

The Cyprus Finance Company



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Preface

The tax law of Cyprus, as reformed, is probably the most modern, effective and simple tax system in the EU. The Cyprus tax legislation is fully compliant with the EU Acquis Communautaire and EU Directives.

It is in full compliance with the code of Conduct for Business Taxation and against harmful tax competition. As of April 2009, Cyprus proudly features on the White list of the OECD.

Opportunities to reduce the burden of income tax are numerous, for individuals as well as for domestic and international businesses. The full acceptance by Cyprus of the European Union Code of Conduct and the Campaign against Harmful Tax Competition has added a lot to the reputation of Cyprus, as having a very competitive but internationally respected tax legislation.

The strategic position of Cyprus, connecting Europe, Middle East and Asia naturally make the island a hub for business and trade. Cyprus has gained an enviable position in the international financial arena, mainly due to its good reputation as an international business centre with an experience of over 35 years, with highly skilled and multilingual qualified professionals, sophisticated infrastructure, and transparent legal system based on UK common law.

Cyprus is a member state of the EU since May 2004, has adopted the Euro as its official currency since 2008, and is a country with a strategic location, long history and culture, as well as nice weather with almost year-round sunshine.

All the above positive arguments have created excellent opportunities for tax professionals to establish Cyprus as a major financial centre within the European Union, developing Cyprus from an alleged tax haven country into a Country that has a modern and competitive tax environment.

At Centaur Trust our client-focused and service based mind-set, along with our unprecedented depth of client insight, enables us to enhance the quality and consistency of services offered to our clients.

Our integrated, client-focused approach basically combines insight and innovation from multiple disciplines;

- Corporate Legal
- Tax & VAT
- Accounting & Financial Reporting
- Banking
- IT
- Secretarial
- Fiduciary
- Compliance
- Human Capital

Our aim is to gain detailed business and client industry knowledge, recognise the specific needs of our clients and then try to find and create practical solutions for specific administrative, regulatory, compliance and other corporate processes. By streamlining key processes, we aim to work together with our clients so as to be in a position to generate and maintain the kind of ordered, accurate, consistent and timely financial and non-financial data about all aspects of their business that will enable them to optimise their business performance.



Demetris Papaprodromou (BA, MSc, FCA)
Managing Director



Introduction

Tax considerations may not be the decisive factor in choosing to set up a group finance company in a particular jurisdiction. There are instances where the non-tax considerations may outweigh the tax considerations of an international group in choosing the location of its group finance company.

Some non-tax considerations may include among others:

- Company law requirements
- Political stability and stable economic infrastructure
- Banking stability and presence of international reputable banks
- Availability of human resources
- Telecommunication capabilities
- Set-up and other administration costs
- Spoken language, time zone and location

This publication aims to discuss only the major tax considerations that an international group should take into account in choosing the location of its group finance company.



Group Finance Company Location

Historically group finance companies have been in existence for various commercial reasons, but mainly for reasons of tax and legal convenience. A group finance company is used primarily to provide loans to other companies within the same group. The activities of a Cyprus finance company primarily consist of providing loans to group companies, subsidiaries, associate companies or shareholders. Whilst the function of a group finance company would typically comprise of certain licensable activities such as the business of lending, an exemption from the above mentioned licensing requirement would be applicable insofar as the financing activities are carried out solely with companies which belong to the same group of companies or the parties are closely connected business associates with the finance company and which are not banks or financial institutions.

A Cyprus finance company has virtually no limitations with regards to the types of activities which may be carried out. The finance activities can be combined with holding activities, royalty activities or actual operating activities, like trading or manufacturing. The centralization of activities in a Cyprus finance company will make the structure as a whole more robust and resistant to the international tendency to deny tax advantages to purely tax driven vehicles.

The operations of a Cyprus group finance company constitute a trade for Cyprus tax purposes and the determination of its taxable profits would be established according to the relevant rules applicable to trading activities. Different types of finance companies are used to attain a variety of fiscal and non-fiscal objectives, but mainly for:

- Day to day control of cash and bank accounts, including cash pooling
- Provision of intra-group loans.
- Centralisation of the group treasury and funding operations
- Pulling out operating profits by way of interest deductions
- Locating financing income in a tax efficient jurisdiction
- Implementation of better sheltering of profits and repatriation strategies
 - Tax efficient repatriation of funds to the shareholders owners
 - Establish tax efficient structures for the shareholders themselves as well as for the whole group of companies in general;

Throughout the world the barriers to capital movements are fast disappearing. Tax differences have become a very significant factor in commercial decisions, and therefore investment structures which have the least tax leakage are preferred by investors.

During the last decade various European Countries have introduced group finance regimes and nowadays it is very difficult for a multinational group to select the right jurisdiction in which to establish their finance company.

A multinational group, in choosing a suitable group finance company jurisdiction, should give consideration to a number of tax considerations. Even though tax considerations may not be the decisive factor in choosing to set up a group finance company in a particular jurisdiction, tax costs play a significant role.



The Cyprus Limited Liability Company

The law relating to registered companies is the Cypriot Companies Law, Chapter 113 of the laws of Cyprus, as amended (The Companies Law), which is almost identical to the United Kingdom's former Companies Act 1948, but several amendments have been made due to Cyprus accession to the EU.

Section 29 of the Companies Law defines a private company as:

“A private company means a company which by its articles of association specifically:

- Restricts the right to transfer its shares.
- Limits the number of its members to 50.
- Prohibits any invitation to the public to subscribe for its shares or debentures.

Incorporation and capacity to contract

The type of company that is adopted almost exclusively by foreign investors who are interested in creating a Cyprus registered company is the private Company limited by shares. A Cyprus Limited Liability Company comes into existence as a legal entity as soon as it is incorporated by the Registrar of Companies. This is evidenced by the Registrar issuing a Certificate of Incorporation that is conclusive evidence that the company has satisfied all legal requirements in respect of incorporation and that the company is duly registered under the Companies Law.

