

# INTERNATIONAL TAX STRUCTURE

## INVESTING HOLDING STRUCTURE

A Cyprus holding company is ideal for investments in EU as well as non – EU companies.

It is widely used as an ultimate or intermediary holding company in a number of structures including the holding of operating, financing, real estate as well as shipping companies.

### KEY FEATURES

- Foreign taxes on dividends as well as on other payments received by the Cyprus resident companies are eliminated or minimised due to access to an extensive and favourable double tax treaty network and due to access to the EU Parent Subsidiary Directive.

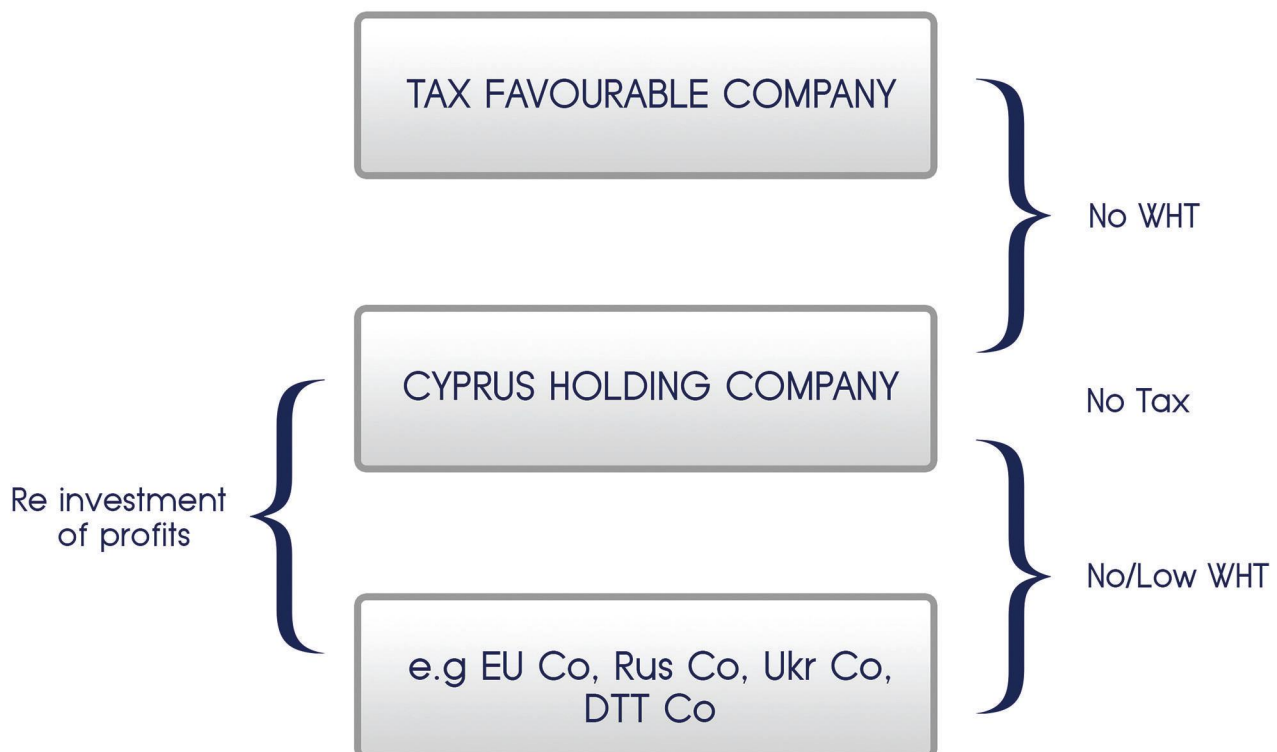
### TAX EFFICIENT REPATRIATION OF PROFITS

No taxes on payments to foreign shareholders of the Holding Company:

- On dividends
- Profit on disposal of the holding company
- Proceeds from the liquidation or capital reductions

### ADDITIONAL BENEFITS

- Reinvestment of profits without any tax leakages
- No Controlled Foreign Companies (CFC) rules



## FINANCING COMPANIES STRUCTURES

There are 2 types of financing structures that can be used.

We propose the (A) structure since no challenges can be raised about the interest income which is the CY Finco.

(B) structure has strong argument that Cy Finco is the beneficial owner of the interest income but challenges may be raised.

