



## CHRYSSES DEMETRIADES & CO. LLC

Advocates and Legal Consultants

### Head Office

Fortuna Court, 284 Makarios III Avenue, 3105 Limassol

Postal Address: P.O. Box 50132, 3601 Limassol, Cyprus

Telephone: +357 25 800 000

Facsimile: +357 2558 7191 or +357 2558 7309

E-mail Address: [commercial@demetriades.com](mailto:commercial@demetriades.com)

Website: <http://www.demetriades.com>

Company Registration № 242111

May 2010

## The Merchant Shipping (Fees and Taxing Provisions) Law 44(I)/ 2010

### 1. INTRODUCTION

The long awaited new tonnage tax regime for Cyprus has recently been enacted in the form of The Merchant Shipping (Fees and Taxing Provisions) Law 44 (I)/2010 (the "**Law**"). The Law is wider in scope than its predecessor in that more types of shipping activity may now qualify for the so called "**Tonnage Tax**". The Law governs the taxation regime for (a) shipowners, (b) charterers and (c) shipmanagers who are generally speaking corporations, and as a precondition, must be Cyprus tax resident and must have exercised an option to be taxed under Tonnage Tax. Such corporations are now defined as "**Tonnage Tax Companies**".

In general, Cyprus imposes taxes on any company which is managed and controlled in Cyprus, or carries on business in Cyprus through a permanent establishment.

However, Tonnage Tax Companies will be taxed on the basis of a notional profit calculated on the net tonnage of the ships they own, charter or manage, as the case may be. Thus, these companies' profits and dividends derived from the operation or chartering or management, as the case may be, of a **Qualifying ship** in a **Qualifying Shipping Activity** are exempt from tax under the Income Tax Laws of Cyprus

### 2. DEFINITIONS

"**Qualifying Shipping Activity**" means, any commercial business or activity which constitutes maritime transport, or crew or technical management of qualifying

ships.

"**Maritime Transport**" means, the carriage of goods or passengers by sea outside the territorial sea of Cyprus, between a Cyprus port and a foreign port or an off-shore facility, or between foreign ports, or off-shore facilities and includes its ancillary activities.

In brief a "**Qualifying Ship**" is a seagoing vessel.

The following ships are excluded from this definition:-

- fishing and fish factory vessels;
- vessels used primarily for sport or recreation;
- vessels constructed exclusively for inland waterway navigation;
- harbour, estuary and river ferries and tug boats;
- fixed offshore installations which are not used for maritime transport;
- non self-propelled floating cranes;
- non-ocean going tug boats;
- stationary vessels employed for hotel and/or catering operations (floating hotels or restaurants); and
- vessels employed mainly as gambling facilities and/or casinos ( floating or cruising casinos).

### 3. PERIOD OF COMMITMENT

Although there is an obligation for Tonnage Tax Companies to commit to the Tonnage Tax system for a pe-

riod of 10 years, the Law does have a number of “get-out” provisions reflecting commercial realities i.e. when a vessel is sold, or a charter or management agreement is terminated.

## 4. SHIPOWNERS

### 4.1 Cyprus Flag

Owners of a Cyprus flag ship or a Bareboat Charterer of a ship registered parallel-in under the Cyprus flag (now known as a “**Qualifying Owner**”) continue to be eligible for Tonnage Tax, the said Tonnage Tax calculated on the net tonnage of the ship, subject to the ship in question being a qualifying ship engaged in qualifying shipping activity.

### 4.2 Foreign Flag

The following are also Qualifying Owners:-

- a **tax resident owner of a Community ship** which ship is: (a) a qualifying ship, and (b) engaged in a qualifying shipping activity; and
- a **tax resident owner of a fleet of ships comprising Community and non-Community ships** which said ships are: (a) qualifying ships, and (b) engaged in a qualifying shipping activity, and meet certain other criteria, including the “**Community flag link**” requirement, which as a general rule requires 60% of the fleet in terms of net tonnage to be Community ships. This requirement has a number of exceptions to it inter alia allowing a fleet with less than the said 60% share, if the Community flag share is increased or maintained within a period of 3 years from opting to be taxed under the Tonnage Tax and if not increased or maintained, excluding therefrom only those additionally acquired non-EU ships.

### 4.3 All or nothing rule

Qualifying Owners when opting to enter the tonnage tax system must include in the tonnage tax *all* qualifying ships. A Cyprus tax resident group of companies must enter all qualifying companies of the group into the tonnage tax system as soon as one company of the Group has opted to enter the tonnage tax system.