When a Cyprus company is formed, the memorandum of association will state:

- the amount of share capital the company will have; and
- the division of the share capital into shares of a fixed amount.

The usual timeframe for the registration of a Cyprus private Company limited by shares, is a period of about five working days.

Authorised & Issued Share Capital

The amount of share capital stated in the memorandum of association is the company's 'authorised' capital. The amount of the authorised capital in itself is of no importance as an indication of creditworthiness. All that it shows is the maximum number of shares that the company can issue.

There is no maximum authorised share capital and no minimum share capital for Cyprus private limited companies. The authorised share capital can be denominated in any of the main currencies, though the default currency is the Euro. There is no requirement that the fixed amount of each share should be as a minimum of Euro1,00, consequently any subdivisions of the Euro are possible for the minimum fixed value of a share.

The number of shares from the authorised share capital that have been issued to shareholders is the issued share capital. The amount of issued capital cannot exceed the amount of the authorised capital and there is no requirement on companies to issue all their authorised share capital. Thus a Cyprus limited company can be established with only Euro1,00 as issued share capital.

Payment for shares

The law does not require that full payment should be made on the allotment of shares.

Nor does it require that payment should be made wholly in cash. As a result, payment for shares can take the form of goods, services, property, good will, know-how, or even shares in another company. The latter is often used when one company takes over another.

In summary shares may be allotted for payment in any of the following ways:

- 100% for cash;
- Partly for cash and partly for a non-cash payment; or
- 100% for a non-cash payment

Shareholders

A Cyprus company limited by shares must have at least one registered shareholder that can be an individual or a legally incorporated entity (local or foreign corporations, trusts, foundations).



Directors

A Cyprus company limited by shares must have a director and a director can be an individual or a legally incorporated entity.

The sole director of the company cannot also be the secretary of the company. However, this restriction is not applicable to single member private limited liability companies. Thus the sole member can also act and as the sole director as well as the secretary of the company.

Residency status of a director

The law does not require that directors of Cyprus private limited companies should be Cyprus nationals. On the contrary, irrespective of the country of residency and on whether it is an individual or a legally incorporated entity, anyone can be appointed as a director of a Cyprus company. Even though for legal purposes the residency status of a director is not important, for tax purposes it is quite important.

Cyprus companies are not automatically deemed to be tax resident in Cyprus by virtue of incorporation alone. Rather, in determining the tax residence status of a Cyprus company, the tax authorities will consider such criteria as the location of the Central Management & Control of the company. Therefore, for a Cyprus company to be considered as tax resident in Cyprus, it is strongly suggested for the majority of the board of directors to be residents of Cyprus.

Secretary

A Cyprus company limited by shares must have a secretary and a secretary can be an individual or a legally incorporated entity.

Registered office

A Cyprus company limited by shares must have a registered office in the Republic of Cyprus to which all communications, writs and notices can be served upon the Company.



Tax Considerations

The major tax considerations that a multinational group should take into account in choosing a suitable finance company jurisdiction should include the following:

- Tax regime with regards to withholding taxes on outward interest payments
- Tax regime with regards to the tax deduction of interest payments
- Tax regime with regards to the extraction of interest payments from other group companies
- Back to back inter-group loans
 - Tax regime with regards to the tax treatment of interest receivable
 - Tax regime with regards to the net taxable interest margin required by the tax authorities and the availability of pre-transaction rulings
- Substance requirements and the beneficial ownership clause
- Notional Interest Deduction on New Capital
- Other significant tax considerations
 - Tax treatment of capital gains from the disposal of shares in participation holdings
 - Tax treatment of outward dividends
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 - Extraction of dividends from subsidiary companies
 - Controlled Foreign Companies (CFC) Rules
 - Thin Capitalisation Rules
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 - Tax Losses
 - Group Relief
 - Tax Credit for foreign tax paid
 - Stamp Duty
 - Capital Duty
 - Re-Domiciliation of Companies
 - Re-organisation rules
 - EU Interest and Royalties Directive
 - Tax Treatment of Liquidation Proceeds
 - Transfer pricing
 - VAT
- Double Tax Treaties

A photograph showing three business professionals in a meeting. A woman in a grey blazer is writing in a notebook. A man in a dark suit is holding a large white document. Another man in a light blue shirt is also holding a document. They are seated at a dark table with several notebooks and pens.

Tax regime with regards to withholding taxes on outward interest payments

If a Cyprus Finance company is financed in the form of loans by its non-resident parent company, or by its non-resident individual shareholder, it will make the interest payments to the non-resident individual or company gross, without any tax deducted.

The 0% withholding tax rate applies irrespective of the existence or not of any double tax treaties or on whether the individual or the parent company is located in an offshore jurisdiction or not.

Non-Domicile Status

In a recent amendment to the Special Defence Contribution (the 'SDC') law, the term "domicile" was introduced. A Cyprus tax resident who is not domiciled in Cyprus and who obtains non-domiciled tax status will not be subject to SDC on any interest, rental income or dividends received (actual or deemed). Unlike other jurisdictions offering non-domiciled status, the treatment applies also to income derived from sources within Cyprus, regardless of whether such income is remitted in Cyprus or not.

An individual is not domiciled in the Republic of Cyprus if:

- An individual doesn't have domicile of origin in Cyprus; and
- The individual was Cyprus tax resident for less than 17 out of the last 20 years before the relevant tax year



Tax regime with regards to the tax deduction of interest payments

In general, interest payments by a Cypriot company on borrowings are fully tax deductible.

However, any interest payable by the Cyprus finance company that was not incurred for the purpose of the production of income will not be tax deductible.

Under normal circumstances, if a Cyprus company pays interest in order to finance its trading activities, such interest is a tax deductible expense. However, as an example, if a Cyprus finance company borrows money from its shareholder at an interest rate of 5%, but advances the money to its subsidiary free of any interest, then this interest payable will not be a tax deductible expense, as it was not incurred for the purpose of the production of income.