### (A) FINANCING COMPANY STRUCTURE (NOTIONAL INTEREST DEDUCTION)

#### Notional interest deduction – The Basics

The Notional interest Deduction ("NID") is a new powerful tool provided to local and international businesses which enables them to de-leverage and realise a tax efficient return on new (qualifying) equity. This return is achieved through the deduction of a "notional" interest expense from their taxable income.

#### Purpose and Scope

##### Why was the NID introduced in Cypriot Legislation?

Alignment of the tax treatment of equity finance with tax treatment of debt finance. Before the introduction of the NID, remuneration for debt financing was generally tax deductible while equity financing was not.

Promotion of capital – intensive investments in Cyprus. Through the introduction of the NID Cypriot companies can be used as financing, central procurement and factoring centres of international groups.

As an additional support for small and medium sized businesses.

##### Who can benefit from the NID?

Cyprus tax resident companies and the Cyprus permanent establishments of non – Cyprus tax resident companies.

The NID is a useful tool for enterprises seeking new options for financing operations.

Financing can now be considered as a useful alternative to the debt financing norm as Cypriot companies can achieve through the NID effective tax rates of up to 2,5%

## The NID explained

### General

A tax deduction is allowed following the application of the NID rate to the amount of New Equity injected to Cyprus companies or permanent establishments of non – Cyprus tax resident companies.

The NID is deductible in a similar manner as for actual interest expense (i.e only if it is used to finance most types of business assets).

NID is deducted following the determination of a company's taxable profit. The deduction cannot exceed 80% of the taxable profit (as calculated prior to NID) of the Company/permanent establishment.

As the NID is a “notional” deduction there is no need for any expense being booked or any exchange of funds to take place in order for the NID to apply.

### New Equity

New equity for the purposes of the NID means equity contributed as from 1 January 2015 in the form of paid up share capital or share premium.

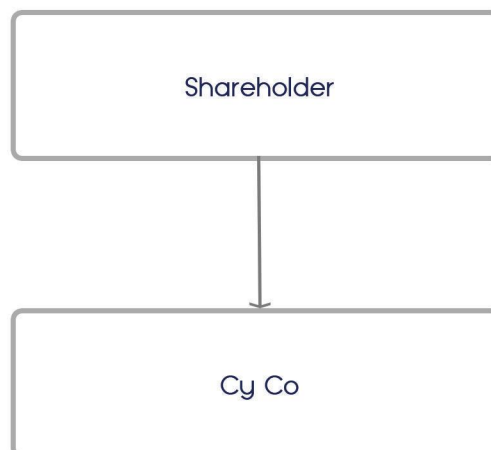
New equity can be contributed either in cash or in kind.

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.

### NID Rate

The NID rate is the yield on the 10 year government bonds (as at 31 December the year preceding the tax year the NID is claimed) of the country where the funds are employed in the business of the company plus a 3% premium. This is subject to a minimum amount which is the yield of the 10 year Cyprus Government bond (defined similarly as above) plus a 3% premium.





#### Practical examples

For the purposes of the below example it is assumed that New Equity amounting to 1.000.000 is contributed to Cy Co and that an 8% NID interest rate is applicable.

	Not taking into consideration the NID	After taking into consideration the NID
Taxable profit	100.000	100.000
NID		80.000
Taxable profit	100.000	20.000
Tax	12.500	2.500
Effective tax rate	12,5%	2,5%

