HARNEYS

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A Guide to the Cyprus Holding Company Regime

Why set up a holding company? In essence, holding companies are set up as an effective means of consolidating ownership of operating subsidiaries. Deciding where to set up a holding company is not always a tax driven exercise, but usually, a business entrepreneur will seek the most tax effective means of consolidating ownership of his or her operating subsidiaries.

As aptly stated by Lord Tomlin in IRC v Duke of Westminster, "every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Act is less than it otherwise would be". Indeed, no taxpayer is obliged to pay more tax than he can be compelled to, so a lot of structuring is often resorted to in order to minimize the incidence of taxation. The revenues flowing from such investment are considerable so it is no wonder that there is increasing competition over which jurisdiction can offer the best holding regime.

Main features of the Cyprus holding regime

Extraction of dividends from subsidiaries

A Cyprus holding company can achieve low or zero withholding tax rates when extracting dividends from underlying subsidiaries by relying either on its double tax treaty network, or on the Parent/Subsidiary Directive. When there is a choice between these two means (ie when the investment is an intra-EU qualifying investment) the Parent/Subsidiary Directive should be preferred as it eliminates the incidence of taxation altogether. Where the investment is outside the EU, or where the conditions of the Parent/Subsidiary Directive are not met, Cyprus can rely on a rich network of double tax treaties, the rates of which, especially as far as Eastern European investments are concerned, are considered particularly advantageous. The treaty network of Cyprus with applicable rates is attached as Appendix A.

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July 2014

Tax treatment of incoming dividends

Dividends received by a Cyprus holding company from a Cyprus subsidiary are exempted from any taxation in Cyprus. Cyprus taxes foreign incoming dividends at a rate of 17 per cent but provides for a generous exemption mechanism which is almost always satisfied resulting in the non-taxation of the foreign-source dividend income. The exemption mechanism as well as the distinction between local and foreign source dividends will be explained in further detail below.

Tax treatment of outgoing dividends

There are no withholding taxes on dividend payments to non-residents regardless of the country of residence of the non-resident shareholder or the existence or not of a double tax treaty with such country of residence.

Tax treatment of capital gains

There is no capital gains tax in Cyprus other than on gains accruing from the disposal of immovable property held in Cyprus or shares in companies (not listed on a recognised stock exchange), the property whereof consists of immovable property held in Cyprus. Moreover, Cyprus legislation specifically exempts from taxation any gains accruing from the disposal of shares, securities and debentures.

Additional features of the Cyprus tax regime

- 12.5 per cent tax on corporate profits;
- No withholding tax on royalties for use outside Cyprus;
- Active interest income (interest income effectively connected with the carrying on of a trade or business of the company) is subject to the corporate income tax rate of 12.5 per cent as regular trading income.
- Passive interest income, (income not connected to a trade or business), is exempt from corporate income tax and taxed separately at the Special Contribution for Defence (SCD) at the rate of 30 per cent on a gross basis.
- Credit relief available for foreign withholding tax unilaterally;
- Ability to carry forward losses for a period of five (5) years;
- Group relief rules available;
- Flexible and tax efficient reorganisation provisions;
- Wide network of double tax treaties;
- IP box exemption whereby profits from the use or sale of IP reduced by 80 per cent before being taxed at the corporate income tax rate of 12.5 per cent resulting in an effective tax rate on IP income of less than 2.5 per cent (and broad definition of IP includes all intangible assets (such as brands, franchises, copyrights, designs, computer software, patents etc.)
- Generous permanent establishment provisions in DTT network.

Special defence for tax on dividends

Under the Cyprus tax legislation, dividend income received by a Cyprus resident will not be charged under the income tax law but under the Special Contribution for the Defence Law (SCDL) at 17 per cent. The SCDL implements the Parent/Subsidiary Directive whereby tax-paying companies in the European Union are entitled to receive dividends from subsidiaries in other EU countries free of foreign withholding tax and upon receipt must either exempt the dividend income or provide a credit for the underlying tax paid. Cyprus uses the exemption method. Dividends received by a Cyprus resident are taxed at the rate of seventeen per cent (17 per cent), except the following:

- Dividends paid from one Cyprus resident company to another.
- Dividends received from an overseas company by a resident company of Cyprus or a company which is not a resident of Cyprus but has a permanent establishment in Cyprus. This exemption does not apply if a) more than 50 per cent of the paying company's activities result directly or indirectly in investment income and b) the foreign tax burden on the income of the company paying the dividends is substantially lower than the Cypriot tax burden. The conjunction "and" implies that both criteria have to be met for the exemption to not apply.

