

## Corporate Tax - Cyprus

### New double tax agreement with Georgia

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#### Introduction

On May 13 2015 Cyprus and Georgia signed a new double tax agreement. Unlike many former members of the Union of Soviet Socialist Republics (USSR), Georgia did not adopt the 1982 Cyprus-USSR double tax agreement when it became independent and the new agreement is the first between the two countries. It will come into force once it has been ratified in accordance with both countries' domestic legal procedures.

The new agreement closely follows the 2010 Organisation for Economic Cooperation and Development (OECD) Model Tax Convention, with only minor modifications, and the protocol to the agreement clarifies the information exchange provisions.

#### Details of agreement

##### **Taxes covered**

The agreement covers all taxes on income and capital levied by either state or by any of its sub-divisions or local authorities, including taxes on capital appreciation and on gains from the alienation of movable or immovable property.

The agreement applies to income tax, profit tax and property tax in Georgia and income tax, corporate income tax, special contribution for defence tax, capital gains tax and immovable property tax in Cyprus.

The agreement will also apply to any identical or substantially similar taxes that are imposed in future in addition to, or in place of, existing taxes.

##### **Residence**

Article 4 of the agreement reproduces the provisions of the OECD Model Tax Convention regarding residence verbatim.

##### **Permanent establishment**

Article 5 of the agreement – which deals with permanent establishment – also reproduces the provisions of the OECD Model Tax Convention almost verbatim, with the same definition of a 'permanent establishment' and list of ancillary activities that *prima facie* do not give rise to a permanent establishment, including:

- the storage and display of goods;
- the maintenance of stock for processing by a third party;
- a purchasing or information-gathering facility; or
- a facility for preparatory or auxiliary purposes.

As in the OECD Model Tax Convention, the following will give rise to a permanent establishment:

- a place of management;
- a branch;
- an office;
- a factory;
- a workshop or a mine;
- an oil or gas well;
- a quarry; or
- any site of extraction, exploration or exploitation of natural resources.

Further, a building site, a construction, assembly or installation project or a supervisory or consultancy activity connected with any of the above will be deemed to be a permanent establishment if it lasts for more than nine months (rather than the 12 months required in the OECD Model Tax Convention).

As in the OECD Model Tax Convention, the agreement provides that an independent broker or agent that represents the enterprise in the ordinary course of business will not be caught by this provision. However, Paragraph 5 of Article 5 introduces a reservation. In the event that a person other than an agent of independent status is acting on behalf of an enterprise in a contracting state and has, and habitually exercises, the authority to conclude contracts in the name of the enterprise, the enterprise concerned will be deemed to have a permanent establishment in that state in respect of any activities which that person undertakes for the enterprise – unless the activities concerned are limited to those that do not give rise to a permanent establishment as listed above. This means that particular caution needs to be exercised regarding the issue of general power of attorney, so as not to risk inadvertently creating a permanent establishment with potential adverse consequences.

### ***Offshore activities***

Many of the double tax agreements that Cyprus has established since gas reserves were discovered in its exclusive economic zone in 2008 have included provisions on offshore hydrocarbon exploration and exploitation activities. The Cyprus-Georgia agreement does not include any specific provision regarding offshore hydrocarbon exploration and exploitation activities, but instead relies on the provision that an oil or gas well, quarry or any other place of extraction, exploration or exploitation of natural resources gives rise to a permanent establishment.

### ***Income from immovable property***

As in the OECD Model Tax Convention, income from immovable property may be taxed in the territory of the state where the property is situated.

### ***Business profits***

The profits of an enterprise are taxable only by the contracting state in which it is resident, unless it carries out business in the territory of the other state through a permanent establishment, in which case the profit attributable to the permanent establishment may be taxed by the contracting state in which it is located.

The agreement follows the OECD Model Tax Convention regarding the apportionment of profits to permanent establishments.

### ***International shipping and transport***

Profits from the operation of ships or aircraft in international traffic (including income from containers, trailers and related equipment and profits from participation in a pool, a joint business or an international operating agency) are taxable only by the contracting state in whose territory the enterprise is resident.

### ***Associated enterprises***

The provisions for adjusting the profits of associated enterprises operating other than on an arm's-length basis reproduce the corresponding article of the OECD Model Tax Convention.

### ***Dividends***

Dividends paid by a resident of one contracting state to a resident of the other are taxable only by the second contracting state, with the usual reservation regarding dividends that arise from a permanent establishment in the first contracting state. There is no stipulation regarding beneficial ownership.

### ***Interest***

Interest arising in one contracting state and paid to a resident of the other is taxable only in the contracting state in which the recipient is resident, subject to the usual reservations regarding interest arising from a permanent establishment in the first contracting state and any excess above the amount that would be payable on an arm's-length basis.

### ***Royalties***

Royalties arising in one contracting state and paid to a resident of the other are taxable only by the contracting state in whose territory the recipient is resident, provided that the recipient is the beneficial owner.

### ***Capital gains***

Gains derived by a resident of one contracting state from the alienation of immovable property situated in the territory of the other, or from the disposal of immovable or movable property associated with a permanent establishment situated in the other, may be taxed by the contracting state in whose territory the immovable property or the permanent establishment is situated.

Gains derived from the disposal of all other property are taxable only by the contracting state of residence of the donor.

### ***Elimination of double taxation***

Elimination of double taxation is achieved by the credit method. In relation to income or capital that is exempt pursuant to other provisions of the agreement, the contracting state in which the recipient is resident may take into account the exempt income or capital when calculating the tax liability of the recipient (exemption with progression).

### **Non-discrimination and mutual agreement procedure**

The agreement reproduces the corresponding provisions of the OECD Model, except that it includes no arbitration procedure to settle issues that cannot otherwise be resolved.

### **Exchange of information**

The exchange of information article reproduces Article 26 of the OECD Model Tax Convention verbatim. However, the protocol to the agreement provides robust safeguards against abuse of the information exchange provisions by requiring the contracting state that requests information to fulfil specified procedures to demonstrate the foreseeable relevance of the information to the request. No request is to be submitted unless the party making the request has reciprocal procedures and means of obtaining similar information, and every request must be accompanied by comprehensive details in writing of:

- the identity of the person under examination or investigation;
- the specific information sought; and
- the justification for the request.

This means that the authorities requesting the information must have a *prima facie* case before they request the information and must make a reasoned request for disclosure. These provisions are in line with the robust safeguards against abuse of the exchange of information provisions contained in Cyprus's Assessment and Collection of Taxes Law.

Requests for exchange of information are dealt with by a specialist unit and the informal exchange of information between tax officers that bypasses the competent authority is prohibited. A request must be more than a brief email containing the name and identifying information of the individual concerned. Rather, a detailed case must be made with the criteria set out in a formal, reasoned document. This means that the authorities requesting the information must already have a strong case before they request the information. As a final safeguard, the attorney general's written consent must be obtained before any information is released to an overseas tax authority.

### **Assistance with collection of taxes**

The agreement includes no provisions regarding assistance with the collection of taxes.

### **Entry into force and termination**

The agreement will enter into force when the two governments inform one another that the requisite constitutional procedures have been completed. Its provisions will have effect in the territory of both contracting parties from the beginning of the following year.

Termination of the agreement will require written notice to be given by either state at least six months before the end of the calendar year, whereupon the agreement will cease to have effect from the beginning of the following year. Notice may be given only after the agreement has been in force for five years.

### **Comment**

Georgia is turning towards the West in economics and trade and the double tax agreement will be a valuable addition to Cyprus's extensive treaty network. It is hoped that the remaining steps required to bring the new agreement into effect can be completed soon.

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