#### Advantages

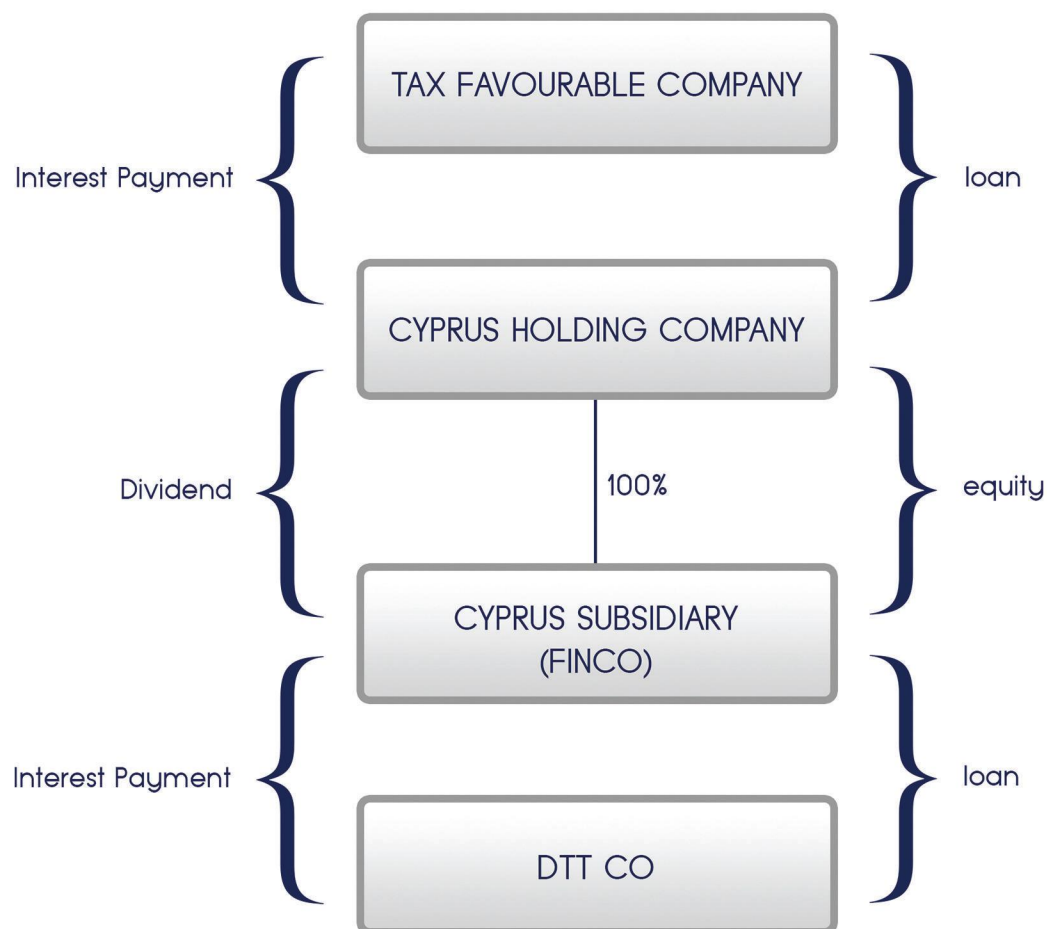
- Can be applied with other incentives for in Cypriot legislation (e.g intellectual property regime)
- Similiar benefits to debt financing
- Companies can maintain tax benefits while increasing their financial robustness

#### How can EVOSERVE AUDITORS LIMITED help?

- Tax efficient structuring of new financing structures
- Review of current structures from a financing nature point of view
- Identify possibilities of efficient debt structures

## (B) FINANCING COMPANY STRUCTURE

- Group financing via Cyprus can be particularly tax efficient. Interest incurred by a Cypriot tax resident company (Cy Holdco) to finance a 100% equity investment to Cypriot tax resident company (Cy Finco) can be tax deductible → Creating tax loss in Cy Holdco.
- Tax loss of Cy Holdco is set – off against taxable income (interest) of Cy Finco.
- After group relief is claimed a small spread in the range of 0,125% – 0,35% is expected to be taxable in Cyprus at 12,5% corporation tax.
- Cy Finco is 100% equity – financed thus strengthening the argument that Cy Finco is the beneficial owner of the interest income.



## INTELLECTUAL PROPERTY (IP) STRUCTURE

Cyprus offers an efficient IP tax regime coupled with the protection afforded by EU Member States and by the signatories of all major IP treaties and protocols.

### The Cyprus IP tax regime

The IP tax regime covers a wide range of individuals including:

- Copyrights, which may take any of the following forms: literary works, dramatic works, musical works, scientific works, artistic works, sound recordings, films, broadcasts, published editions, databases, # publications, software programmes.
- Patented inventions
- Trademarks (and service marks), designs and models that are used or applied on products.

The above is non – exhaustive list.

Registrable IPs need not be registered in Cyprus to benefit from IP regime.

### Tax benefits of Cypriot IP companies

- 80% of worldwide royalty income generated from IP owned by Cypriot resident companies (net of any direct expenses\*) is exempt from income tax.
- 80% of profit generated from the disposal of IP owned by Cypriot resident companies (net of any direct expenses\*) is exempt from income tax.
- Any expenditure of a capital nature for the acquisition or development in the year in which it was incurred and the immediate four following years on a straight – line.