Cyprus reorganisation rules

The Cyprus tax legislation has transposed the Merger Directive into the local income tax law and unlike the Directive itself which provides only for cross-border reorganisations of companies within the European Union and is restricted to income tax consequences has extended the tax benefits to domestic reorganisations, to cross-border reorganisations with EU member and non EU member states and to reorganisations abroad with tax implications in Cyprus.

In accordance with this legislation, no tax consequences arise in the case of a reorganisation involving a Cyprus holding company.

Conclusion

The Cyprus legislation has introduced a number of tax opportunities for Cyprus holdings and has brought the Cyprus holding company to the fore as an international competitor in the field of holding regimes. A Cyprus holding company can receive dividends at mitigated rates of withholding tax based on its double tax treaty network, can exempt the incoming dividend from tax subject to a few simple conditions, and can distribute the dividend to its non-resident shareholders (whether or not they reside in the EU or in a country with which Cyprus has a double tax treaty) free of any withholding tax in Cyprus. Moreover the disposal by a Cyprus company of its underlying shareholding will not attract capital gains tax if immoveable property in Cyprus or shares representing immoveable property situated in Cyprus are not the subject of such disposal, and the reorganization rules offer flexibility and significant tax planning opportunities for restructuring via Cyprus.

Appendix A

Cyprus double tax treaties – summary of withholding taxes

Cyprus Companies	Effective Date	PAID FROM CYPRUS (1)			RECEIVED IN CYPRUS		
		Dividends %	Interest %	Royalties %	Dividends %	Interest %	Royalties %
Treaty countries		0	0	0 (2)	Treaty rates	Treaty rates	Treaty rates
Armenia	01/01/2012	0(27)	5 (6)	5	0(27)	5 (6)	5
Austria	01/01/1991 (31)	0	0	0	10	0	0
Belarus	01/01/2000	5 (17)	5	5	5 (17)	5	5
Belgium	01/01/2000	10 (8)	10 (6,18)	0	10 (8)	10 (6,18)	0
Bulgaria	01/01/2002	5 (22)	7 (6)	10	5 (22)	7 (6, 23)	10 (23)
Canada	01/01/1985	0	15 (4)	10 (5)	15	15 (4)	10 (5)
China	01/01/1992	0	10	10	10	10	10
Czech Republic	01/01/2010	5 (28)	0	10	5 (28)	0	10
Denmark	01/01/2012	15 (29)	0	0	15 (29)	0	0
Egypt	01/01/1996	15	15	10	15	15	10
Estonia	01/01/2014	0	0	0	0	0	0
Finland	01/01/2014	5 (9)	0	0	5 (9)	0	0
France	28/01/1983	0	10 (10)	0 (3)	10 (9)	10 (10)	0 (3)
Germany	01/01/2012	5 (30)	0	0	5 (30)	0	0
Greece	01/01/1967	25	10	0 (12)	25 (11)	10	0 (12)
Hungary	01/01/1982	0	10 (6)	0	5 (47)	10 (6)	0
India	01/01/1993 (32)	10 (48)	10 (10)	15 (15)	10 (48)	10 (10)	15 (15)
Ireland	01/01/1962 (33)	0	0	0 (12)	0	0	0 (12)
Italy (34)	01/01/1970	0	10	0	15	10	0
Kuwait	01/01/2014	0	0	5	0	0	5
Lebanon	01/01/2006	5	5	0	5	5	0
Lithuania	(46)	0 (45)	0	5	0 (45)	0	5
Malta	01/01/1994	15	10	10	0	10	10
Mauritius	01/01/2001	0	0	0	0	0	0
Moldova	01/01/2009	5 (22)	5	5	5 (22)	5	5
Montenegro (25)	01/01/1987	0	10	10	10	10	10
Norway(35)	01/01/1954	0	N/A (49)	0	0 (13)	N/A (49)	0
Poland(36)	01/01/2013	0 (37)	5 (6)	5	0 (37)	5 (6)	5
Portugal	01/01/2014	10	10	10	10	10	10
Qatar	01/01/2010	0	0	5	0	0	5
Romania	01/01/1983	10	10 (6)	5 (7)	10	10 (6)	5 (7)
Russia	01/01/2000 (38)	5 (16)	0	0	5 (16)	0	0
San Marino	01/01/2008	0	0	0	0	0	0
Serbia (25)	01/01/1987	0	10	10	10	10	10
Seychelles	01/01/2007	0	0	5	0	0	5
Singapore	01/01/2002	0	10 (6,24)	10	0	10 (6,24)	10
Slovakia (39)	01/01/1981	0	10 (6)	5 (7)	10	10 (6)	5 (7)
Slovenia	01/01/2012	5	5 (6)	5	5	5 (6)	5
South Africa	01/01/1999	0	0	0	0	0	0
Spain	(44)	0 (43)	0	0	0 (43)	0	0
Sweden	01/01/1988	0	10 (6)	0	5 (47)	10 (6)	0
Syria	01/01/1996	0 (47)	10 (6)	15 (26)	0 (47)	10 (6)	15 (26)
Thailand	01/01/2001	10	15 (6,20)	5 (21)	10	15 (6,20)	5 (21)
Ukraine (19)	01/01/2014	5 (41)	2	10 (42)	5 (41)	2	10 (42)
U.A.E	01/01/2014	0	0	0	0	0	0
United Kingdom	01/01/1973 (40)	0	10	0 (3)	15 (14)	10	0 (3)
United States	01/01/1986	0	10 (10)	0	5 (50)	10 (10)	0