Tax regime with regards to the extraction of interest payments from other group companies with low or no-withholding taxes

A Cyprus holding company can achieve low or zero withholding tax rates when extracting interest payments from other group companies with low or no-withholding taxes, by relying either on its extensive double tax treaty network, or on the EU Interest & Royalties Directive that Cyprus has transposed into Cypriot Law.

Extraction of Interest payments from EU-countries

Cyprus has transposed into Cypriot Law the EU Interest & Royalties directive. Cyprus companies are eligible EU-Companies under the directive and thus if the loan provided by the Cyprus finance company is to a company in another member state and provided all conditions of the EU Interest & Royalties directive are met, the incidence of withholding tax is eliminated altogether. On the basis of the Directive, a 0% withholding tax rate applies for qualifying interest payments (or royalties payments) between qualifying associated corporations established in the EU. A corporation is considered associated if it has cross holdings of at least 25% or a third corporation has a direct minimum holding of 25% in two other EU corporations. The benefits of the Directive are only granted to companies which are:

- subject to corporate tax in the EU,
- tax resident in an EU Member State and
- of a type listed in the annex to the Directive.

Extraction of Interest payments from non EU-countries

Where the loan provided by the Cyprus finance company is to a company outside the EU, or where the conditions of the EU Interest & Royalties Directive are not met, Cyprus can rely on its extensive network of double tax treaties, the rates of which, especially as far as Eastern European investments are concerned, are considered particularly advantageous. Appendix 1, shows the list of double tax treaties that Cyprus has enacted with third countries, as well as the corresponding rates of withholding tax.



Back-to-back loans: Tax regime with regards to the tax treatment of interest receivable

Interest Receivable – Main Trading Activity

Interest income “derived in the ordinary course of business”*, or interest income closely connected with the carrying on of a business**, is subject to tax normally, at the standard rate of 12,5%.

The 12,5% is not calculated on the total amount of interest received, but on the net profit (less interest payable and other deductible tax expenses).

*** Interest income derived from the ordinary course of business.**

Interest falling into this category can be classified as the interest that is earned by banks, finance companies, hire purchase companies etc.

**** Interest closely connected with the normal carrying on of a business.**

Interest falling into this category can be classified as the interest that is earned by:

- A company acting as a vehicle to finance other group companies.
- A company that is having trading debtors and is charging interest for late payment.
- A property developer receiving interest in the course of his business by extending the credit period given to his customers.
- An investment company that is earning interest on deposits until good investment opportunities arise.

Interest Receivable—Not Main Trading Activity

If interest income is neither considered to arise in the ordinary course of business nor is closely connected to the ordinary course of business, the gross amount of interest is subject to defence tax at 30%.



Back-to-back loans:

Tax regime with regards to the net taxable interest margin required by the tax authorities and the availability of pre-transaction rulings

A pre-transaction ruling in respect of a particular type of transaction serves to remove taxation uncertainties.

Cyprus has for some years now introduced an advance ruling practice in accordance with OECD recommendations.

The commissioner of Income Tax does provide advance interpretations of the law, when requested, concerning the tax consequences of proposed transactions.

Via its tax rulings division, the Commissioner of Income Tax will issue advance tax rulings regarding transactions (or series of transactions) proposed to be undertaken by new or existing companies, as well as for transactions relating to tax years for which the due date for filing a return has not yet passed. For example, ruling requests for transactions concluded in 2015 will be accepted up to March 31 2017, the statutory deadline for filing 2015 tax returns.

The issuance of pre-tax rulings confirming the acceptance of pre-approved interest margins (as shown on the table below) can remove the taxation uncertainty significantly.

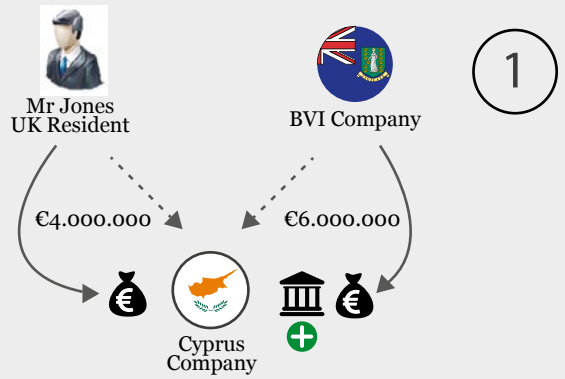
Loan Amount	Net Interest Margin
Up to €50 million	0,35%
Between €50 million - €200 million	0,25%
In excess of €200 million	0,125%

Flowchart 1, gives a diagrammatical example showing the tax treatment of back-to-back loans

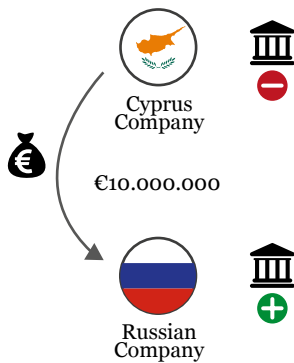
Flowchart 1 | Back To Back Loans

Loan Financing – Cyprus Company

- On 1/1/2015 the two shareholders of the Cyprus company gave a loan to the Cyprus company equal to €10.000.000. Mr Jones gave €4.000.000 and BVI Co gave €6.000.000.
- The interest rate on both loans was 8%.
- According to the terms of the loan agreement, repayment of the loan amount as well as the interest should be made at the end of 2015.



2



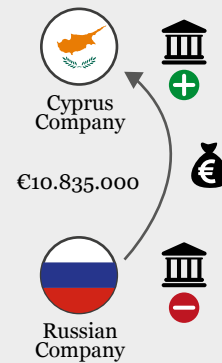
Loan Financing - Russian Company

- On 1/1/2015, the Cyprus company financed its Russian subsidiary company, with €10.000.000, under a loan agreement bearing an interest rate of 8.35%.
- According to the terms of the loan agreement, repayment of the loan amount as well as the interest should be made at the end of 2015.

