

*Cypriot tax
developments:
Cypriot answer to new
global challenges*

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Nicos Chimarides
Partner in charge of Direct Tax Services
PwC Cyprus

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What is the practical significance of the Protocol?



What is the practical significance of the Protocol?

- Removal of Cyprus from the Black List will be announced soon, in accordance with the agreed minutes of the negotiations
- Removal was agreed to be effective as from 1 January 2013

Therefore ...

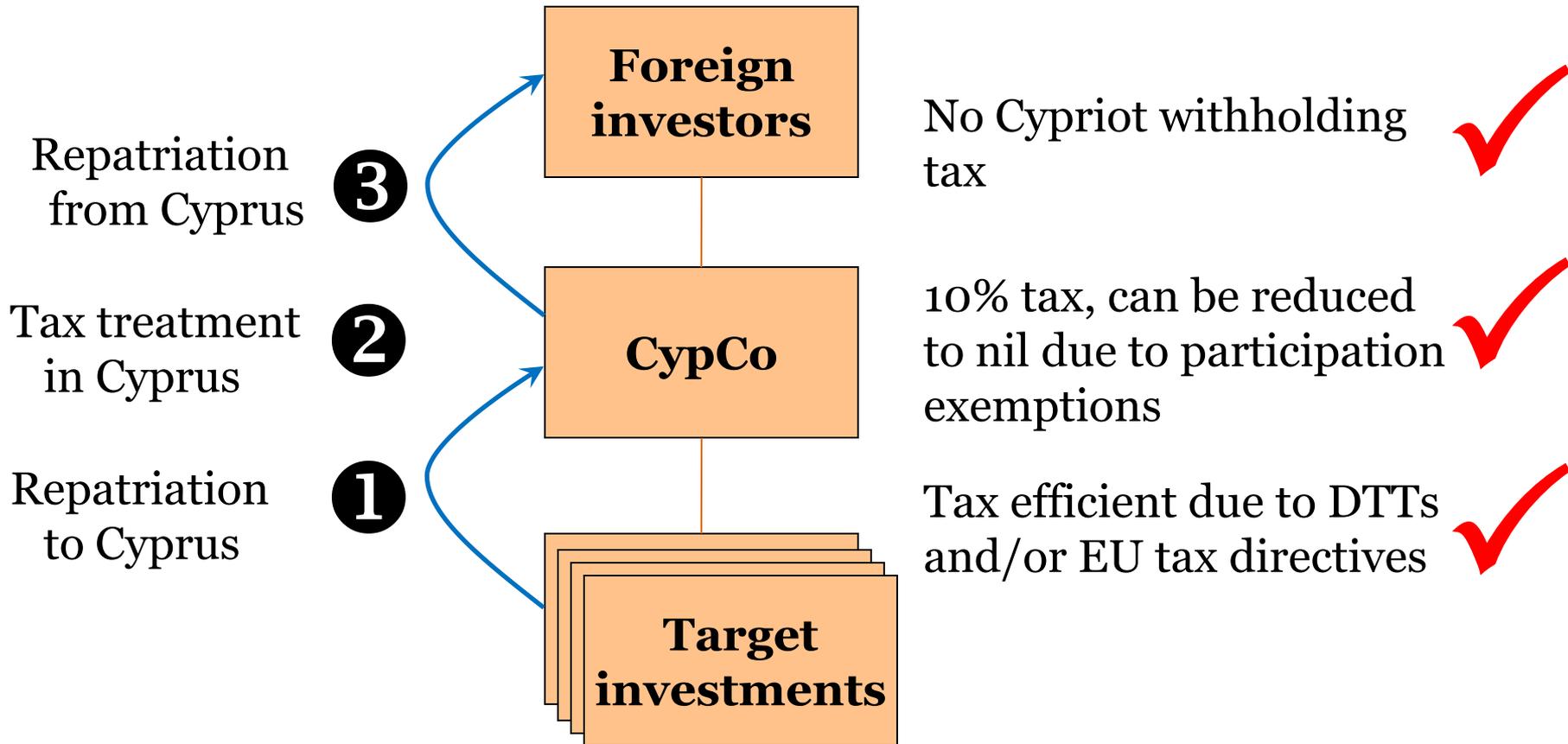
Practical significance of Protocol and removal from Black List:

1. Enables Cyprus to be used for **Russian outbound investments**. Dividends paid from Cyprus to Russian parent may now qualify for exemption in Russia (previously 9% tax in Russia). Result:
 - Cyprus used as gateway for Russian Companies into:
Africa - Asia - Europe
 - Access to global financial markets through Cypriot holding companies
 - ***Opportunities in Oil & Gas sector in Cyprus***
2. Eliminates pressure from Russian Transfer Pricing rule in relation to transactions between unrelated parties
3. Foreign Investments into Russia
 - The development of Cyprus as a Funds centre through the introduction of the EU Funds Directive

