



Cyprus' Tax Regime

Benefits for International Business

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Cyprus has always been an excellent location for holding companies for a host of reasons, including its transparent legal system, excellent communications and world-class professional and banking services. It is an EU member state with an open market economy and no restrictions on capital movements

From a tax perspective, a multinational group requires five things from a holding company.

Three of them are:

- The holding company must be able to receive income streams from and the proceeds of the sale of an operating company, while suffering no, or at least the lowest possible, tax cost in the operating company's jurisdiction;
- Dividends from and proceeds of the sale of operating companies should not be taxed in the holding company jurisdiction;

- It should be possible (and this has usually been the most difficult step) to take dividends out of the holding company without giving rise to any charge to tax in the holding company jurisdiction.

How does Cyprus measure up against these benchmarks?

In brief, the answer is "very well":

- Cyprus has an extensive network of double tax treaties and as an EU member state, entitles resident companies to the benefits of the EU Parent-Subsidiary Directive;
- Any dividends received by a Cyprus resident company are also exempt from tax in Cyprus, except in the case of dividends from abroad where more than 50% of the activities of the paying company result directly or indirectly in investment income; and the paying company is subject to tax at 5% or less.

- The profits of a Cyprus company's permanent establishment in another jurisdiction are similarly exempt, subject to the same conditions as dividends;
- Non-exempt dividend income is subject to tax at 15%. Tax credits are available for taxes paid abroad;
- Interest income that is the result of the main activities of the company or that is closely connected to those activities is taxable at the standard corporate income tax rate of 10% after deduction of associated finance expenses, like any other "active" trading income. In practice, the liberal transfer pricing regime allows group debt finance to be routed through Cyprus subject to tax at 10% on only a small interest rate margin;
- Mergers, acquisitions and other re-organisations may be effected without tax cost;

- The only withholding tax levied by Cyprus is (subject to treaty provisions) a 10% withholding tax on royalties derived from the use of a right or asset within Cyprus. All other dividend, interest and royalty payments made to non-resident recipients may be made without deduction of tax.

- Crucially, capital gains deriving from the disposal of shares and other securities are exempt from all forms of taxation in Cyprus providing the company whose shares are being sold does not hold Cyprus real estate;

- In addition, Cyprus's domestic corporate tax regime is extremely attractive, with profit taxed at 10%, the lowest rate in the EU, generous rules on the deductibility of expenses incurred in producing taxable income and the absence of any specific thin capitalisation regime.

The Verdict

These factors make Cyprus a highly attractive intermediate holding company jurisdiction as they offer the following benefits:

- Groups investing outside Cyprus may flow-through income streams, which is generally tax exempt in Cyprus and not attract withholding tax as they leave;

- Subsidiaries that have scope for significant capital appreciation may be held in Cyprus and sold without any liability to tax on the gain;

- Other assets (including, in certain circumstances, foreign real estate) that have scope for significant capital appreciation may be placed in a Cyprus corporate wrapper and sold without any liability to tax on the gain;

- Cyprus's double tax treaty network and the EU Parent-subsidiary directive offer a number of other

tax planning opportunities to reduce withholdings from income paid to the Cyprus resident company;

- Cyprus allows payment of dividend, interest and royalties without payment of withholding tax.

Cyprus can also be used as the location for the ultimate holding company, for instance in a group that is relocating to a new jurisdiction or on formation of a new publicly traded corporation with international operations. It is particularly suitable for any fund or investment vehicle since there is no tax on transactions in securities, even if this is the entity's main trading activity. Since there is no withholding tax on dividends there is no uncertainty over recovery of tax paid.

To take full advantage of the Cyprus holding company regime, the holding company must both be tax resident in Cyprus and have a genuine reason for being. Tax residence is secured by ensuring that management and control are exercised in Cyprus by the directors. If the company is no more than a tax-driven device without an economic function or substance in Cyprus, it may not be able to benefit from the advantages of Cyprus's extensive tax treaty network and, in particular, it may be caught by anti-avoidance rules imposed by operating company jurisdictions to withdraw the benefits of the EU Parent-Subsidiary Directive.

The holding company must produce financial statements complying with International Financial Reporting Standards, particularly IAS 27, which requires consolidated accounts to be presented unless the exemptions set out in paragraph 10 of IAS 27 are available.

The final choice of a holding company location is a question of balancing tax and non-tax considerations. While no single location can claim first place on every test, Cyprus should always be on the shortlist.



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