1. Under Cyprus legislation there is no withholding tax on dividends, interests and royalties paid to non-residents of Cyprus.
2. In case where royalties are earned on rights used within Cyprus there is withholding tax of 10 per cent.
3. Five per cent on film and TV royalties.
4. Zero per cent if paid to a Government or for export guarantee.
5. Zero per cent on literary, dramatic, musical or artistic work.
6. Zero per cent if paid to the Government of the other State.
7. This rate applies for patents, trademarks, designs or models, plans, secret formulas or processes, or any industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience.
8. 15 per cent if received by an individual or if received by a company controlling directly or indirectly less than 25 per cent of the capital of the paying company.
9. 15 per cent if received by an individual or if received by a company directly controlling less than ten per cent of the voting power.
10. Zero per cent if paid to a Government bank or financial institution.
11. The treaty provides for withholding taxes on dividends but Greece does not impose any withholding tax in accordance with its own legislation.
12. Five per cent on film royalties (apart from films broadcasted on television).
13. Five per cent if received by a person controlling less than 50 per cent of the voting power.
14. Zero per cent if recipient is a company which alone or together with associated companies) control directly or indirectly at least ten per cent of voting power.
15. Ten per cent for payments of a technical, managerial or consulting nature.
16. Ten per cent if dividend paid by a company in which the beneficial owner has invested less than EUR 100.000.
17. If the investment is less than EUR 200.000, dividends are subject to 15 per cent withholding tax which is reduced to ten per cent if the recipient is the beneficial owner and directly controls 25 per cent or more of the share capital of the paying company.
18. No withholding tax for interest on deposits with banking institutions.
19. The old USSR/Cyprus treaty is applicable until 31 December 2013. From 1 January 2014, the provisions of the Ukraine-Cyprus Double Tax Treaty enter into force.
20. Ten per cent on interest received by a financial institution or when it relates to sale on credit of any industrial, commercial or scientific equipment or of merchandise.
21. This rate applies for any copyright of literary, dramatic, musical, artistic or scientific work. A ten per cent rate applies for industrial, commercial or scientific equipment. A 15 per cent rate applies for patents, trademarks, designs or models, plans, secret formulae or processes.
22. This rate applies to companies holding directly at least 25 per cent of the share capital of the company paying the dividend. In all other cases the withholding tax is ten per cent.
23. This rate does not apply if the payment is made to a Cyprus international business entity by a resident of Bulgaria owning directly or indirectly at least 25 per cent of the share capital of the Cyprus entity.
24. Seven per cent if paid to a bank or financial institution.
25. Montenegro and Serbia apply the Yugoslavia/Cyprus treaty.
26. A rate of ten per cent applies to copyrights on literary, artistic and scientific work including cinematograph films, and films or tapes for television or radio broadcasting.
27. The zero per cent is applicable if the beneficial owner has invested in the capital of the company not less than the equivalent of 150.000 Euro at the time of the investment. In all other cases the rate is five per cent.
28. Zero per cent if dividends received and beneficially held by a company directly holding at least ten per cent of the capital of the company paying the dividends for an uninterrupted period of at least one year.
29. Zero per cent of the gross amount of the dividends if the beneficial owner is a company (other than a partnership) which holds directly at least ten per cent of the capital of the company paying the dividends where such holding is being possessed for an uninterrupted period of no less than one year, 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 or 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.
30. 15 per cent if received by an individual or if received by a company directly holding less than ten per cent of the share capital of the company paying the dividends.
31. A protocol signed on 21 May 2012 entered into force on 11 January 2013 and is effective as of 1 January 2014. The protocol introduces new provisions on exchange of Information but does not amend the existing withholding rates set by the original Treaty.
32. The provisions of the Treaty enter into force on 1 January 1993 for Cyprus and 1 April 1993 for India.
33. The provisions of the Treaty enter into force on 1 January 1962 for Cyprus and 1 April 1962 for Ireland.
34. An amending protocol, signed on 4 June 2009, entered into force on 23 November 2010. The Protocol introduces clarifications as to the elimination of double taxation and further new provisions on exchange of information but does not amend the existing withholding rates set by the original Treaty.