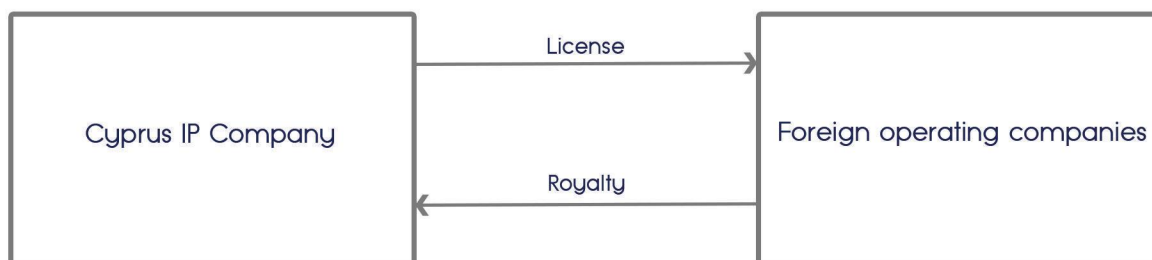
Cyprus' wide double tax treaty network and access to the EU Interest and Royalty Directive serve as additional means for the group to achieve tax optimization when it comes to IP exploitation through Cyprus.

\*Direct expenses include finance costs to acquire/develop IP and annual tax amortization

## Example 1

Assume that a Cyprus IP company licenses its IP to its operating foreign companies and in turn it receives royalty income of €100,000 per year.

Structure is presented below:



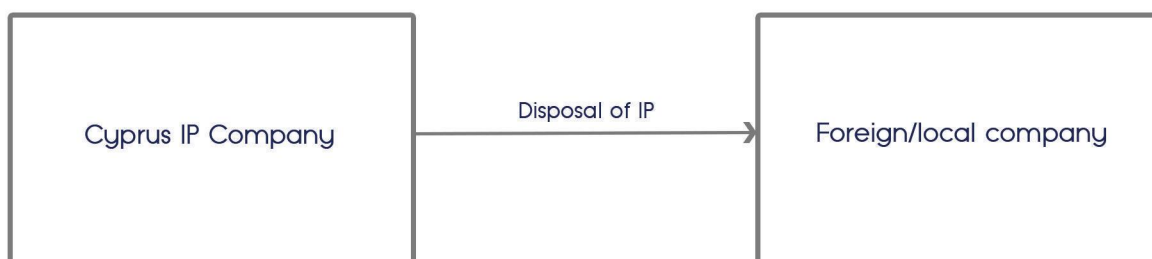
The expected annual tax for the Cyprus IP Company will be as follows:

Annual royalty income	€100,000
Direct expenses (say)	(€20,000)
Net income	€80,000
80% deemed deduction	(€64,000)
Taxable income	€16,000
@12,5% corporation tax	€2,000
Effective tax rate	2%

\*Under the majority of Cyprus double tax treaties on royalty payments is 0%.

## Example 2

Assume that a Cyprus IP company disposes an IP to another foreign/local company for the amount of €100,000. The cost of acquisition of the IP was €50,000 and ammortization was claimed for 2 years.



The expected annual tax for the Cyprus IP Company will be as follows:

Disposal price of IP	€100,000
Less: Cost of acquisition	(€50,000)
Net profit	€50,000
Add: amortization claim for 2 years	(€20,000)
Net income	€70,000
80% deemed deduction	€56,000
Taxable income	€14,000
@12,5% corporation tax	€1,750
Effective tax rate	1,75%

