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Bills for prevention of international tax abuse voted by the Cyprus Parliament

In brief

On 9 December 2021, the Cyprus Parliament voted to pass into law two bills for amending the Cyprus tax legislation, with the purpose of strengthening the Cyprus tax framework for the prevention of tax abuse, tax evasion and tax avoidance (the “bills”).

Each of the bills state that they will enter into force on 31 December 2022. They contain the following developments:

- For payments from Cyprus to companies in jurisdictions in the EU ‘blacklist’ (i.e. companies in jurisdictions included in Annex I of the EU list of non-cooperative jurisdictions for tax purposes), withholding taxes (WHTs) are introduced (or, in the case of royalties, expanded) as follows:
 - for payments of dividends by non-quoted companies, WHT at the rate of 17%, to shareholders with an “over 50% holding”;
 - for payments of passive interest (excluding payments by individuals), WHT at the rate of 30%;
 - for payments of royalties and similar type payments (excluding payments by individuals), WHT at the rate of 10%.
- The Cyprus corporate tax residency test (currently the ‘management and control’ test) is expanded with the introduction of a test based on incorporation/registration in Cyprus, for companies that do not have a tax residency anywhere else in the world.

The bills will need to be published in the Government’s Gazette in order to complete the legal process of being passed into law.

In detail

The comments below on these developments are subject to the final text which is yet to be published in the Cyprus Government Gazette.

1. WHTs for payments to companies in EU blacklisted jurisdictions.

(i) Status of the recipient:

For the newly-introduced WHTs to be triggered, the direct recipient of the dividends, interest and royalties should be a company in an EU blacklisted jurisdiction; that is:

- a company tax resident in an EU blacklisted jurisdiction; or
- a company incorporated / registered in an EU blacklisted jurisdiction and which is not tax resident in a non EU blacklisted jurisdiction.

(ii) Dividends

A WHT at the rate of 17% is introduced in the Special Defence Contribution Law ("SDC Law") for dividends paid by Cyprus tax resident companies to companies in EU blacklisted jurisdictions (refer to (i) above), where the direct recipient holds directly more than 50% of the capital, votes or entitlement to profit (an "over 50% holding") in the Cyprus company paying the dividends.

The above mentioned WHT does not apply in the case of dividend payments on shares which are quoted on a recognised stock exchange.

The "over 50% holding" is also met when the company receiving the dividend participates directly in the Cyprus paying company jointly with associated companies, which are also in EU blacklisted jurisdictions and that also participate directly in the Cyprus paying company, and the combined holding of the associated companies is over 50%.

(iii) Interest

A WHT at the rate of 30% is introduced in the SDC Law for passive interest paid from Cyprus sources to companies in EU blacklisted jurisdictions (refer to (i) above).

Payments of passive interest by individuals are explicitly excluded from the scope of the above. Also excluded from the scope of the above are interest payments on instruments (e.g. bonds) quoted on a recognised stock exchange.

(iv) Royalties

The WHT at the rate of 10% on royalties and similar type payments in the Income Tax Law ("IT Law"), which is currently applicable to royalties and similar type payments only under certain conditions, is expanded to cover royalties and similar type payments from Cyprus sources to companies in EU blacklisted jurisdictions (refer to (i) above), with the exception of payments by individuals.

2. Additional Cyprus corporate tax residency test

Currently companies that are "managed and controlled" from Cyprus are tax residents of Cyprus, as per the IT Law. The new addition introduced in the IT Law by the bill does not impact this rule and it will remain the case that such companies are tax residents of Cyprus.

The bill relates to companies which are incorporated / registered in Cyprus and which are "managed and controlled" from outside Cyprus. With this new additional Cyprus corporate tax residency test, such companies will be considered as tax residents of Cyprus provided they are not tax residents of any other jurisdiction.

The takeaway

These bills are a strong indication of Cyprus' willingness to prevent international tax abuse, tax evasion and tax avoidance.

The Cyprus Ministry of Finance, in comments accompanying the bills, notes that the bills are in line with recent EU Country-Specific Recommendations (CSRs) for Cyprus and with the EU guidelines for defensive tax measures to be adopted by EU Member States towards EU blacklisted jurisdictions. The bills were also referred to in the Cyprus Recovery and Resilience Plan (refer to our newsletter [N-22-2021](#))

The EU plans to update the list of EU blacklisted jurisdictions up to two times per year. The current list comprises: American Samoa, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, US Virgin Islands and Vanuatu.

The bills do not indicate the effective date of application of Cyprus WHTs to jurisdictions added to each new version of the EU blacklist, or the effective date of disapplication of Cyprus WHTs to jurisdictions removed from each new version of the EU blacklist. It is expected that this and other matters (e.g. application of the Cyprus WHTs on a cash basis vs accruals basis, etc) will be clarified by the Cyprus authorities in the near future.

Taxpayers should evaluate how this may affect their existing and new structures as well as their business in advance of the 31 December 2022 entry into force.

Let's Talk

For a deeper discussion of how this issue might affect your business, please contact:

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