35. By Exchange of Notes, the Convention of 2 May 1951 concluded between Norway and the United Kingdom has been extended, in accordance with Article XX, to Cyprus. A new DTT has been signed between Cyprus and Norway on 5 December 2013. The Treaty is not in force yet. It provides that the WHT on dividends is 15 per cent or zero per cent (subject to conditions) and the WHT on interest and royalty payments is zero per cent.
36. An amending protocol, signed on 22 March 2012, entered into force on 9 November 2012. The protocol introduces among others new rates for dividend and interest as well as further amendments to the initial Treaty; the withholding rates outlined herein refer to the new rates introduced by the Protocol.
37. The zero per cent is applicable if the beneficial owner holds directly at least ten per cent of the capital of the company paying the dividend for an uninterrupted period of 24 months. In all other cases the rate is five per cent.
38. An amending protocol, signed on 7 October 2012, entered into force on 2 April 2012. The provisions of the new Protocol are effective as of 1 January 2013 with the exception of the Provisions on “Gains from Alienation of Property” (1 January 2017) and the provisions on “Assistance in Collection” that will generally apply upon the introduction of the necessary legal basis by Cyprus. The Protocol introduces among others, new exchange of information provisions but does not amend the existing withholding rates set by the original Treaty.
39. In an Exchange of Letters dated 10 December 1999 and 10 January 2000, Cyprus and the Slovak Republic agreed to continue to apply the Czechoslovak treaty of 15 April 1980 in relations between the two states.
40. The provisions of the Treaty enter into force on 1 January 1973 for Cyprus and 1 April 1973 for the United Kingdom.
41. The five per cent applies where the company receiving the dividend owns at least 20 per cent in the capital of the paying company or has invested an amount of at least EUR100.000. In all other cases, a 15 per cent withholding shall apply.
42. A reduced five per cent withholding tax in respect of the use or the right to use any copyright of scientific work, patent, trade mark, secret formula, process or information concerning industrial, commercial or scientific experience will apply under the new Treaty. In all other cases a general withholding tax on royalties of ten per cent will apply.
43. Five per cent if the recipient is an individual or if the recipient is a company directly holding less than ten per cent of the capital.
44. Pending exchange of ratification documents.
45. This rate applies to companies who are the beneficial owners of the dividend and hold directly at least ten per cent of the share capital of the company paying the dividend. In all other cases the withholding tax is five per cent.
46. The Treaty has been signed but ratification and entry into force is pending.
47. 15 per cent if received by an individual or if received by a company controlling directly less than 25 per cent of the capital of the paying company
48. 15 per cent if received by an individual or if received by a company controlling less than ten per cent of shares.
49. Reference to interest has been deleted through a subsequent modification of the DTT.
50. To be entitled to this rate (a) must be a corporation, AND (b) minimum ten per cent ownership of the outstanding shares of the voting stock during the part of the paying corporation’s taxable year which precedes the date of payment of the dividend and during the whole of its prior taxable year (if any), AND (c) not more than 25 per cent of the gross income of the corporation paying the dividends (for such prior taxable year (if any)) consists of interest/dividends (other than interest derived from the conduct of a banking, insurance, or financing business and dividends/interest received from subsidiary corporation, 50 per cent or more of the outstanding shares of the voting stock of which is owned by the paying corporation at the time such dividends/ interest is received). Otherwise a 15 per cent WHT rate applies.

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