cyprus company as a shareholder of the company paying the dividend does not serve any substantial commercial or economic purpose but is primarily intended to prevent, reduce or postpone the payment of SDC, the Commissioner may deem that the dividend is paid directly to the Cyprus tax resident and domiciled individual(s) who directly/indirectly control the Cyprus company receiving the dividend and require the payment of the SDC on the dividend either from the Cyprus company receiving the dividend or from the Cyprus tax resident individual(s) who directly/indirectly control the Cyprus company.

### Effective Date

The above provisions have come into effect on 16 July 2015, which is the date they were published in the Official Gazette

### **AuditPro View**

*The anti-avoidance measure has been introduced to guard against possible abuse of the deemed distribution provisions by Cyprus resident and domiciled individuals. It does not affect Cyprus resident companies owned directly or indirectly by non-resident or non-domiciled shareholders.*

## CAPITAL GAINS TAX LAW

### Exemption from Capital Gains Tax on Immovable Property acquired until 31<sup>st</sup> December 2016

The Capital Gains Tax (CGT) Law has been amended to provide that gains from the disposal of immovable property consisting of land or land and buildings are exempt from CGT, provided that:

- i. It is acquired from the date the amended Law comes into effect (16 July 2015) until 31 December 2016.
- ii. It is acquired through purchase or purchase agreement and not through an exchange or donation, at market value, from a non-related party.



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This exemption does not apply to disposals of immovable property that has been acquired under foreclosure procedures.

### Effective Date

The above provisions have come into effect on 16 July 2015, which is the date they were published in the Official Gazette

### **AuditPro View**

*This amendment aims to revive the Cyprus immovable property market and it does not apply to the disposal of share in companies that own immovable property.*

## DEPARTMENT OF LANDS AND SURVEYS (LEVY AND DUTIES) LAW

### Reduction in Immovable Property Transfer Fees & Lease/Sublease registration fees

As per the amended Law, for any transfer of immovable property as well as the registration of any lease/sublease until 31 December 2016, a 50% reduction in immovable property transfer fees and lease/sublease registration fees is provided.

The above reduction does not apply to transfers of immovable property that have been acquired under foreclosure procedures.

### Abolition of Levy Refunds

The amended Law has abolished the provisions by which the Commissioner refunded after five years from the day of transfer the amount of levy imposed and collected:

- on transfers of immovable property from a partnership to a company having as sole shareholders the partners of the assignor partnership.
- on transfers of immovable property to a (family) company by an individual shareholder of the company or his/her close relatives (i.e. spouse or relatives up to third degree kindred).

### Abolition of Special Levies on Transfers from a Company to relatives of the shareholders

According to the amendment to the Law, the special levies imposed on transfers of immovable property from a company to relatives of up to third degree of kindred of the shareholders are abolished and such transfers are now subject to the normal rates of levy on the values of the immovable property.

### Effective Date

The above provisions have come into effect on 16 July 2015, which is the date they were published in the Official Gazette.

### **AuditPro View**

*These amendments aims to revive the Cyprus immovable property market by providing a further reduction in the transfer fees. It is worth noting that the 50% exemption on the transfer of property subject to VAT continues to apply and as a result there may be instances where the transfer of an immovable property can be affected without any transfer fees if the transfer takes place during the above prescribed period.*