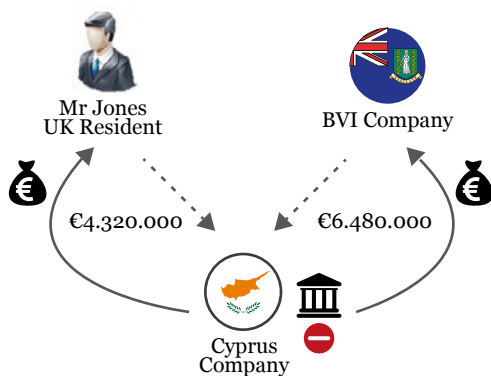
Loan Repayment- Russian Company

- The double tax treaty between Russia and Cyprus, imposes a withholding tax rate on interest payments from Russia to Cyprus of 0%.
- On 31/12/2015 the Russian Company pays €10.835.000 to the Cyprus company, being the loan amount together with the outstanding interest.

3



4



Loan Repayment – Cyprus Company

- Cypriot tax rules provide no withholding tax on interest payments made to non-residents of Cyprus. On 31/12/15, Mr Jones will receive €4.320.000 and BVI Co will receive €6.480.000, both receipts without any withholding tax deduction in the Cyprus company.

Tax Payable – Cyprus Company

Interest Receivable	€835.000
Interest Payable	€800.000
Net Profit	€35.000
Tax @ 12,5%	4.375

5



Substance requirements and the beneficial ownership clause

Real Economic Substance

Whenever an international group establishes structures where there would be a group finance company in a low tax jurisdiction and there would be subsidiary companies in the so called high tax countries, substance has become a crucial consideration.

Even in cases where a double tax treaty exists, current anti-abuse provisions require that the group finance company is not simply interposed, just for the purposes of avoiding withholding tax on interest payments in the countries where the subsidiaries are located. Over the last decade the international community has also become increasingly aware of the phenomenon of treaty shopping i.e. the use of conduit companies with the main purpose to benefit from the reduced withholding tax rates provided by tax treaties. Many countries have incorporated anti-abuse provisions in either their domestic tax legislation or in the tax treaties concluded with other countries, to counter the use of purely tax driven conduit companies.

In our experience and in accordance with the propositions made by most of the countries in their domestic tax legislation, a group finance company should operate from genuine offices, employ genuine staff in real financing activities.

The following factors are decisive in determining whether the company is involved in real economic operations in the country of residence

- The general finance policy of the company should be formulated in the country of residence. The place of effective management is generally understood to be the place where the Head Office is: the Head Office in the sense of - not the registered office - but the central directing source. That its major/important treasury decisions should be taken by the board in the country of residence.
- The appointed directors of the company should be fit to hold office or be employed in the administration of the Company's affairs. When appointing a board of directors, the individual members should be persons of high caliber, such as successful business men, Chartered and Certified accountants, lawyers, or persons with a relevant background in relation to the company's proposed activities. The directors should have the necessary knowledge and expertise to really understand and know the business activities of the company and they should actually be part of the strategic treasury decision making process of the company. They should not just rubber stamp any decisions taken by the shareholders or their advisors. They should formulate and implement the treasury strategy of the company.
- With regards to decision making at Directors' level, a minimum level of information should always be provided, that would enable the directors of a company to consider whether or not they should make a decision. It is also prudent to ensure that board minutes properly document the information the directors have used to consider and then make decisions.
- Related to the point above, care should be taken to ensure that the board meetings are properly documented, i.e. detailed notes taken, outlining the matters for consideration of the board, as well as the information provided in the board pack to enable them to make their decisions.
- Last but not least, the company should have a valid commercial reason for its existence. Even though this can sometimes be a tax oriented reason, it should also have commercial benefits for setting up a company in the particular jurisdiction and the decision to establish a Cyprus group finance company should not be taken solely based on tax considerations.
- Consideration also needs to be given to whether the company's activities have sufficient economic substance, yielding a verifiable income, as well as looking at its economic operations in order to fulfill the general requirements for setting up the company in the chosen jurisdiction.



Beneficial Ownership Clause

It may be evident from the factual and functional analysis that the finance company undertakes minimal functions and carries little if any risk. Establishing whether an entity is entitled to the beneficial ownership of income also requires a fully functional and factual analysis of the recipient's rights to enjoy income. In the case of most treaties, the recipient of the interest has to be the beneficial owner of the income as a condition of obtaining clearance under the treaty to pay interest without deduction of withholding tax (or with WHT at a lower rate).

The concept of a group finance company having the actual right to income (in international practice – “beneficial owner”), for the purposes of applying a double tax treaty should be a company that has the power to use for itself and/or dispose of such income. In defining whether the finance company has the actual right to receive and dispose of the income, all the functions being exercised by the finance company should be considered, and also the risks being assumed by them.

For the purposes of applying most of the international tax treaties the finance company shall not be treated as having the actual right to such income if it has:

- limited power to dispose of the income; or
- exercises intermediary functions relating to the income for the benefit of another person, without performing any other functions and without itself assuming any risks, paying such income directly or indirectly (in full or in part) to such other person.

Most treaties have a “look-through” approach in determining the beneficial owner of income. According to this approach, if, at the moment of payment of interest the payee company as tax agent, knows that the beneficial owner of income is not the direct recipient of income, the tax agent may apply the double tax treaty and the respective rates signed between its country of residence and the country of residence of the real beneficial owner

For Financing structures involving the well-known back-to-back Cyprus financing structures (as explained further above) where the taxable income left in the Cyprus company was only a required margin in accordance with the Cyprus law of 0,35% for amounts up to Euro50 million, it is important to understand that this financing structure might no longer work, due to the fact that with back-to-back loans the Cyprus group finance company does not use its own funds (out of its own capital), but rather is using funds provided by third party loans. In the next section we explain in quite some detail the approach that should be followed by a Cyprus finance company in order to mitigate as much as possible the beneficial ownership risk.

