

Corporate income taxation in Cyprus - 2017

Basis of taxation

All Cyprus tax resident companies are taxed on their income accrued or derived from all chargeable sources in Cyprus and abroad. A non-Cyprus tax resident company is taxed on income accrued or derived from a business activity which is carried out through a permanent establishment in Cyprus and on certain income arising from sources in Cyprus.

A company is a resident of Cyprus if it is managed and controlled in Cyprus.

Foreign taxes paid can be credited against the Corporation Tax liability.

The corporation tax rate for all companies is 12,5%.

Exemptions

1. Profit from the sale of securities. The term "Securities" is defined as shares, bonds, debentures, founders' shares and other securities of companies or other legal persons, incorporated in Cyprus or abroad and options thereon. Circulars have been issued by the Tax Authorities further clarifying what is included in the term Securities. According to the circulars the term includes, among others, options on Securities, short positions on Securities, futures/forwards on Securities, swaps on Securities, depositary receipts on Securities (ADRs, GDRs), rights of claim on bonds and debentures (rights on interest of these instruments are not included), index participations only if they result on Securities, repurchase agreements or Repos on Securities, units in open-end or close-end collective investment schemes. The circulars also clarify specific types of participation in foreign entities which are considered as Securities.
2. Dividends (excluding, as from 1 January 2016, dividends which are tax deductible for the paying company). Such dividend income may be subject to Special Contribution for Defence.
3. Interest not arising from the ordinary activities or closely related to the ordinary activities of the company. All the interest income of Collective Investment Schemes is considered to be arising from the ordinary activities or closely related to the ordinary activities of the Scheme. Such interest income may be subject to Special Contribution for Defence.
4. Profits of a foreign permanent establishment. With effect as from 1 July 2016, taxpayers may elect to tax the profits earned by a foreign permanent establishment, with a tax credit for foreign taxes incurred on those foreign permanent establishment profits. Transitional rules apply in certain cases on the granting of foreign tax credits where a foreign permanent establishment

was previously exempt and subsequently a taxpayer elects to be subject to tax on the profits of the foreign permanent establishment.

5. Gains relating to foreign exchange differences (forex) with the exception of forex arising from trading in foreign currencies and related derivatives.

Deductions

Generally, expenses incurred wholly and exclusively in earning taxable income and supported by documentary evidence are deductible for corporate tax purpose, including:

1. Interest expense incurred for the direct or indirect acquisition of 100% of the share capital of a subsidiary company will be treated as deductible for income tax purposes provided that the 100% subsidiary company does not own (directly or indirectly) any assets that are not used in the business. If the subsidiary owns (directly or indirectly) assets not used in the business the interest expense deduction is restricted to the amount which relates to assets used in the business. This applies for acquisitions of subsidiaries from 1 January 2012.
2. Equity introduced to a Cyprus company or a permanent establishment of a non-Cyprus tax resident company as from 1 January 2015 (new equity) in the form of paid-up share capital or share premium is eligible for an annual notional interest deduction (NID). New equity can be contributed either in cash or in kind. In the case of assets in kind the amount of new equity may not exceed the market value of the asset, which must be substantiated. Reserves existing as at 31 December 2014 can only be considered as new equity if they are used for financing new business activities. The annual NID deduction is calculated as an interest rate on the new equity. The relevant interest rate is the yield on 10-year government bonds (as at December 31 of the prior tax year) of the country where the funds are employed in the business of the company plus a 3% premium (subject to a minimum amount which is the yield on the 10 year Cyprus government bond as at the same date plus a 3% premium). For 2016, the minimum relevant interest rate is 6,685%. A taxpayer may elect not to claim all or part of the available NID for a particular tax year. The NID deduction cannot exceed 80% of the taxable profit derived from assets financed by new equity (as calculated prior to the NID deduction).
3. 80% of the net profit, as calculated using the modified nexus fraction, of royalty income, embedded income and other qualifying income derived from qualifying intangible assets in the 'new' Cyprus intellectual property (IP) box (provision applies with effect from 1 July 2016). 'Intangible assets' comprise patents, copyrighted software, utility models, intangible assets that grant protection to plants and genetic material, orphan drug designations, extensions of patent protection. It also comprises of other intangible assets which are non-obvious, useful and novel, that are certified as such by a designated authority, and where the taxpayer satisfies size criteria (i.e. annual IP related revenue does not exceed €7,5m for the taxpayer, and group total annual revenue does not exceed €50m, using a 5-year average for both calculations). A fraction is applied to the net profit based on research and development (R&D) activity of the taxpayer; the higher the amount of R&D undertaken by the taxpayer itself (or via a taxable foreign permanent establishment or via unrelated third party outsourcing), the higher the amount of R&D fraction (modified nexus fraction).