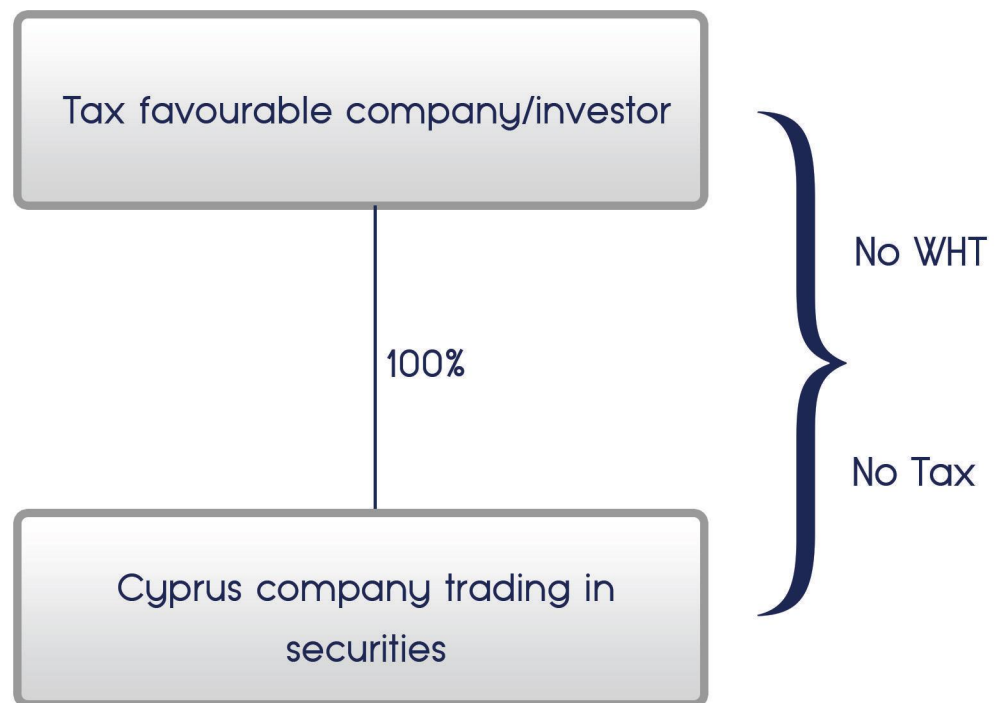
## COMPANIES TRADING IN SECURITIES

Cyprus offers the best tax regime for a company which its activity is the trading in securities.

The term "Securities" is defined a shares, bonds, debentures, founders' shares and other securities of companies or other legal persons incorporated in Cyprus or abroad and options, options on Securities, short positions on Securities, futures/forwards on Securities, swaps on Securities, depositary receipts on Securities (ADRs, GDRs), repurchase agreements or Repos on Securities and etc.

### KEY FEATURES

- Profit from disposal of securities is tax exempt
- No taxes on payment to foreign shareholders (tax favourable company/investor) of the Cyprus company.