Notional Interest Deduction (NID) on New Capital

Cyprus resident companies, that obtain new equity/capital as of 1 January 2015, would be able to claim a notional interest deduction of up to 80% of their taxable income. In accordance with the law the NID will be calculated on the basis of a reference interest rate on new equity/capital held by the company and used in the business. The above measure reduces significantly the tax charge of 12,5% of the Cyprus finance company up to an effective interest rate of 2,5%. The NID in general terms brings parity as any distortions between equity and debt capital, are finally removed since both forms of capital are now entitled to a tax deduction from taxable income.

The NID as shown in the below formula, will equal the multiple of "Reference Interest Rate" and "New Capital".

Reference Interest Rate

The applicable reference interest rate is the 10 year government bond yield rate (as at 31st December of the previous tax year) of the country in which the new equity is invested in, increased by 3%, (subject to a minimum rate equal to the 10 year Cyprus government bond yield, increased by 3%). The minimum applicable reference interest rate for Cyprus companies in 2015 was 8% (5% +3%).

What is meant by New Capital?

Any new equity capital introduced in the business on or after January 1, 2015. This includes issued fully paid share capital and share premium, but does not include amounts which have been capitalized and result from a revaluation of movable or immovable property or retained earnings (prior to 31st December 2014).

Anti-abuse provisions

- The NID regime is considered as interest expense and is subject to the same limitation rules as interest. In order to safeguard the coherence of the tax base, the NID will not be available in the case of losses neither can it exceed 80% of the taxable profit. Effectively this means that the NID cannot create or increase a tax loss.
- The NID may be restricted by the Tax Commissioner in the case where arrangements have been put into place aiming to benefit from the deduction, with no valid economic or commercial reason or in the case where old equity is attempted to be re-characterized as new equity through related party transactions and other arrangements.

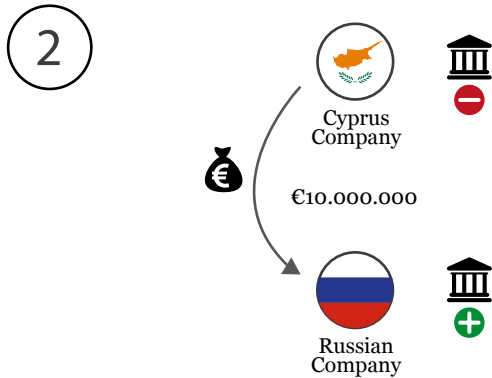
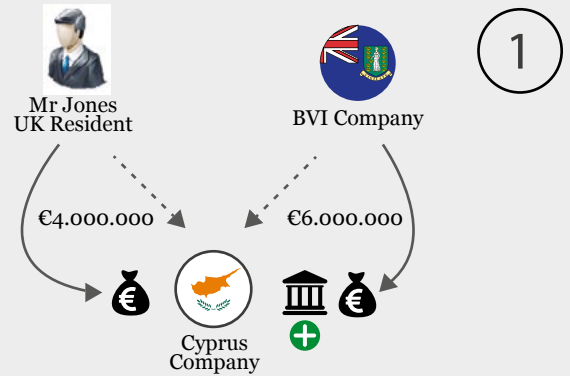
Flowchart 2, gives a diagrammatical example showing the tax treatment of interest receivable taking into account the Notional Interest Deduction on New Capital.

$$\text{Reference Interest Rate} \times \text{New Capital} = \text{Notional Interest Deduction}$$

Flowchart 2 | Taxation of Interest - Notional Interest on Capital

Loan Financing – Cyprus Company

- On 1/1/2015 the Cyprus company issued at a premium, 1.000 shares of nominal value of Eur1,00 each for Eur10.000 each. (No stamp duty applies on share premium)
- The two shareholders of the Cyprus company subscribed for the total amount of €10.000.000. Mr Jones gave €4.000.000 and BVI Co gave € 6.000.000.

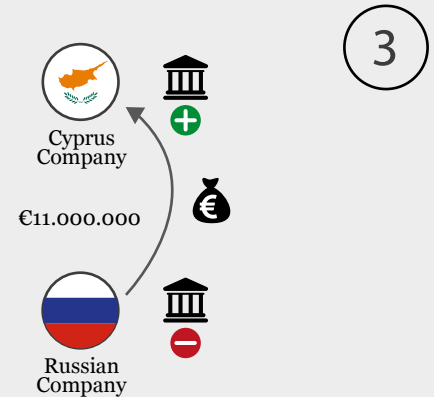


Loan Financing - Russian Company

- On 1/1/2015, the Cyprus company financed its Russian subsidiary company, with €10.000.000, under a loan agreement bearing an interest rate of 10%.
- According to the terms of the loan agreement, repayment of the loan amount as well as the interest should be made at the end of 2015.

Loan Repayment- Russian Company

- The double tax treaty between Russia and Cyprus, imposes a withholding tax rate on interest payments from Russia to Cyprus of 0%.
- On 31/12/2015 the Russian Company pays €11.000.000 to the Cyprus company, being the loan amount together with the outstanding interest.



4

Interest Receivable	€1.000.000
Deemed Interest Payable	(€800.000)
Net Profit	€200.000
Tax @ 12,5%	25.000

Loan Repayment – Cyprus Company

- The Cyprus company is allowed to have a notional interest deduction “NID” that is calculated on the basis of a reference interest rate on new equity/capital held by the company and used in the business.
- Since the new capital was used to finance a Russian subsidiary company, the applicable reference rate for Russia should be used (around 13% in 2015).
- The Cyprus company is able to claim a notional interest deduction of up to 80% of its taxable income.
- Thus, the Cyprus company is going to pay Cyprus tax equal to Euro25.000. This means an effective tax rate of 2,5%.



