

Cyprus Tax Alert

Amendments to the Cyprus Taxation Laws

Introduction

The Cyprus Parliament on the 22 October 2009 has enacted amendments to the Cyprus taxation Laws, in particular the Income Tax Law and the Special Contribution for Defence of the Republic Law ("SDC"), mainly aimed at making Cyprus an even more attractive place for foreign investors.

The enacted amendments facilitate the setting up and operation of collective investment schemes in Cyprus, and also provide clarity and certainty in respect of taxation of interest and of dividends received from abroad.

The amendments come into force immediately with retroactive effect to 1 January 2009.

**"Cyprus
more
attractive to
portfolio
investors"**

**"Retroactive
effect to**

1 January 2009"

Dividend Income

The Special Contribution for Defence Law has been amended in order to abolish the minimum participation requirement of 1% when it relates to dividends received from abroad by a Cyprus tax resident Company.

Before these changes, the dividend income was subject to a 15% SDC if a minimum 1% holding in the payer company was not maintained, regardless of whether other exemption criteria were met.

This change facilitates portfolio investors to benefit from the dividend participation exemption.

Consequently, under the new requirement a company resident in Cyprus which receives dividends from a company which is not resident in Cyprus, shall be exempt from the payment of any taxes on such dividends.

Contact Us

Address:

*Centaur House
2 Apostolos Varnavas
2571 Nisou, Nicosia,
Cyprus*

*Tel: +357 22 499 994
Fax: +357 22 499 984*

Email:

cyprus@centaurtrust.com

Website:

www.centaurtrust.com

For further information, please contact:

Demetris Papaprodromou
Managing Director

demetris@centaurtrust.com

**"1%
minimum
participation
Abolished"**

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The dividend exemption does not apply if:

- the company paying the dividend engages directly or indirectly more than fifty per cent (50%) in activities which lead to investment income;
- AND
- the foreign tax burden on the income of the company paying the dividend is substantially lower than the tax burden of the company which is resident in Cyprus (not official but generally accepted that substantially lower means lower than 5%).

Interest Income

Before the amendments to the Income tax law, the entire interest income of an individual and 50% interest income of a company was exempted from income tax .

**“Interest Income
for companies
exempt from
Income Tax”**

**“Uniform
treatment natural
and legal persons”**

The Cyprus Income Tax Law has been amended abolishing the existing rules on taxation of interest income and introducing a uniform treatment in relation to the taxation of interest income derived by individuals and legal persons.

Thus, sub-section 19 of Section 8 has been replaced by a new sub-section 19 which exempts interest income from income tax, whether it is earned by an individual or by a company.

Interest received by a company in the ordinary course of its business including interest closely connected to the ordinary course of business is taxed under income tax law after deducting expenses at the standard corporation tax rate of 10%.

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Collective Investment Schemes— (CIS)

Cyprus Tax Laws have been amended to provide further tax incentives for the set up and operation of Collective Investment Schemes.

Disposal of Securities

The whole profit from the sale of “securities” is exempt from income tax. Securities as defined in the income tax law include among others shares, bonds, debentures, and any warrants or options on them.

The Cyprus Income Tax Law has been amended by the addition thereto of a provision which reads as follows: “Provided that the redemption of a participation or share in a collective investment scheme of open or closed type, constitutes disposal of security.”

Therefore, profits derived on the disposal of a unit in a collective investment scheme will be exempt from tax in Cyprus.

“Redemption of Units – No tax implications”

“Profits on the sale of units – Exempt from tax”

Redemption of Securities

The redemption of a unit holding in a collective investment scheme does not constitute a reduction of capital under the Deemed Distribution provisions of the Special Contribution for Defence Law (SCD) and, therefore, there will not be any tax implications on the distribution arising from the redemption.

Interest Income

Interest income derived by a CIS is considered to be “active” interest income and taxed only at 10% corporate income tax (less expenses).

The Special Contribution for Defence Law has been amended accordingly to make clear that interest derived by a CIS is not considered to be interest for SCD purposes and therefore is not subject to Defence tax.

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Deemed Dividend Distribution

Collective Investment Schemes will be subject a 3% taxation under the SDC Law (instead of the normal 15%) in the event that the scheme fails to distribute at least 70% of its accounting profits within a period of two years from the tax year to which the profits relate, to the extent that the CIS has Cyprus tax resident unit holders.

The above taxation on Deemed Dividend Distribution is not applicable in the event where the unit holders of the CIS are not tax residents in Cyprus.

**“Foreign Unit holders
of a CIS**

**No Tax on Liquidation
of the CIS”**

Liquidation of CIS

On liquidation of a CIS, the proceeds will be subject to tax under the Special Contribution for Defence Law at the rate of 3% but exempt in the case where the unit holders are not tax residents of Cyprus.

**“Foreign Unit holders
of a CIS**

**Deemed distribution
provisions do not
apply”**

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