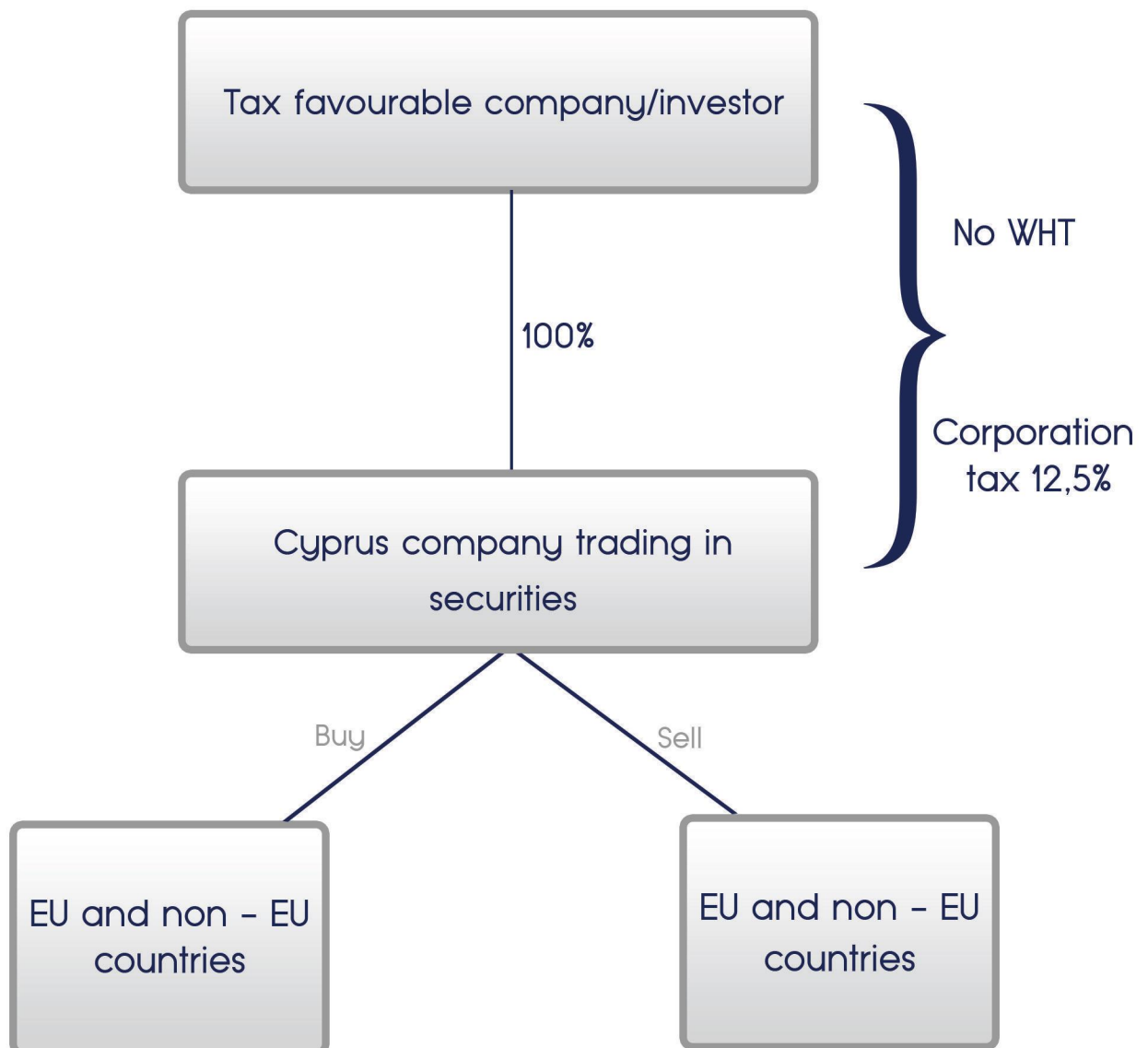
## GENERAL TRADING COMPANIES IN GOODS AND SERVICES STRUCTURE

Cyprus offers the best tax regime for a Company conducting international trading in goods and services.

In case the Cyprus company is dealing with general trading in goods, the physical delivery of the goods in Cyprus is not a requirement.

### KEY FEATURES

- Profit is taxable at a corporation rate of 12,5%
- No taxes on payments to foreign shareholders (tax favourable company/investor) of the Cyprus company.
- VAT registration number for Cyprus Company
- VIES registration number for Cyprus Company in case it sells to other EU Member States



# CYPRUS: THE SHIPPING CENTRE

The Cypriot maritime registry is today one of the largest in the EU and th 10th largest worldwide. Moreover, Cyprus is the biggest third party ship management centre in the EU.

## TAXATION EXEMPTION

The Merchant Shipping Legislation nacted as fro 1st January 2010 places Cyprus in a very competitive position. Cyprus has become the only EU country with an EU approved TT (Tonnage Tax) system that:

- Provides for TT on the net tonnage of the vessels rather than corporationtax on the actual profits, regulated by the DMS (Department of Merchant and Shipping) rather than the Tax Authorities.
- Grants total tax exemption of profits tax and distrubution tax at all levels.
- Allows mixed activities within a company/group (shipping subject to TT and other subject to 12,5% corporation tax).
- Supports an open registry
- Allows split ship management activities (crewing or technical)
- In addition, the favourable income tax legislation compliments the excellent Merchant Shipping Legislation, creating a highly tax efficient harbour for shipping groups and an ideal holding company location.
- Complete tax exemption of all profits and dividends at all levels of distrubution arising from qualifying shipping operations.

## THE TONNAGE TAX SYSTEM

The law provides full exemption to ship owners, charteres and ship managers from all profit taxes and imposes tonnage tax on the net tonnage of the vessels at the following rates.

UNITS OF NET TONNAGE	SHIP OWNERS AND CHARTERERS € TT PER 100 UNITS	SHIP MANAGERS € TT PER 400 UNITS
0 – 1.000	36,50	36,50
1.001 – 10.000	31,03	31,03
10.001 – 25.000	20,08	20,08
25.001 – 40.000	12,78	12,78
>40.000	7,30	7,30



The conditions applicable to each of the three categories, as well as the taxation regime are analysed separately below.

The regime covers **qualifying persons** performing **qualifying activities** in relation to **qualifying vessels**.

**Qualifying activity** for **ship owners and charterers** means maritime transport of goods or people between Cyprus ports and foreign ports/offshore installations, or between foreign ports or offshore installations and specifically includes towage, dredging and cable laying.

Qualifying activity when applied to ship managers means services provided to a ship owner or bareboat charterer on the basis of written agreement in relation to crew and/or technical management.

