Cyprus Tax Updates
The EU Anti-Tax Avoidance Directive

Presented by Savvia Stavrou

Director
K. Treppides & Co Ltd

Agenda

1 Key provisions of the Cyprus Tax Regime

2 Recent and expected tax developments

3 EU Anti-Tax Avoidance Directive

Key provisions of the Cyprus Tax Regime

Key provisions of the Cyprus Tax Regime

- Corporation Income Tax rate is 12,5%
- Gains from trading in qualifying securities are exempt from income tax
- Dividend income for companies is exempt from income tax and also exempt from Special Defence Contribution subject to easily met criteria
- No withholding taxes on dividends and interest payments to non-residents
- Notional Interest Deduction available on new equity (the effective tax rate can be reduced to as low as 2,5%)

Key provisions of the Cyprus Tax Regime

- IP Box regime (80% exemption of qualifying income from qualifying intangible assets subject to certain conditions)
- Special Tonnage Tax Regime
- Extensive Double Tax Treaty network and application of EU Directives
- Tax incentives available for individuals
    - 50% exemption on employment income exceeding EUR100K for non-residents taking up employment in Cyprus
    - Non-domicile rules for individuals becoming Cyprus tax residents
    - Tax residency based on the 60 days rule

Recent and expected tax developments

Recent and expected tax developments

- Exchange of Information
  - Common Reporting Standard (CRS)
  - Country by Country reporting (CbC)
- Transfer Pricing Developments
  - TP requirements for intra-group financing based on the circular issued in 2017
  - TP legislation is expected to be introduced during the year 2019
- OECD Multilateral Instrument (MLI)
  - Signed by Cyprus but pending ratification

Recent and expected tax developments

- Mandatory Disclosure for intermediaries (DAC 6)
  - Effective as from 25 June 2018 and first reporting by 31 August 2020
  - Domestic legislation expected by 31 December 2019
- BEPS/EU Anti-Tax Avoidance Directive
  - **Interest Limitation rules – 1 January 2019**
  - **Controlled Foreign Company (CFC) rules – 1 January 2019**
  - **General Anti-Abuse Rule (GAAR) – 1 January 2019**
  - Exit Taxation – 1 January 2020
  - Hybrid Mismatches – 1 January 2020
  - Reverse Hybrid Mismatches – 1 January 2022

EU Anti-Tax Avoidance Directive

Cyprus legislation in relation to ATAD

Implementation of ATAD in Cyprus

- On 5 April 2019 the Cyprus Parliament voted the amendments of the Income Tax Law implementing the provisions of the Anti-Tax Avoidance Directive (ATAD) in relation to:
  - Interest Limitation rules
  - Controlled Foreign Company (CFC) rules and
  - General Anti-Abuse Rule (GAAR)
- The amendments will be effective retroactively as of 1 January 2019
- The remaining measures of ATAD are expected to be introduced in 2019 and shall apply as from 1 January 2020 (except from Reverse Hybrid Mismatches Rule which shall apply as from 1 January 2022)

What would be the impact of these changes on Cyprus structures?

Interest Limitation Rule

Overview	***Exceeding borrowing costs*** that exceeds the 30% of the company's taxable company's taxable earnings before interest, tax, depreciation and amortization ***(EBITDA)*** shall not be allowed
Borrowing costs	Interest expenses on all forms of debt, other costs economically equivalent to interest and expenses incurred in connection with the raising of finance ***Note:*** *Notional Interest Deduction (NID) on new equity is not included in the definition of the borrowing costs*
Exceeding borrowing costs	The amount by which the deductible borrowing costs exceeds the taxable interest income and other economically equivalent revenues

Interest Limitation Rule

Interest Limitation rule will not apply to:
Exceeding borrowing costs below €3 million threshold
Standalone entities (not members of a consolidated group, do not have an associated enterprise or permanent establishment)
Financial undertakings (includes among others credit institutions, investment firms, AIFMs, AIFs, UCITS etc.)
Exceeding borrowing costs in relation to loans concluded before 17 June 2016 and not subsequently amended
Exceeding borrowing costs in relation to loans used to fund certain long-term public infrastructure projects
Companies with equity ratio higher or at least equal (i.e. not lower than 2%) to their group ratio