Protocols comparison

	Cyprus	Luxembourg	Switzerland
Dividend WHT	5% if direct investment of EUR 100k	5% if 10% holding requirement AND direct investment of EUR 80k	5% if 20% holding requirement AND direct investment of CHF 200k
Interest	0%	0%	0%
Royalty	0%	0%	0%
Capital Gains	Sale of shares “property-rich” companies taxed in both States BUT 4 year period exemption	Sale of shares “property-rich” companies taxed in both States with immediate effect	Sale of shares “property-rich” companies taxed in both States with immediate effect (excludes business assets)
Limitation of Benefits	Applicable ONLY in cases where companies are not incorporated in Cyprus	Applicable in ALL cases	Applicable in ALL cases

Main tax considerations



Domestic tax provisions comparison

	Cyprus	Luxembourg	Switzerland
Corporate Tax Rate	10%	28,8%	Can be 12,7% - 24,2% depending on location
Taxation of Dividends	exempt	exempt subject to conditions	exempt subject to conditions
Participation Threshold	none	10% or EUR 1,2 mln	10% or CHF 1 mln
Participation Period	none	12 months	none
Foreign Capital Gains	exempt	exempt subject to conditions	exempt subject to conditions
Trading in Securities	exempt	taxable	taxable
Dividend Withholding Tax to Non-Treaty Countries	none	15%	35%
Operational Costs	low	high (e.g. transfer pricing studies and rulings)	high (e.g. maintenance and rulings)

Conclusions

- ✓ Favourable withholding tax regime remains unaffected
- ✓ Cyprus remains No. 1 investor into Russia
- ✓ Will be removed from Russia's black list
- ✓ Cyprus regains its competitiveness for Russian outbound investments
- ✓ Protocol added more certainty

Cyprus domestic tax developments



Income Tax Law

“Exemptions” - Tax incentives to attract highly paid employees

50% of employment income **exempt** for five years if:

- ➔ remuneration is in excess of **€100k**
- ➔ employment starts after **1 January 2012**

Benefits:

- ▶ Top rate of personal tax reduced to 17.5%
- ▶ Effective rate can be lower than 10%
- ▶ Enhanced substance of Cypriot companies as decision-makers are encouraged to move to Cyprus

Income Tax Law

Interest-free loans to shareholders and directors

- As from 1 January 2012, imposition of notional interest at 9% per year in the hands of the company is abolished
- Loans to corporate shareholders: imposition at “market” rate
- Loans to individual shareholders/directors: benefit at 9% per annum assessed in the hands of individuals

Income Tax Law

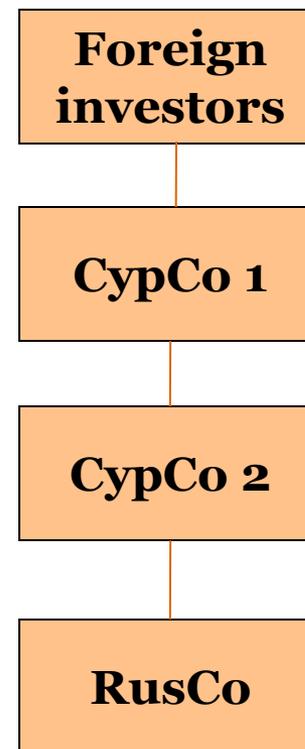
Availability of tax credit for tax suffered abroad on income taxable in Cyprus

- Tax credit available against Cypriot tax on same income
- Detailed rules and regulations have been issued
- Importance of evidence/ documentation duly supporting tax credit claims to be available.

Special Defence Contribution Law

The end of Deemed Dividend Distribution (“DDD”) for companies ultimately held by non-Cyprus tax residents

- Circular issued in September 2011 to clarify that the DDD provisions will no longer apply for groups ultimately held by non-Cyprus resident companies or individuals.
- Allows double or more tier Cyprus company structures to operate with less tax compliance burden.



Special Defence Contribution Law

DDD implications from capital reduction

As from 1 January 2011, DDD on capital reduction is now defined as the difference between any amounts paid to the shareholders and the amount of share capital that was originally invested. It only applies to shareholders who are individuals resident in Cyprus.

Significance:

No DDD obligation as a result of a capital reduction for the benefit of corporate shareholders.