Qualifying vessel is a sea – going vessel that:

- Has been certified in line with international principles and legislation of the flag country, and
- Is registered in the register of a member country of the International Maritime Organization (IMO) and International Labour Organization (ILO)

The definition includes vessels that transport humanitarian aid but excludes the following vessels:

- Fishing boats
- Boats that are primarily used for the athletic and entertaining purposes boats that have been constructed exclusively for domestic navigation
- Ferry and trailer boats that are used in ports, mouth of rivers and/or rivers
- Fixed offshore constructions that are not used for maritime transport
- Non self – propelled floating cranes
- Non sea – going trailers
- Floating hotels and restaurants
- Floating movable casinos

#### THE TONNAGE TAX SYSTEM: SHIP OWNERS

The TT regime applies to any owner of qualifying vessel that carry out a qualifying activity:

- Cyprus flag vessels
- EU/European Economic Area (EEA) flag vessels that exercised the option to be taxed under the TT regime
- Fleet of EU/EEA and non EU/EEA vessels that exercised the option to be taxed under the TT regime

The tax exemption covers:

- Profits from the use of a qualifying vessel
- Profits from the disposal of a qualifying vessel and/or share and/or interest in it
- Profits from the disposal of shares in a ship owning company
- Dividends paid out of the above profits at all levels of distribution
- Interest income relating to the financing/maintenance/use of a qualifying vessel and the working capital, excluding interest on capital and for investments.

Where an option is exercised to enter the TT system, the ship owner must be a Cyprus tax resident and the option must remain in force for at least 10 years.



## THE TONNAGE TAX SYSTEM: SHIP OWNERS

A qualifying ship manager is a legal person tax resident in Cyprus providing technical and/or crewing services in respect of qualifying vessels (Cyprus/EU/EEA/fleet).  
Commercial management is taxable over corporation tax.

An option exists to pay TT at 25% of the rates applicable to ship owner and characters, for all vessels under management. If the choice is not made, profits are taxable under 12,5% corporation tax.

The fleet qualifying criteria are the same as the ship owners/charterers and so is the minimum 10 year duration.

Ship managers have to meet some additional requirements, namely:

- The ship manager is obliged to maintain a fully – fledged office in Cyprus with sufficient in number and qualification.
- At least 51% of all onshore personnel must be EU/EEA citizens.
- At least 2/3 of the total tonnage under management must be managed within the EU/EEA (any excess of 1/3 taxed under 12,5% corporation tax).

The tax exemption covers:

- Profits from technical and/or crew management.
- Dividends paid out of the above profits at all levels of distribution.
- Interest income relating to the working capital/qualifying activity provided such interest is used to pay expenses relating to ship management, excluding interest on capital used for investments.



## TYPES OF SHIPPING ACTIVITIES

### SHIP OWING

Most of the Cyprus registered ships are owed by Cyprus companies with a wide range of foreign interests.

Due to the fact that every limited liability company is a separate legal entity, it is very common to incorporate a ship owning company for every ship to be registered.

### BAREBOAT CHALLENGE

It is possible to have parallel registration of the vessel under the Cyprus flag by bareboat chartering a vessel to a company formed in Cyprus and for a vessel registered under the Cyprus flag to be bareboat chartered – out to a foreign corporation for parallel registration under a foreign flag, provided the law of the other country recognises the concept of bareboat charter registration.

### SHIP MANAGEMENT HEADQUARTERS

Ship management companies are finding Cyprus increasingly attractive as a base for managing ships under various flags. These companies offer full management services to ship owners worldwide and are engaged in chartering, crewing, ship – broking and similar activities. In order to encourage the establishment of ship management companies and other shipping headquarters in Cyprus, the existing legislation grants such companies and their foreign employees various tax advantages and other incentives.

### OTHER PROVISIONS

- Persons in the TT system are granted annually with a certificate by the Department of Merchant Shipping (DMS), a copy of which is sent to the Tax Office.
- A list is kept by the DMS of all Cyprus flag vessels and their owners that are not considered to carry out a qualifying activity.
- Similar lists are kept by the DMS of all ship owners/charterers/ship managers for foreign flag vessels that either do not carry out a qualifying activity or the choice was not made to enter the TT system.
- Remuneration of crew aboard a Cyprus flag vessel is exempt from income tax.
- Provisions relating to safety apply to ship owners and ship managers.





## CYPRUS: THE PREFERRED LOCATION FOR YACHT REGISTRATION

### YACHT LEASING SCHEME

If the TT regime is a treat for commercial shipping enterprises, the yacht scheme is the icing on the cake. It is not covered by the Merchant Shipping Law, but it operates on the basis of the guidance issued by the Cyprus VAT authorities in cooperation with the tax authorities aiming at making Cyprus one of the most attractive jurisdiction for yacht registration within the EU.

The guidelines issued by the Cypriot VAT authorities with regards to the registration of yachts, simple to comprehend and apply, make Cyprus one of the most attractive jurisdictions in the EU in this area, reducing the effective VAT rate for yacht registration to lower than 3%, through the use of Yacht Leasing Scheme.