4. 80% of the net profit of royalty income, embedded income and other qualifying income derived from qualifying intangible assets in the 'old' Cyprus IP box. The term 'intangible assets' includes copyrights, patents and trademarks. The old Cyprus IP box closed as from 30 June 2016. Under transitional/grandfathering rules, taxpayers with intangible assets that were already included in the old Cyprus IP box as at 30 June 2016 continue to apply the old Cyprus IP box provisions for a further five years i.e. until 30 June 2021 for those intangible assets. A much shorter transitional/grandfathering period to 31 December 2016 is applied in the case of intangible assets acquired directly or indirectly from related parties during the period 2 January 2016 – 30 June 2016, unless at the time of acquisition such intangible assets were already benefitting from an IP box (including the Cyprus IP box) or were not acquired with the main purpose (or one of the main purposes) being tax avoidance. Embedded income and income earned from intangible assets economically but not legally owned will only qualify in the relevant transitional/grandfathering period if earned from those type intangible assets that would qualify for the new Cyprus IP box (i.e. patents, copyrighted software, etc.). Additionally, any expenditure of a capital nature incurred for the acquisition or development of such intangible assets may be claimed as a tax deduction in the year in which it was incurred and the immediate four following years on a straight-line basis.
5. Tax amortisation on any expenditure of a capital nature for the acquisition or development of IP (provision applies with effect from 1 July 2016) allocated over the lifetime of the IP (maximum period 20 years). Expenditure excludes goodwill and intangible assets falling under the transitional rules of the old Cyprus IP box which continue with that box's tax amortisation (see above). A taxpayer may elect not to claim all or part of the available tax amortization for a particular tax year.
6. Donations to approved charities (with receipts).
7. Employer's contributions to social insurance and approved funds on employees' salaries.
8. Employer's contributions to:
 - Medical fund for employees (up to 1% of employee's remuneration)
 - Provident/Pension fund for employees (up to 10% of employee's remuneration)
9. Any expenditure incurred for the maintenance of a building in respect of which there is a Preservation Order (Up to €700, €1.100 or €1.200 per square meter, depending on the size of the building).
10. Entertainment expenses for business purposes (lower of €17.086 or 1% of the gross income/turnover of the business).

Specific non-deductible expenses

1. Expenses of a private motor vehicle.
2. Interest applicable to the cost of acquiring a private motor vehicle, irrespective of its use, and to the cost of acquiring any other asset not used in the business, for 7 years from the date of acquisition of the asset.

Losses carried forward

The tax loss incurred during a tax year and which cannot be set off against other income, is carried forward subject to conditions and set off against the profits of the next five years.

The current year loss of one company can be set off against the profit of another, subject to conditions, provided the companies are Cyprus tax resident companies of a group. As from 1 January 2015 a Cyprus tax resident company may also claim the tax losses of a group company which is tax resident in another EU country, provided such EU company firstly exhausts all possibilities available to utilise its losses in its country of residence or in the country of any intermediary EU holding company.

Group is defined as:

1. One Cyprus tax resident company holding directly or indirectly at least 75% of the voting shares of another Cyprus tax resident company.
2. Both of the companies are at least 75% (voting shares) held, directly or indirectly, by a third company.

As from 1 January 2015, interposition of a non- Cyprus tax resident company(ies) will not affect the eligibility for group relief as long as such company(ies) is/are tax resident of either an EU country or in a country with which Cyprus has a double tax treaty or an exchange of information agreement (bilateral or multilateral).

A partnership or a sole trader transferring a business into a company can carry forward tax losses into the company for future utilisation.

Losses from a permanent establishment abroad can be set off with profits of the company in Cyprus. Subsequent profits of an exempt permanent establishment abroad are taxable up to the amount of losses allowed.

Reorganisations

Transfers of assets and liabilities between companies can, subject to conditions, be effected without tax consequences within the framework of a reorganisation and tax losses can be carried forward by the receiving entity.

Reorganisations include mergers, demergers, partial divisions, transfer of assets, exchange of shares, transfer of registered office of a European company (SE) or a European cooperative company (SCE).