Interest Limitation Rule

Potential impact on Cyprus structures	
	It is expected that this rule will affect structures that are highly leveraged The minimum €3 million deduction of exceeding borrowing costs provides a safe harbor for many structures Possibility to carry forward any restricted exceeding borrowing costs in the next 5 years ***Financing and holding companies*** **→** should not be affected by this rule on the basis of the existing provisions in the Cypriot Income Tax Law ***IP companies*** **→** could be affected if incur significant borrowings for the acquisition of the IP

Interest Limitation Rule

Alternative option to consider

Finance the operations/business activities through equity so as to benefit from NID and avoid restriction of exceeding borrowing costs

Notional Interest Deduction (NID)

- NID on new equity introduced in the company after 1 January 2015 and used in its business activities
- The NID is calculated on the basis of a reference interest rate on new equity
- The NID reference rate constitute the interest rate of the 10 year government bond yield of the country in which the new equity is invested or of the Republic of Cyprus (as at 31st December of the previous tax year), whichever is the higher, increased by 3%
- The NID is restricted to 80% of the taxable income

Controlled Foreign Company (CFC) rules

Overview	The ***non-distributed income*** of an entity which is treated as ***CFC***, that arises from ***non-genuine arrangements***, is added to the taxable income of the Cypriot tax resident company
Non-distributed income	Is considered the after tax accounting profit of the CFC that was not distributed to the Cyprus tax resident company during the same tax year or within the seven months from the end of the year
Non-genuine arrangements	An arrangement or a series of arrangements shall be regarded as non-genuine to the extent that the significant people functions that generate CFC's income are carried out by the Cypriot tax resident company

Controlled Foreign Company (CFC) rules

Definition of CFC	A foreign company or an exempt permanent establishment (PE), provided that: 1. the Cypriot company, alone or together with its associated enterprises, has a direct or indirect participation in a foreign company of more than 50% interest in the share capital, voting rights or profits distributions of that company; and 2. the actual corporate tax paid on the profits is lower than 50% of the tax that would have been charged on that foreign company or PE, if such profits were taxed in Cyprus

Note: *Corporate Income Tax in Cyprus is 12,5%*

→ CFC if taxed at a rate lower than 6,25%

Controlled Foreign Company (CFC) rules

Potential impact on Cyprus structures

- It is not expected to have an impact on structures with operating subsidiaries that have appropriate personnel carrying out their functions
- Cyprus groups that hold directly or indirectly participations in no tax jurisdictions may be impacted by the implementation of these rules

Option for consideration

Distribution of profits in order to be excluded from the CFC rules

Dividends received by a Cyprus company from a foreign company is:

- Exempt from Income Tax in Cyprus
- Exempt from Special Defence Contribution tax, unless:
  1. the paying company engages (directly or indirectly) more than 50% in activities which lead to investment income **and**
  2. the foreign tax is substantially lower than the tax burden in Cyprus (less than 6,25%)

General Anti Abuse Rule (GAAR)

Overview	For the purposes of calculating the corporate tax liability, it shall be excluded, an arrangement or series of arrangements which have been put into place for the main purposes or one of the main purpose of obtaining a tax advantage that defeats the object or purposes of the Cyprus tax legislation and are **not genuine**, having regard to all relevant facts and circumstances
Non-genuine arrangements	Are defined as an arrangement or a series of arrangements that are not put into place for valid commercial reasons which reflect economic reality
Potential impact on Cyprus taxpayers	▪ It is not expected to have significant impact (similar provision in the Cyprus Tax legislation) ▪ It is expected that this rule will apply only to wholly artificial arrangements as set out in the EU tax framework

Key points

Next Steps

- Review current structures to identify companies that may be affected
- Assess the impact of the new rules on the current structures
- Consider alternative options
- Take appropriate actions
- Monitor international tax developments
- Create sufficient level of substance

Cyprus remains a competitive and an attractive jurisdiction for doing business internationally if operations are structured properly

Contact details

Savvia Stavrou
Director
sstavrou@treppides.com

Nicosia Office
Treppides Tower, 9 Kafkasou Str.
Aglantzia, CY 2112, Nicosia, Cyprus
P.O. Box 27142, CY 1642, Nicosia, Cyprus
Tel: (+357) 22678944
Fax: (+357) 22681887

Limassol Office
Kristelina Tower, 12 Arch. Makarios III Avenue
Mesa Geitonia, CY 4000 Limassol, Cyprus
Tel: (+357) 25822722
Fax: (+357) 25822723

London Office
7 Milner Street
London SW3 2QA

Malta Office
Level 1, Somnium, Tower Road
Swatar, Birkirkara BKR 4012

www.treppides.com