Other Significant Tax Considerations

Tax Treatment of Capital gains from the disposal of shares in participation holdings

Cypriot tax rules provide full exemption from local taxation on the realisation of capital gains from the disposal of shares in participation holdings, irrespective of whether the gain is considered to be of a capital or of a revenue nature.

There is no requirement for any minimum holding period, minimum investment amount or minimum % holding.

Tax treatment of outward dividends

Outward dividends paid by a Cyprus company to its ultimate parent company do not suffer any withholding tax in Cyprus.

The exemption applies to dividend payments made to both resident and non-resident Cyprus companies, irrespective of the country of residency of the parent company, whether it is resident in an EU country or not.

Outward dividends paid by the Cyprus company to individuals non-resident in Cyprus, or individuals resident in Cyprus but not domiciled, do not suffer any withholding tax in Cyprus.

Tax treatment of inward dividends

Dividends received from Cypriot participation holdings

Cyprus provides full exemption from local taxation in respect of dividends received by a Cyprus company from its local subsidiaries. This exemption is given regardless of the holding period of the shareholding and without any minimum investment amount or % holding requirements.

Dividends received from non-Cypriot participation holdings

Cyprus provides full exemption (subject to certain conditions) from local taxation in respect of dividends received by a Cyprus company from its non-Cypriot participation holdings. This exemption is given regardless of the holding period of the shareholding and without any minimum investment amount or % holding requirements.

The exemption will not be granted only if both of the conditions below are satisfied:

- 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 in Cyprus. (Generally accepted by the tax authorities in Cyprus that substantially lower means lower than 6,25%)

Extraction of dividends from subsidiary companies

A Cyprus company can achieve low or zero withholding tax rates when extracting dividends from foreign participation holdings by relying either on its extensive double tax treaty network, or on the EU Parent Subsidiary Directive.

If the participation holding is in the capital of a company in another member state and provided all conditions of the EU Parent/Subsidiary directive are met, the incidence of taxation is eliminated altogether.

Where the investment is in the capital of a company outside the EU, or where the conditions of the Parent/Subsidiary Directive are not met, the Cyprus company can rely on the extensive network of double tax treaties of the Cyprus Government, the rates of which, especially as far as Eastern European investments are concerned, are considered particularly advantageous. Appendix 1, shows the list of double tax treaties that Cyprus has enacted with third countries, as well as the corresponding rates of withholding tax.



Controlled Foreign Companies (CFC) Rules

Countries such as Germany, UK, France, Denmark and many more others have CFC legislation. Under their CFC rules, income and sometimes capital gains of a subsidiary or sub-subsidiary company may be appropriated to the parent company.

Cyprus does not have in its legislation CFC rules as strict as those in the above countries. As a result, no income is appropriated to the parent company even if the income arises in a tax haven company.

Thin Capitalisation

Most of the European countries, with some exceptions (such as Austria and Ireland), have thin capitalisation rules, such as rules imposing minimum debt to equity ratio requirements. A company is said to be thinly capitalised when its capital is made up of a much greater proportion of debt than equity, i.e. its gearing, or leverage, is too high. When a company is thinly capitalised part of the interest deduction may be disallowed and treated as a dividend distribution.

Cyprus tax legislation does not contain thin capitalisation provisions.

Inheritance or Estate Taxes

Cyprus does not have in its legislation any inheritance or estate taxes.

Wealth Taxes

Cyprus does not have in its legislation any taxes that are imposed on wealth.

Tax Losses

When a loss is not wholly set-off against income from other sources in the same year, it can be carried forward for the next five years (from the end of the tax year in which they were incurred) and set-off against future taxable income of the company. Loss is automatically set-off against the first available taxable income of the company. Losses can only be carried forward. No carry-back of losses is allowed.

Group relief

Current year tax losses may be surrendered by one Cyprus tax resident group company to another.

Current year tax losses may also be surrendered by an EU group company, provided such company firstly exhausts all possibilities available to utilise its tax losses in its country of residence or in the country of any intermediary EU holding company.

Group relief is available if both companies are members of the same group for the entire tax year.

Two companies are considered to be part of a group for group relief purposes if:

- one is a 75% subsidiary of the other, or
- both are 75% subsidiaries of a third company

Tax Credit for foreign tax paid

Any tax suffered abroad on income subject to income tax will be credited against any income tax payable on such income irrespective of the existence of a double tax treaty.

Stamp Duty

In accordance with the Stamp Duty Law of 1963 as amended, section 4 of the law, states that every document listed in the first schedule to the law needs to be stamped, if it concerns property that is situated in the Republic, or if it concerns matters or things that are going to be executed or will be carried out in the Republic, irrespective of the place where these have been drafted or prepared.

It is important to be stated that any contracts relating to assets situated outside Cyprus or business affairs that take place outside Cyprus are exempt from stamp duty (e.g. purchase of shares in foreign companies). For 2016 the maximum stamp duty on contracts is Euro20.000.



Capital Duty

According to the Cyprus Companies Act Law, every Cyprus incorporated company must pay capital duty on incorporation equal to Euro103 plus 0,6% on the authorised share capital, or on any subsequent increase in the authorised share capital.

As there is no capital duty payable on share premium, a company can arrange its capital structure in such a way as to have small authorised capital and issue the shares above their nominal value, at a premium.

Re-Domiciliation of Companies

Re-domiciliation of companies in and out of Cyprus is permissible, however the other jurisdiction's legislation must also recognize such a possibility.

Reorganisation rules

The Cyprus tax legislation has transposed the Merger Directive into the local income tax law and in accordance with this legislation, no tax consequences arise in the case of a reorganisation involving a Cyprus holding company.

EU Interest and Royalties Directive

Cyprus has transposed into Cypriot Law the EU Interest and Royalties Directive (Council Directive 2003/49/ EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments between associated companies of different Member States).