Annual wear and tear allowances on tangible fixed assets

The following allowances which are given as a percentage on the cost of acquisition are deducted from the chargeable income:

Fixed assets

Plant and machinery (1)	%
Plant and machinery	10
Furniture and fittings	10
Industrial carpets	10
Boreholes	10
Machinery and tools used in an agricultural business	15
Buildings (2)	%
Commercial buildings	3
Industrial, agricultural and hotel buildings (3)	4
Flats	3
Metallic greenhouse structures	10
Wooden greenhouse structures	33 1/3
Vehicles and Means of Transportation (1)	%
Commercial motor vehicles	20
Motor cycles	20
Excavators, tractors, bulldozers, self-propelled loaders and drums for petrol companies	25
Armoured Motor Vehicles (e.g. used by Security Services)	20
Specialised Machinery for the laying of Railroads (e.g. Locomotive engines, Ballast wagons, Container wagons and Container Sleeper Wagons)	20
New Airplanes	8
New Helicopters	8
Sailing vessels	4,5
Motor Yachts	6
Steamers, tugs and fishing boats	6
Shipmotor launches	12,5
New cargo vessels	8
New passenger vessels	6
Used cargo/passenger vessels	Useful life

Other (1)	%
Televisions and videos	10
Computer hardware and operating systems	20
Application software	33 1/3
Expenditure on application software less than €1.709, is written off in the year of acquisition	
Wind Power Generators	10
Photovoltaic Systems	10
Tools in general	33 1/3
Videotapes property of video clubs	50

Notes

1. Plant and machinery, vehicles (excluding private motor vehicles) and other assets acquired during the tax years 2012 - 2016 (inclusive) are eligible to accelerated tax depreciation at the rate of 20% (excluding such assets which are already eligible for a higher annual tax rate of tax depreciation).
2. The rates stated for buildings are for new buildings. Rates are amended in the case of second-hand buildings.
3. In the case of industrial and hotel buildings which are acquired during the tax years 2012 - 2016 (inclusive), an accelerated tax depreciation at the rate of 7% per annum applies.

Shipping companies

The Merchant Shipping Legislation fully approved by the EU provides for exemption from all direct taxes and taxation under tonnage tax regime of qualifying ship-owners, charterers and ship-managers, from the operation of qualifying community ships (ships flying a flag of an EU member state or of a country in the European Economic Area) and foreign (non-community) ships (under conditions), in qualifying activities.

The legislation allows non-community vessels to enter the tonnage tax regime provided the fleet is composed by at least 60% community vessels. If this requirement is not met, then non-community vessels can still qualify if certain criteria are met.

The legislation includes an "all or nothing" rule, meaning that if a ship-owner/ charterer/ ship-manager of a group elects to be taxed under the tonnage tax regime, all ship-owners/ charterers/ ship-managers of the group should elect the same.

Exemption is also given in relation to the salaries of officers and crew aboard a Cyprus ship.

Ship-owners

The exemption applies to:

1. Profits derived from the use/chartering out of the ships.
2. Interest income relating to the working capital of the company.
3. Profits from the disposal of qualifying ships.
4. Dividends received from the above profits at all distribution levels.
5. Profit from the disposal of ship-owning companies and its distribution.

The exemption also applies to the bare boat charterer of a vessel flying the Cyprus flag under parallel registration.

Charterers

The exemption applies to:

1. Profits derived from the operation of chartered in ships.
2. Interest income relating to the working capital of the company.
3. Dividends received from the above profits at all distribution levels.

The law grants the exemption provided that the option to register for Tonnage Tax is exercised for all vessels and provided a composition requirement is met: at least 25% (reduced to 10% under conditions) of the net tonnage of the vessels owned or bare boat chartered in.

Ship-managers

The tax exemption covers:

1. Profits from technical and/or crew management.
2. Dividends paid out of these profits at all levels of distribution.
3. Interest income relating to the working capital of the company.

In order to qualify, ship-managers must satisfy the following additional requirements:

1. Maintain a fully-fledged office in Cyprus with personnel sufficient in number and qualification.
2. At least 51% of all onshore personnel must be community citizens.
3. At least 2/3 of total tonnage under management must be managed within the community (any excess of 1/3 taxed under corporation tax).

The application of the tonnage tax system is compulsory for owners of Cyprus flag ships and optional for owners of non-Cyprus flag ships, charterers and ship-managers. Those who choose to enter the Tonnage Tax regime must remain in the system for at least 10 years unless they had a valid reason to exit such as disposal of their vessels and cessation their activities.

Insurance companies

Profits of insurance companies are liable to corporation tax similar to all other companies, except in the case where the corporation tax payable on taxable profit of life insurance business is less than 1,5% of the gross premium. In this case, the difference is paid as additional corporation tax.