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Cyprus Tax legislation reform

In an effort to accelerate growth and attract foreign investment, Cyprus introduced a several amendments to tax law on July 9, 2015. The laws that have been modified are:

i. The Income Tax Law;
ii. The Special Contribution for Defence Law; and
iii. The Capital Gains Tax Law

1. The Income Tax Law

Deemed interest deduction on new equity

With the new amendment it is being introduced in Article 9 of the Law a provision which provides for a Notional Interest Deduction (NID) in taxable income of Cyprus tax residents companies. The NID will be calculated as a percentage of the reference interest rate on the new equity. The new equity should have a significant economic or commercial purpose.

- Reference Interest Rate is the yield of the 10 year government bond of the country in which the new equity is invested plus a 3% premium, having as a minimum rate the 10 year Cyprus government bond yield as at 31 December of the tax year preceding the relevant tax year, plus a 3% premium.

- New Equity is the equity introduced in the business on or after 1 January 2015 and does not include amounts that have been capitalized and which were derived from revaluation of movable or immovable property or amounts that are derived directly or indirectly from reserves that existed as at 31 December 2014 and are not related with new assets. Also the term equity is defined as issued share capital and share premium, provided that these are fully paid.

Additionally, the legislation includes the following provisions:

- The NID granted on new equity cannot exceed 80% of the taxable profit as calculated before allowing the NID. It is further provided that in the case of a loss such deduction is not granted.
- A company may in any given tax year elect to claim the whole or part of the amount of the NID available.
- In the case where equity is contributed in the form of assets, the amount of equity must not exceed the market value of those specific assets.
- In the case where the new equity is derived directly or indirectly from loans on which interest expense deduction is claimed, the NID on the new equity is reduced accordingly.

2. Special Contribution for Defence Law

Discharge of individuals which are not domiciled in Cyprus from the imposition of Special Contribution for Defence

With the new amendment to the legislation, it is being introduced the term "*domicile in the Republic*" which provides the following:

- An individual has a "domicile in the Republic" when:

(a) He/she has a domicile of origin in Cyprus based on the provisions of the Wills and Succession Law (WSL) (i.e. domicile of the father at the time of birth), except for:

i. An individual who has acquired and maintains a domicile of choice outside Cyprus based on the provisions of the WSL, provided that he/she has not been resident in Cyprus as defined in accordance with the provisions of the Income Tax Law (ITL) for any period of at least 20 consecutive years prior to the relevant tax year, or

ii. An individual who has not been resident in Cyprus as defined in accordance with the provisions of the ITL for a period of at least 20 consecutive years immediately prior to the entry into force of the provisions of this Law or

(b) Regardless from (a) above, any individual who is resident in Cyprus, as defined in accordance with the provisions of the ITL for at least 17 out of the last 20 years prior to the relevant tax year.

An individual which has not a domicile in Cyprus, is exempted from the payment of Special Contribution for Defence (SDC), regardless if he/she is a tax resident of Cyprus.

Based on the above, individuals who are not domiciled in Cyprus but they are Cyprus tax residents, are exempt from SDC on interest and dividends which are not derived from trading activities, from sources inside or outside Cyprus. In the case of rental income, this will be taxable only under the provisions of ITL.

Lastly, the legislation provides that in the case where any person domiciled in Cyprus transfers assets to a relative up to third degree who is not domiciled in Cyprus, for the main purpose to avoid the imposition of SDC, the income arising from these assets is subject to SDC.

3. Capital Gains Tax Law

Exemption from Capital Gains Tax Law for immovable property acquired between 16 July 2015 and 31 December 2016

With the new amendment, any gains that arise from the sale of immovable property that was acquired between the above mentioned dates, is exempt from Capital Gains Tax (CGT) irrespectively from the date of sale. Based on the provisions of the law, the following terms are explained: “Immovable property” is land with buildings or buildings and which was acquired through purchase or purchase agreement and not through an exchange or donation at market value, from a non-related party.