Though Cyprus tax rules are more liberal than the requirements of the Directive.

- There is no withholding tax on interest payments made to companies or individuals non-resident in Cyprus.
- There is also no withholding tax on royalty payments, where the rights have been granted for use outside Cyprus, irrespective of the form of the recipient of the income.

Tax Treatment of Liquidation Proceeds

Non-resident shareholders

In case of the liquidation of a Cyprus resident company, irrespective of the method of liquidation, there are no taxes to be paid on the distribution of assets to non-resident shareholders, whether this is in the form of dividends, proceeds from liquidation etc.

There is one exemption to the above rule. If the Cyprus company owns immovable property situated in Cyprus then the disposal of the Cyprus situated property can result in Capital Gains Tax.

Transfer Pricing

There is no specific transfer pricing legislation in Cyprus, other than a provision in the Income Tax Law which requires transactions between 'related parties' to be in accordance with the 'arm's length principle'. The "arm's-length principle" of transfer pricing states that the amount charged by one related party to another for a given product must be the same as if the parties were not related. An arm's-length price for a transaction is therefore what the price of that transaction would be on the open market.

The Cyprus tax legislation adopted the OECD model and guidelines to determine whether a transaction is at arm's length.

VAT

A Cyprus finance company can have a range of structures and purposes. Where the exclusive purpose of a Cyprus finance company is the provision of loans to other group companies, with the intention of deriving interest income, such a company is considered to be performing an economic activity for VAT purposes and consequently it does have the status of a taxable person for VAT purposes and consequently is able to register for VAT.

Where a Cyprus finance company is registered for VAT purposes, it may claim input VAT on goods and services acquired in Cyprus and other EU Member States.

Appendix 1 - Double Tax Treaties

	RECEIVED IN CYPRUS	Dividends	Interest	Royalties
	Treaty countries:			
1	Armenia	0 ⁽³²⁾	5 ⁽³³⁾	5
2	Austria	10	0	0
3	Bahrain ⁽³¹⁾	0	0	0
4	Belarus	5 ⁽⁴⁾	5	5
5	Belgium	10 ⁽¹⁾	10 ⁽¹⁶⁾	0
6	Bulgaria	5 ⁽¹⁹⁾	7 ⁽²⁵⁾	10 ⁽²⁰⁾
7	Canada	15	15 ⁽⁷⁾	10 ⁽¹¹⁾
8	China	10	10	10
9	Czech Republic	0 ⁽³⁰⁾	0	10
10	Denmark	0 ⁽³⁴⁾	0	0
11	Egypt	15	15	10
12	Estonia	0	0	0
13	Ethiopia ⁽³¹⁾	5	5	5
14	Finland	5 ⁽³⁷⁾	0	0
15	France	10 ⁽²⁾	10 ⁽⁹⁾	0 ⁽²⁶⁾
16	Georgia ⁽³¹⁾	0	0	0
17	Germany	5 ⁽²⁾	0	0
18	Greece	25	10	0 ⁽¹²⁾
19	Guernsey	0	0	0
20	Hungary	5 ⁽¹⁾	10 ⁽⁸⁾	0
21	Iceland	5 ⁽³⁹⁾	0	5
22	India	10 ⁽²⁾	10 ⁽⁸⁾	15 ⁽¹⁵⁾
23	Iran ⁽³¹⁾	5 ⁽¹⁹⁾	5	6
24	Ireland	0	0	0 ⁽¹²⁾
25	Italy	0	10	0
26	Kuwait	10	10 ⁽⁸⁾	5 ⁽¹⁴⁾
27	Kyrgyzstan ⁽²⁷⁾	0	0	0
28	Lebanon	5	5 ⁽¹⁶⁾	0
29	Lithuania	0 ⁽⁴⁰⁾	0	5
30	Malta	0 ⁽²²⁾	10 ⁽⁸⁾	10
31	Mauritius	0	0	0
32	Moldova	5 ⁽¹⁹⁾	5	5

	RECEIVED IN CYPRUS	Dividends	Interest	Royalties
33	Montenegro ⁽²⁸⁾	10	10	10
34	Norway	0 ⁽³⁾	0	0
35	Poland	0 ⁽³⁶⁾	5 ⁽⁸⁾	5
36	Portugal	10	10	10
37	Qatar	0	0	5
38	Romania	10	10 ⁽⁸⁾	5 ⁽¹⁴⁾
39	Russia	5 ⁽⁶⁾	0	0
40	San Marino	0	0	0
41	Serbia ⁽²⁸⁾	10	10	10
42	Seychelles	0	0	5
43	Singapore	0	10 ⁽²³⁾	10
44	Slovakia ⁽²⁹⁾	10	10 ⁽⁸⁾	5 ⁽¹⁴⁾
45	Slovenia	5	5 ⁽³³⁾	5
46	South Africa	10 ⁽⁴¹⁾	0	0
47	Spain	0 ⁽³⁵⁾	0	0
48	Sweden	5 ⁽¹⁾	10 ⁽⁸⁾	0
49	Switzerland	0 ⁽³⁸⁾	0	0
50	Syria	0 ⁽¹⁾	10 ⁽⁸⁾	15 ⁽¹³⁾
51	Tajikistan ⁽²⁷⁾	0	0	0
52	Thailand	10	15 ⁽¹⁷⁾	5 ⁽¹⁸⁾
53	Ukraine	5 ⁽²¹⁾	2	5
54	United Arab Emirates	0	0	0
55	United Kingdom	0 ⁽²⁴⁾	10	0 ⁽²⁶⁾
56	United States of America	5 ⁽⁵⁾	10 ⁽¹⁰⁾	0
57	Uzbekistan ⁽²⁷⁾	0	0	0

NOTES:

Paid from Cyprus

Dividends

Outward dividends paid by a Cypriot Company to non-tax residents of Cyprus, do not suffer any withholding tax in Cyprus.

