Tax Insights

from Tax Advisory Services

Cyprus and India sign new double tax treaty (DTT)

Issue N-14-2016, 28 November 2016

In brief

Cyprus and India signed a new DTT and accompanying Protocol on 18 November 2016 opening the way for new investment opportunities and further development in trade relations between the two States. Cyprus subsequently ratified the new DTT on 25 November 2016. The new DTT is yet to be published in India in its Official Gazette.

The new DTT will take effect in Cyprus from the next 1 January and in India from the next 1 April, following the date of its entry into force. India's Government announced on 18 November 2016 that the new DTT is expected to come into effect in India as from 1 April 2017. Once it comes into effect the new DTT will replace the existing DTT.

The withholding tax rate provided for in the new DTT is 10% on dividends, interest, royalties and fees for technical services. The Protocol clarifies that India due to its domestic law will not currently levy the 10% withholding tax on dividends provided for in the new DTT.

The new DTT includes provisions for source based taxation for capital gains from the disposal of shares in certain cases, with the Protocol including a "grandfathering" provision for investments acquired prior to 1 April 2017, where the exclusive taxing rights will remain with the State of the seller.

Upon signing the new DTT the Cyprus Government announced that following its entering into force the Indian Authorities will proceed with rescinding the classification of Cyprus as a 'Notified Jurisdictional Area' with retroactive effect as from 1 of November 2013 (this was already announced by Cyprus in June 2016).

In detail

Cyprus and India signed a new DTT and accompanying Protocol on 18 November 2016 opening the way for new investment opportunities and further development in trade relations between the two States. Cyprus subsequently ratified the new DTT on 25 November 2016. The new DTT is yet to be published in India in its Official Gazette.

The new DTT will take effect in Cyprus from the next 1 January and in India from the next 1 April, following the date of its entry into force. India's Government announced on 18 November 2016 that the new DTT is expected to come into effect in India as from 1 April 2017. Once it comes into effect the new DTT will replace the existing DTT.

The new DTT provides for a 10% withholding tax rate on dividends. The Protocol clarifies that as regards India this rate is not currently applicable as per Indian domestic law India does not impose withholding tax on dividends paid by Indian companies to its shareholders.

A 10% withholding tax rate also applies on interest, royalties and fees for technical services with the exception of interest in those cases where the beneficial owner of the interest is:

- ❖ The government, a political sub-division or a local authority of the other Contracting State; or
- ❖ In the case of India, the Reserve Bank of India, the Export-Import Bank of India, the National Housing Bank; and
- ❖ Any other institution as may be agreed upon from time to time between the competent authorities of Cyprus and India through exchange of letters;

in such cases no withholding tax applies.

The new DTT provides for source based taxation for capital gains from the disposal of shares in the following cases:

- Shares of a resident of the source State; or
- Shares of a company the property of which consists directly or indirectly principally of immovable property situated in the source State.

Importantly, the Protocol provides a "grandfathering" clause for investments in shares acquired prior to 1 April 2017 where it has been agreed that the taxation of a future disposal of such shares remains exclusively with the State of residence of the seller.

Upon signing the new DTT the Cyprus Government announced, as it had done in its earlier June 2016 announcement, that following the entering into force of the new DTT the Indian Authorities will proceed with rescinding the classification of Cyprus as a 'Notified Jurisdictional Area' ('NJA') with retroactive effect as from 1 of November 2013 (i.e. the date on which Cyprus was previously classified as a NJA by the Indian Authorities).

The takeaway

The grandfathering of investments in shares acquired prior to 1 April 2017 is a welcome development and provides clarity to taxpayers holding existing investments. In cases where a Cyprus tax resident is the seller of such grandfathered investments, under the new DTT the exclusive taxing rights on gains realised will remain with Cyprus, as is the case with the existing DTT currently in force between the two States.

The announcement by the Cyprus Government that, following the entering into force of the new DTT the Indian Authorities will proceed with rescinding the classification of Cyprus as a NJA with retroactive effect as from 1 of November 2013, is also a welcome development. Being a NJA results in a mandatory levy of withholding tax in India and application of Indian transfer pricing provisions to transactions with Cyprus tax residents. The rescinding of the notification will remove such additional burden. Further, taxpayers that have suffered the mandatory levy of withholding tax in India should consider making applications for refunds.

Irrespective of the withholding taxes provided for in this new DTT on dividends and interest, as per the domestic Cyprus tax legislation there is no Cyprus withholding tax on payments of dividends and interest to non-Cyprus tax residents.

Further, irrespective of the withholding taxes provided for in this new DTT on royalties and fees for technical services, as per the Cyprus domestic tax legislation Cyprus only applies withholding tax on such payments to non-Cyprus tax residents where the royalties/fees relate to rights or activities used/performed within Cyprus.

Let's talk

For a deeper discussion of how this development might affect you or your business, please contact:

Theo C Parperis
Partner
Head of Tax & Legal
theo.parperis@cy.pwc.com

Marios S Andreou
Partner
In charge of Tax Advisory
marios.andreou@cy.pwc.com

Nicos P Chimarides
Partner
In charge of Corporate Compliance
nicos.chimarides@cy.pwc.com

Eftychios G Eftychiou
Partner
Head of Tax Technical Committee
eftychios.eftychiou@cy.pwc.com

Or your usual PwC contact

PwC Cyprus
PwC Central
43 Demostheni Severi Avenue
CY-1080 Nicosia, Cyprus
P O Box 21612
CY-1591 Nicosia, Cyprus

www.pwc.com.cy