Current and future trends



Current and future trends

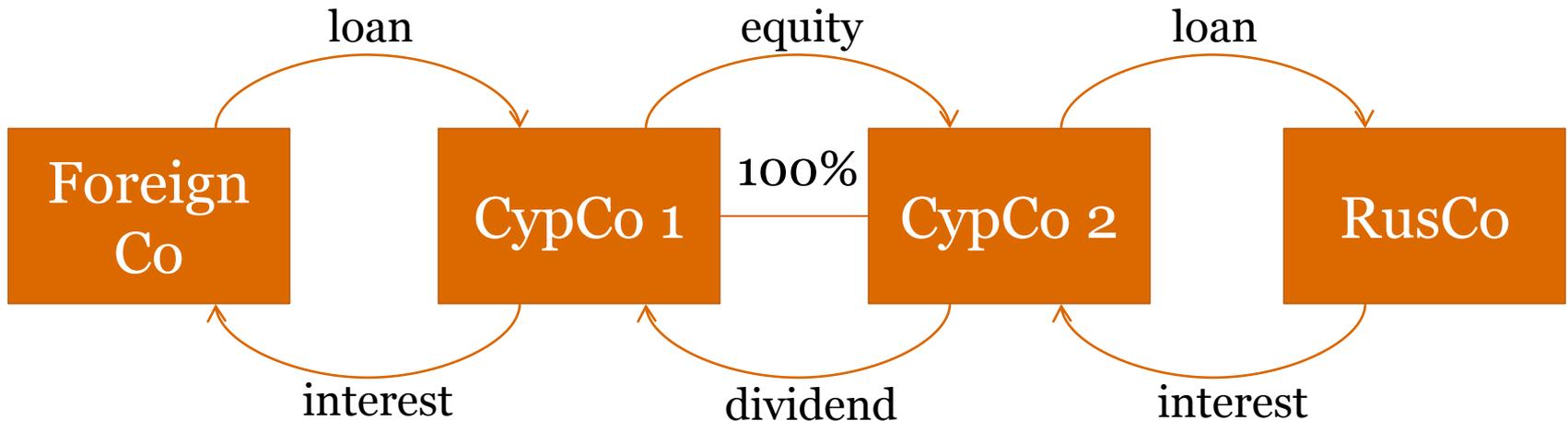
Improved rules on deductibility of interest

- Interest expense incurred by a Cypriot tax resident company to finance an equity investment into 100% subsidiary, will be treated as tax deductible provided that the subsidiary invests in **business assets**.
- If the subsidiary also invests in non-business assets, the interest expense incurred by the parent company will be treated as non-tax deductible on a pro-rata basis.
- Loans to related parties are considered **business assets**.



Current and future trends

Deductibility of interest – example:



- ➔ CypCo 1 may transfer tax loss to CypCo 2
- ➔ CypCo 2 taxed on “spread”
- ➔ CypCo 2 is adequately capitalised for Russian tax purposes

Current and future trends

Intellectual Property regime

- ▶ 80% exemption from tax on:
 - Net royalty income from intellectual property
 - Net gains on disposal of intellectual property

realised by Cypriot tax resident companies

Current and future trends

Yacht scheme

- ▶ Cyprus becomes the most attractive jurisdiction in the EU for yacht registration
- ▶ The effective VAT rate for yacht registration in the EU can be reduced to as low as 3.4% through the use of the Yacht Leasing Scheme.
- ▶ The total profit from the leasing agreement which amounts to 10% on the initial value of the yacht, will be subject to Income Tax at the rate of 10%.

Current and future trends

Mutual Funds

- Governed by the ‘Open-ended Undertakings for Collective Investment in Transferable Securities (UCITS) and related issues Law’
- Under the supervision of the CySEC
- Can take the form of Mutual Funds or Variable Capital Investment Companies
- Common Funds can only be created by a Management Company
- Variable Capital Investment Companies can be self managed under certain strict conditions
- Min. capital for Management Companies is €770k and for UCITS €1.7m
- Investment restrictions as per UCITS Directive
- Requires a local depositary (custodian)
- Approval process 2 to 6 months

Current and future trends

Mutual Funds

Opportunities:

- ▶ The ability of a Management Company to manage UCITS Funds in/from another European Union country
- ▶ The creation of Umbrella funds and Master / Feeder structures
- ▶ Set up of Capital guaranteed funds
- ▶ Listing of shares / units on a stock exchange

Current and future trends

Draft legislation enabling the use of cell companies:

- ▶ One legal entity – the company
- ▶ The company can have different cells
- ▶ Each cell treated as different tax payer and files own tax return
- ▶ Income / assets of each cell protected from other cells – ie no legal claim against one cell for liabilities of another cell
- ▶ Can be of specific use to mutual funds and insurance companies which have investors with different risk profiles and wish to invest in specific investments.

Thank you!

Nicos Chimarides

PwC, Nicosia, Cyprus

Tel: +357 22 555270

Mob.:+357 99 406464

e-mail: nicos.chimarides@cy.pwc.com

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