Interest

Interest payments by a Cypriot Company to non-tax residents of Cyprus, are made gross, without any tax deducted.

Royalties

No withholding tax is levied on royalties as long as the right is used outside Cyprus. 10% in the case of royalties granted for use within the Republic. 5% on film and TV rights.

1	15% if received by a company controlling less than 25% of the voting power.
2	10% if received by a company controlling more than or equal to 10% of the capital. 15% in all other cases.
3	NIL if the beneficial owner is a company (other than a partnership) which holds directly at least 10% of the capital of the company paying the dividend. 15% in all other cases.
4	5% if the amount invested by the beneficial owner is over €200.000 irrespective of the % of voting power acquired. 10% is imposed if received by a holder of at least 25% of the share capital of the paying company. Otherwise the rate is 15%.
5	5% if received by a company controlling at least 10% of the voting power. 15% in all other cases.
6	10% if received by company, which has invested less than €100.000.
7	NIL if paid to the Government or for export guarantee.
8	NIL if paid to the Government of the other State or to a financial institution.
9	NIL if paid to the Government of the other State or in connection with the sale on credit of any industrial, commercial or scientific equipment or any merchandise by one enterprise to another or in relation to any form of loan granted by a bank or is guaranteed from government or other governmental organisation.
10	NIL if paid to the Government of the other State, to a bank or a financial institution or in respect to debt obligations arising in connection with sale of property or the provision of services.
11	NIL on literary, dramatic, musical or artistic work with the exception of films used for television programs.
12	5% on film royalties (except films shown on TV).
13	10% on literary, musical, artistic work, films and TV royalties.
14	NIL on literary, artistic or scientific work including films.
15	Treaty rate restricted to Cyprus legislation rate of 10%. 10% also applies to payment of technical fees, management fees and consultancy fees.
16	NIL if paid to the Government of the other State, a political subdivision or a local authority, the National Bank or any institution the capital of which is wholly owned by the State or a political subdivision or a local authority or in the form of interest income from bank deposits.
17	10% on interest received by financial institutions, on interest paid in connection with industrial, commercial, scientific equipment or the sale or merchandise between two companies.
18	10% on right to use industrial, commercial or scientific equipment or for information concerning industrial, commercial or scientific experience and 15% for patents, trademarks, designs, models, plans, secret formulas or processes.
19	5% if the dividend is received by a company owning directly at least 25% of the capital of the company paying dividend. 10% in all other cases.
20	This rate does not apply, where 25% or more of the capital of the Cypriot resident is owned directly or indirectly by the Bulgarian resident paying the royalties and the Cyprus company pays less than the normal rate of tax.
21	5% is applicable if the dividend is received by a company owning at least 20% of the capital of the dividend paying company or has invested in the acquisition of shares or other rights of the dividend paying company of at least €100.000. 15% in all other cases.
22	The treaty provides that the tax on the gross amount of the dividends shall not exceed that chargeable on the profits out of which the dividends are paid.
23	7% if paid to a bank or similar financial institution. NIL if paid to the government.
24	The treaty provides for 15% withholding tax but the local taxation provides for 0% withholding tax.
25	NIL if paid to or is guaranteed by the Government, statutory body, the Central Bank.
26	5% on film royalties, including films used for television programs.
27	The treaty between the Republic of Cyprus and the United Soviet Socialist Republic still applies.
28	The treaty between the Republic of Cyprus and the Socialist Federal Republic of Yugoslavia still applies.
29	The treaty between the Republic of Cyprus and the Czechoslovak Socialist Republic still applies.
30	NIL if the beneficial owner is a company (other than a partnership) which holds directly at least 10% of the capital of the company paying the dividends where such holding is being possessed for an uninterrupted period of not less than one year. 5% in all other cases.
31	The treaty has been published in the Gazette but has not come into effect until the time of publication of this publication.

32	5% if the beneficial owner has invested in the capital of the company less than the equivalent of €150.000 at the time of the investment.
33	NIL if paid to the Government or to a local authority, or to the Central Bank.
34	NIL if the beneficial owner is a company (other than a partnership) which holds directly at least 10% of the capital of the company paying the dividends, where such holding is being possessed for an uninterrupted period of no less than 12 months. NIL if the beneficial owner is the other Contracting State or the Central Bank of that other State, or any national agency or any other agency (including a financial institution) owned or controlled by the Government of that other State. NIL if the beneficial owner is a pension fund or other similar institution providing pension schemes in which individuals may participate in order to secure retirement benefits, where such pension fund or other similar institution is established, recognized for tax purposes and controlled in accordance with the laws of that other State. 15% in all other cases.
35	NIL if the dividend is received by a company (other than a partnership) holding at least 10% of the capital of the dividend paying company. 5% in all other cases.
36	NIL if the beneficial owner is a company (other than a partnership) which holds directly at least 10% of the capital of the company paying the dividends, where such holding is being possessed for an uninterrupted period of no less than 24 months. 5% in all other cases.
37	5% if the dividend is received by a company (other than a partnership) which controls directly at least 10% of the voting power in the company paying the dividends. 15% in all other cases.
38	NIL if the beneficial owner is: <ul style="list-style-type: none"> i. a company (other than a partnership) the capital of which is wholly or partly divided into shares and which holds directly at least 10% of the capital of the company paying the dividend for an uninterrupted period of at least one year. ii. a pension fund or other similar institution recognised as such for tax purposes, or iii. the Government, a political subdivision, local authority or central bank of one of the two contracting states. 15% in all other cases.
39	5% if the beneficial owner is a company (other than a partnership) which holds directly at least 10% of the capital of the company paying the dividends. 10% in all other cases.
40	NIL if the beneficial owner is a company (other than a partnership) which holds directly at least 10% on the capital of the company paying the dividends. 5% in all other cases.
41	5% if the dividend is received by a company which holds at least 10% of the capital of the company paying the dividend. 10% in all other cases.



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