

Tax News

After extensive discussions between the political parties, the Government, the trade unions and the business community, the House of Representatives voted on Friday 26 August 2011, as a first step, amendments to various tax legislations and others, in order to raise revenues and decrease government spending to enable the Government to deal with the economic crisis which Cyprus faces. These changes relate to increasing various taxes, introducing a levy for all companies incorporated in Cyprus, as well as introducing/increasing contributions to pension schemes of employees of the government, local authorities and semi-governmental organisations, and introducing a special levy for two years on the salaries and pensions paid to employees of the government, local authorities and semi-governmental organisations.

In the next few months a second and possibly a third package of additional measures is expected to be voted by the House of Representatives, which hopefully should concentrate on further deductions in government expenditure. The increase in the VAT rate from 15% to 17% is expected to be approved with the second package of measures. The most significant changes in the tax and company legislation are set out below:

The Income Tax Law

- ▶ **Increase in the maximum personal income tax rate to 35%**
A new income tax rate of 35% is introduced for individuals on taxable income in excess of €60.000.
- ▶ **Tax incentives for the employment in Cyprus of highly paid non Cypriot resident individuals**
In order to encourage the establishment or expansion in Cyprus of new businesses, tax incentives are offered for the employment in Cyprus of persons who are not tax residents of Cyprus. In such a case, if the income from employment exceeds €100.000 per annum, a 50% deduction is allowed for such income for the first 5 years of employment.
The incentive is granted both to Cypriots and non Cypriots, on condition that prior to employment in Cyprus such a person was resident outside Cyprus and was not considered as a tax resident of Cyprus.
- ▶ **Entry into force**
The increase in the personal tax rate will come into effect as from 1 January 2011, whereas the incentive for new employees will come into force for employments starting as from 1 January 2012.

The Special Contribution for the Defence of the Republic Law

▶ Increase in the rate of defence tax on interest from 10% to 15%

The rate of special contribution for the Defence of the Republic ("defence tax") on interest received or credited by Cypriot tax residents is increased from 10% to 15%. This applies to both individuals and corporations. In the case of corporations, if the interest results from the ordinary carrying on of any business, including any interest closely connected with the ordinary carrying on of the business, it is not subject to defence tax, but instead is subject to corporate income tax. Therefore, financing companies, including companies involved in intra - group financing activities, are not expected to be affected from the change in the rate.

It should be noted that no defence tax is payable on interest payments to non residents. It should also be noted that this provision applies to interest received by resident individuals or corporations, both from sources within Cyprus and outside of Cyprus.

For provident funds defence tax on interest received remains at 3%, as well as in the case of an individual whose total income for the year does not exceed €12.000 (including interest income). The same rate applies to interest received by an individual from Government savings certificates and development stocks.

▶ Increase in the rate of defence tax on dividends from 15% to 17%

The rate of defence tax on dividends received by a Cypriot tax resident is increased from 15% to 17%. This applies only to individuals, since under the provisions of the legislation companies are generally exempt from the payment of defence tax on dividends. The increase in the rate also applies when the deemed distribution rules are applied in cases where a tax resident company does not distribute within two years at least 70% of its after tax profits.

It should be noted that no defence tax is levied on dividends paid to non resident individuals or corporations. It is also noted that the deemed distribution rules are not applicable in the case where shareholders of a resident company are non tax residents of Cyprus. However, the deemed distribution rules are applicable in the case of a Cypriot tax resident company owned by another Cypriot tax resident company, which in turn is owned by non residents. It is expected that shortly such companies will be excluded from the provisions of the deemed distribution rules, therefore there would be a significant benefit for such companies in case of inability to distribute an actual dividend.

▶ Entry into force

The above provisions will enter into force as soon as the new law is published in the official gazette of the Republic.

The Immovable Property Tax Law

The rates applicable for the payment of immovable property tax, which is paid by both individuals and companies on property owned in Cyprus are significantly increased, as well as the threshold as from which taxes are paid is lowered. It should be noted that tax remains levied on the assessed value of the property as at 1 January 1980.

The rates are as follows:

Up to €120.000	0%o
From €120.000 to €170.000	4%o
From €170.001 to €300.000	5%o
From €300.001 to €500.000	6%o
From €500.001 to €800.000	7%o
Over €800.000	8%o

The increase will be effective as from the year 2012.

The Value Added Tax Law

Under existing legislation, individuals who buy or construct a flat or house to be used as private main residence are entitled to apply for a refund amounting to about €17.000 from the Government. This provision is replaced with the introduction of a reduced VAT rate of 5% on the purchase or construction of a house or flat to be used as private main residence, provided the area of the property does not exceed 200 square meters (the reduced rate of 5% also applies on the first 200 square meters if the total area of the property does not exceed 300 square meters).

The Companies Law

- ▶ As from 2011 an annual levy of €350 is introduced for all companies incorporated in Cyprus payable to the Registrar of Companies. For groups of companies the maximum levy is fixed at €20.000
- ▶ The levy for 2011 must be paid by 31 December 2011, whereas the levy for 2012 onwards must be paid by 30 June of each year.
- ▶ Dormant companies, companies which do not own any assets, as well as companies owning property located in the non Government controlled areas of Cyprus are exempted from the payment of the levy.

In case where the levy is not paid within the prescribed period, if the levy is paid within two months from the due date, a penalty of 10% is payable which is increased to 30% if the levy is paid within five months from the due date. If the levy is not paid within five months, the Registrar of Companies will remove the company from the registry (something which is expected to restrict the company from filing documents or requesting certificates from the Registrar's Office). The return of the company to the registry can be effected within two years with the payment of a levy of €500 per annum and thereafter with the payment of a levy of €750 per annum.

About Ernst & Young

Ernst & Young is a global leader in assurance, tax, transaction and advisory services. Worldwide, our 144,000 people are united by our shared values and an unwavering commitment to quality. We make a difference by helping our people, our clients and our wider communities achieve their potential.

For additional information, please contact:

Neophytos Neophytou
Phone: +357 2520 9999
E-mail:
Neophytos.Neophytou@cy.ey.com

Maarten Koper
Phone: +357 2520 9999
E-mail:
Maarten.Koper@cy.ey.com

Petros Liassides
Phone: +357 2220 9999
E-mail:
Petros.Liassides@cy.ey.com

Philippos Raptopoulos
Phone: +357 2520 9999
E-mail:
Philippos.Raptopoulos@cy.ey.com

www.ey.com

© 2011 Ernst & Young
All Rights Reserved.

Ernst & Young refers to the global organization of member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients.

This document contains information in summary form and is therefore intended for general guidance only. It is not intended to be a substitute for detailed research or the exercise of professional judgment. Neither EYGM Limited nor any other member of the global Ernst & Young organization can accept any responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication. On any specific matter, reference should be made to the appropriate advisor.