

Cyprus Executive Briefing – New VAT and tax legislation

July 2002

New tax legislation

The House of Parliament has finally approved the proposed tax reforms with some changes. Some of the principal measures effective from 1 January 2003 and some provision effective from 2002 affecting individuals and companies are highlighted below.

Corporation Tax for entities

A company is resident in Cyprus if its management and control is in Cyprus. All companies are now local companies and the distinction between local companies and international business companies (IBCs) is now abolished. The taxable profits of all companies will be taxed at the rate of 10%. Existing IBC's that at 31 December 2001 were generating income from sources outside Cyprus from a business carried outside Cyprus, from investments in shares and securities, royalties or rental income may elect to continue to be taxed at the rate of 4.25% for the fiscal years 2003, 2004 and 2005.

If the company elects for the transitional provisions:

- The election must be made for all three years.
- The company must continue to generate income only from sources outside Cyprus.
- Dividends received are subject to tax and any tax credit can be set off against Cyprus income tax.
- Gains from the sale of shares, which are treated as trading profits are included in the taxable income.
- Interest received is taxed with the exemption of interest received from local banks and any tax credit can be set off against Cyprus income tax.
- The company cannot claim group relief.
- Losses up to 2000 can be carried forward only for 5 years. Losses for the year 2001 onwards may be carried forward indefinitely.
- Cannot benefit under the merger provisions.

For 2002 international business companies will continue to be taxed at the rate of 4.25% as the law comes into effect on 1 January 2003.

Profits earned from permanent establishment abroad (i.e. a place of management, a branch, an office, a factory, a workshop, a mine, oil gas well, quarry or place of extraction of minerals, a building site or construction or installation project or supervisory activities relating to such projects) are fully exempt.

Dividend income from Cyprus and abroad is wholly exempt from income tax.

Losses can be carried forward and set off against future trading profits and the five-year restriction for carrying forward losses is now abolished. Losses of a company can also be set off against profits of another company of the same group. Abolition of the 10% minimum tax on utilization of losses brought forward from previous years, which existed for ex local companies.

mail address	office
P.O. Box 16026 CY 2085 Acropolis, Cyprus Tel.: 357-22-752990	11 Karpenisiou Str., Off. 202 CY-1077 Nicosia, Cyprus Fax: 357-22-752815

No taxation on the profits from the disposal of securities for all the companies that are residents in Cyprus.

The current provisions for no withholding tax on dividends, interest or royalties to non-residents will continue to apply.

Royalties are subject to a 10% withholding tax but only on royalties arising from the use of the asset in Cyprus.

Film rentals are subject to a 5% withholding tax.

Income of nonresident professionals entertainers and athletes from activities in Cyprus is subject to a 10% withholding tax.

Abolition of reduced income tax rates from profits from exports and abolition of exemptions available for the importation of foreign exchange from activities abroad, which were given as an incentive for ex-local companies.

Additional special tax for the years 2002, 2003 and 2004 for semi-government bodies and companies that are not controlled by foreigners based on the entities profits.

Interest income earned from a company resident in Cyprus is 50% exempt from income tax unless the interest is earned from the trading activities of a company, which is fully taxable. In the year 2002 20% of the interest income earned will be exempt from income tax.

No tax implications on mergers, acquisitions and amalgamations of companies (i.e. no taxes on transfer of the business, no taxes on the transfer of the assets, no taxes on exchange of shares, losses incurred prior to the merger may be carried forward by the new company, no stamp duties are payable on documents to effect the merger)

Profits of ship management companies are taxed at the rate of 4.25% unless the company elects to pay tonnage tax on ships it manages.

Special contribution for defence for entities

A 15% withholding tax for special contribution for defence will apply on dividends where the shareholder is resident in Cyprus. In case a company resident does not proceed with the distribution on a dividend within two years from the end of the fiscal year on which profits have been earned, 70% of the profit will be considered as distributed (deemed dividend distribution). Foreign owners will be exempt as there is no deemed distribution of dividends to them.

