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Recent Amendments to the Cyprus Taxation Laws

Introduction

The Parliament of the Republic of Cyprus has recently enacted amendments to the Cyprus Taxation Laws, in particular the Income Tax Laws and the Special Contribution for Defence of the Republic Law (“**SCD Law**”), mainly aiming at improving and making more attractive and advantageous for foreign investors the legal framework for the creation and operation of Collective Investment Schemes in Cyprus. These amendments take effect retrospectively from 1 January 2009.

(1) Amendments to the Income Tax Law

- (a) Under sub-section 19 of Section 8 of the Income Tax Law which the entire interest income of an individual and 50% interest income of a company was exempted from income tax (subject to certain conditions). This sub-section has been replaced by a new sub-section 19 which exempts interest income from income tax, whether it is earned by an individual or by a corporation.
- (b) The proviso to sub-section 19 of Section 8 of the Income Tax Law has also been replaced by the extension of the application thereof to interest earned by a collective investment scheme and now this proviso reads as follows:-

“Provided that interest earned by a person in the ordinary course of its business, including interest closely connected with the ordinary course of business, as well as interest earned by a collec-

tive investment scheme of open or closed type, shall not be considered as interest for the purposes of this sub-section.”

Effectively by the application of the above proviso, the interest which is not exempted by the application of the provisions of sub-section 19, as amended, is considered ordinary business income for the purposes of the Income Tax Law.

- (c) At the same time, sub-section 22 of Section 8 of the Income Tax Law, which exempts from income tax profit from the disposal of securities has been amended by the addition thereto of a proviso which reads as follows:

“Provided that the redemption of a participation or share in a collective investment scheme of open or closed type, constitutes disposal of security.”

Effectively not only are profits realised on a sale or otherwise disposal of a share or interest in a collective investment scheme of an open or closed type exempt from any tax in Cyprus, but any profit realised from the redemption of any share or interest in such scheme is also fully exempted from income tax.

(2) Amendments to the SCD Law

- (a) A definition of “shareholder” has been inserted with a view to extend the application of the SCD Law to the holder of a share or interest in a collective investment scheme of open or closed

type.

- (b) The requirement for a minimum holding by a Cyprus resident company of 1% in the capital of a non-resident company for the application of the exemption from the obligation for payment of special defence contribution at 15% of the gross amount of dividends has been abolished and a new proviso has been added.

Under the new proviso any person, individual or corporation, who is a tax-resident in the Republic of Cyprus who is deemed to have received dividends from a collective investment organisation, the creation and operation of which is regulated by the Open-ended Collective Investments in Transferable Securities (UCITS) and Related Matters Law or by any other legislation regulating the creation and operation in the Republic of other collective investment schemes shall be subject to special defence contribution at the rate of 3% on the gross amount of the dividend.

Under this proviso the dividends from organisations of collective investments to any type as set out above, will not be subject to the usual 15% special defence contribution which is otherwise payable but the rate of such contribution is reduced to 3%.

Of course, if the payment is made to a person who is tax resident in the Republic, whether an individual or a corporation, such dividend shall

be fully exempt from special defence contribution in Cyprus.

- (c) An amendment has also been introduced with respect to the imposition of special defence contribution at the rate of 10% on the gross amount of interest earned by a person who is tax resident of Cyprus except where such interest is earned by such person in the ordinary course of its business, including interest closely connected with the carrying of the ordinary course of the business.

Following the amendment, the exemption is extended to also cover interest earned by a collective investment scheme of open or closed type. Therefore, such interest which is exempted from special defence contribution, is considered ordinary business income in accordance with the provisions of the Income Tax Law, as explained in 1(a) above.

- (d) Further to the above, it has been clarified by the amendment to the SCD Law that accumulated undistributed profits of a collective investment scheme of an open or closed type which are distributed to the person entitled thereto in the event of dissolution or liquidation of such a scheme, shall not be subject to special defence contribution. Likewise any redemption of any share or interest in collective investment scheme of an open or closed type shall also be exempt from special defence contribution.

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