#### What is the Yacht Leasing Agreement?

This special regime applies to yachts owned by a Cyprus company which are leased to physical or legal persons. The purpose of this scheme is to determine the percentage of time a yacht spends within the EU based on the yacht size and type and apply VAT according to this percentage.

The lessor (the Cyprus Company being the owner of the yacht) contracts the use of the yacht to the lessee (the legal or natural person who leases the yacht) in return for a consideration.

At the end of the lease period, the lessee may opt to purchase the yacht at a fraction of the original price. Such final purchase is strictly an option which may be exercised by the lessee, at the end of the lease period, for a separate consideration,

#### What is the VAT treatment of the Yacht Leasing Agreement?

For VAT purposes, the leasing of the yachts is considered as a supply of services with the right of deduction of input VAT by the lessor. This supply of services by the lessor, is taxable at the basic VAT rate of 19% but only to the extent that the leased yacht is used within the territorial water of the European Union (EU). A specific condition which applies is that the lessor must be a company registered in Cyprus.

The lessee may be an individual or legal person, irrespective of residence/place of incorporation.

#### How is the use of the yacht within the EU territorial waters calculated?

Taking into consideration the inherent difficulty of trailing the movements of each yacht in order to determine the time that the yacht is used within the territorial waters of the EU and the time it is used outside the EU, the Yacht Leasing Guidelines provide that Cyprus VAT will only be applied on a percentage of the lease consideration. The applicable percentages have been determined by the Cypriot tax authorities and depend on the length and type of the yacht (motor or sailing yachts) and indicate the presumed length of use of the yacht in EU waters. There is therefore, no need to maintain for VAT purposes, any detailed record or log books of the movements of the yacht.





### Certificate confirming VAT payment

On entering into the scheme, the Tax Authorities will issue a Provisional VAT paid certificate. In the case where the lessee exercises the option to buy the yacht at the end of the lease period, the Tax authorities will issue a certificate to the lessee confirming full payment of the total VAT liability, provided that all the VAT liability has been paid.

### What is the Yacht Leasing Agreement?

The VAT treatment prescribed in the Yacht Leasing Guidelines will apply if the following conditions are met:

- A lease agreement is concluded between a Cyprus company and an individual or legal person, irrespective of residence/place of incorporation (as a lessee). Using two Cyprus companies is recommended.
- The yacht arrives in Cyprus within 1 month from the date of inception of the lease agreement. Any extension of the above mentioned time limit may only be given by the Tax Commissioner. Such extension shall not exceed under any circumstances the time at which the option to purchase the yacht is exercised.
- An initial payment amounting to at least 40% of the value of the yacht must be paid by the lessee to the lessor at the inception of the lease agreement.
- The lease payments are payable on a monthly basis, and the lease period must under no circumstances exceed the period of 48 months.
- The lessee may purchase the yacht at the end of the lease period, for a final consideration of not less than 2,5% of the value of the yacht.
- The lessor is expected to make a total profit from the leasing agreement of at least 5% on the initial value of the yacht.
- The prior approval of the Tax Commissioner needs to be obtained for the application of the Yacht Leasing Guidelines in each case. Such approval will cover the acceptability of the initial value of the yacht and the applicable percentage of the use within EU waters on the basis of which VAT will be applied. The application of the Tax Commissioner must be accompanied by documentation supporting the purchase price/value of the yacht and a copy of the lease agreement concluded between the two parties.

### Income Tax Treatment

The total profit from the leasing agreement which amounts to 5% on the initial value of the yacht, will be subject to Income Tax at the rate of 12,5%.

### Applicable effective tax rate

The table below indicates presumed percentage of use of the yacht in EU waters and the effective tax rate:

Table A: Motor Boats		
Length of yacht	Percentage of use within EU waters	Effective tax rate on lease payments
Over 65 meters	10%	3,05%
45,01 – 65	15%	4,02%
24,01 – 45	20%	5%
14,01 – 24	30%	6,94%
8,01 – 14	50%	10,84%
Up to 8 meters	60%	12,79%

Table B: Sailing Boats		
Length of yacht	Percentage of use within EU waters	Effective tax rate on lease payments
Over 65 meters	10%	3,05%
45,01 – 65	15%	4,02%
24,01 – 45	20%	5%
20,01 – 24	30%	6,94%
10,01 – 14	50%	10,84%
Up to 8 meters	60%	12,79%