A 15% special contribution for defence will apply on dividends received from abroad by the company, unless dividends are received from a company abroad, in which the recipient company holds at least 1% of the share capital and the paying company does not derive more than 50% of its profits from investment activities, which are taxed at substantially lower rates than the Cypriot corporation tax rate.

Special defence contribution existed for ex local companies is now abolished.

mail address	office
P.O. Box 16026 CY 2085 Acropolis, Cyprus Tel.: 357-22-752990	11 Karpenisiou Str., Off. 202 CY-1077 Nicosia, Cyprus Fax: 357-22-752815

Interest income earned from companies resident in Cyprus will be subject to special contribution for defence at the rate of 10%. There is no special contribution for defence for interest income earned from usual trading activities.

A 3% special contribution for defence will apply on 75% of rental income from property.

Income tax for individuals

An individual is resident of Cyprus if he lives in Cyprus for one or more periods, which exceed the total of 183 days per fiscal year.

Personal Tax Rates for the year 2002

C£	%
0 - 9.000	0
9.001 - 12.000	30
12.001 and over	40

Personal Tax Rates for the year 2003

C£	%
0 - 9.000	0
9.001 - 12.000	20
12.001 - 15.000	25
15.001 and over	30

Personal Tax Rates for the year 2004

C£	%
0 - 10.000	0
10.001 - 15.000	20
15.001 - 20.000	25
20.001 and over	30

Note:

All personal allowances are eliminated, except for claims in relation to social insurance and provident fund contributions and life insurance policies, which will continue to apply. Also social grant will be given in lieu of the children allowances abolished.

Interest and dividend income is fully exempt from income tax. However for the year ended 2002 only £600 plus 50% of the amount exceeding £600 of interest income is exempt from income tax.

No taxation on profits from disposal of securities for individuals that are residents in Cyprus.

Profits of an individual earned from permanent establishment abroad are wholly exempt from income tax.

mail address	office
P.O. Box 16026 CY 2085 Acropolis, Cyprus Tel.: 357-22-752990	11 Karpenisiou Str., Off. 202 CY-1077 Nicosia, Cyprus Fax: 357-22-752815

The option given to expatriates working for international business companies to be taxed at half the normal rates is now abolished. Non residents taking employment in Cyprus will have a special exemption of 20% of the income earned or £5.000 per annum whichever is the lower only for the first three years of their employment.

Special contribution for defence for individuals

From 1 July 2002 special contribution for defence on employees, self employed persons and retirees has been abolished.

Interest income is subject to special contribution for defence at the rate of 10% only on individuals resident in Cyprus. If the annual income of the individual does not exceed £7.000 then the individual can claim 7% from the income tax authorities paying effectively 3%. Individuals earning interest income from saving bonds, development bonds, deposit with the Housing Finance Corporation and provident fund interest will be subject to special contribution for defence at the rate of 3%.

Dividend income is subject to special contribution for defence at the rate of 15% only on shareholders resident in Cyprus.

Immovable property tax

Property value C£	Rate %
Up to 100.000	-
100.001-250.000	2.5
250.001-500.000	3.5
500.000 and above	4

VAT rates

The VAT rate increase from 10% to 13% from 1 July 2002 for a time period before it is increased to 15% on 1 January 2003.

VAT on sale of goods is imposed upon delivery or upon issue of invoice/receipt of money, if this precedes the delivery.

Vat on supply of services is imposed upon completion of the service or upon issue of an invoice/receipt of money if this precedes the completion of the service.

This publication is intended only for general guidance. For further information, contact Ioannis Zervos by fax at 357 22 752815 or by email at info@zervosco.com

mail address	office
P.O. Box 16026 CY 2085 Acropolis, Cyprus Tel.: 357-22-752990	11 Karpenisiou Str., Off. 202 CY-1077 Nicosia, Cyprus Fax: 357-22-752815