### 4.4 Exemption from Income Tax

For a Qualifying Owner operating a Qualifying Ship in Qualifying Shipping Activity (hereinafter the “**Ship**”) **no**

**tax is charged, levied or collected** on the following:-

- upon the **income** derived from the **operation of the Ship**; or
- upon the **dividend** paid to the shareholders or the members of the said owner, out of profits made from the operation of the Ship or made from the sale of the Ship and/or any share, right and/or interest therein, and/or upon the dividend paid to the shareholders and/or the members of the said owner, out of its share in profits made from a relevant qualifying shipping activity, and/or made from the sale of any Ship or share, right or interest therein; or
- upon the **dividend** paid to the shareholder or member of any other corporation recipient of such dividend, and **which originates directly or indirectly** out of profits made by a qualifying owner from the operation of a Ship, or made from the sale of any Ship or share, right and/or interest therein; or
- other than interest on moneys kept for investment, upon any **interest earned on working capital** and/or revenue earned by a Qualifying Owner from a relevant qualifying shipping activity on bank accounts, if such working capital or revenue is used to pay expenses for the financing and/or the operation and/or the maintenance of the ship; or
- upon any **income, dividend and/or profit made by a Qualifying Owner from the sale of any Ship**, and/or any share, right and/or interest therein, **and/or** made from the **sale of any shares in a Qualifying Owner** entity that is the owner of a Ship.

### 4.5 Miscellaneous

Most of the other requirements imposed by the Law (i.e. complying with relevant international standards and Community law requirements, in particular those relating to maritime security, safety, training and certification of seafarers, environmental performance and on-board working conditions) already form international standards and law as applied and adopted by the shipping industry.

## 5. SHIPMANAGERS

Shipmanagers providing ship management services

(crew management services and /or to technical management services) have the right to opt to be taxed with Tonnage Tax, and in cases where all the requirements are fulfilled, will be charged an annual Tonnage Tax calculated on the basis of the net tonnage of the ships they manage. “Commercial management services” are excluded from Tonnage Tax.

## 5.1 Conditions

A ship manager shall be a qualifying ship manager and shall be subject to an annual Tonnage Tax provided that the following conditions are satisfied:-

- the ship manager has opted to be taxed under the tonnage tax system. A ship manager must remain in the tonnage tax system for at least **ten** years.
- the ship manager is tax resident in Cyprus.
- the ship manager provides ship management services (to a qualifying ship or ships of any nationality (flag).
- the ship manager must have a fully fledged office in Cyprus and employ a sufficient in number and qualifications personnel.
- Managed from the EU (two thirds ‘2/3’ rule): Qualifying ships must be entirely managed from the territory of the EU, and the Ship Manager may benefit from the tonnage tax system only in respect of such ships. “**Qualifying ships entirely managed**” means qualifying ships under crew and/or technical management services.

This requirement is deemed as fulfilled, if at least two thirds (2/3) of the total tonnage of the qualifying ships managed in a given fiscal year are managed out of the EU.

Non-compliance of a ship manager with the two thirds (2/3) rule does not however affect the eligibility of the qualifying ship manager for the tonnage tax system.

- Standards: Qualifying ship managers providing crew management services and/or technical management services, as the case may be, are eligible for the tonnage tax system if all the ships and crews they manage comply with relevant international standards and Community law requirements are fulfilled, and in particular those relating to maritime security, safety, training and certification of seafarers, environ-

mental performance and on-board working conditions.

- At the time of opting to be taxed under the tonnage tax system at least sixty per cent (60%) of the fleet managed by the ship manager in terms of net tonnage should be Community ships. All tonnage then automatically qualifies. This is the general rule. There are exceptions to the 60% rule inter alia allowing a fleet with less than the said 60% share, if the Community flag share is increased or maintained within a period of 3 years from opting to be taxed under the Tonnage Tax and if not increased or maintained, excluding therefrom any additional non-EU ships managed by the said ship manager after the date of opting to be taxed under the Tonnage Tax.

## 5.2 Exemption from Income Tax

For a Qualifying Ship Manager rendering crew and/ or technical ship management services to any qualifying ship (hereinafter “**Ship Management Services**”) **no tax is charged, levied or collected** on the following:-

- upon the **income** of a qualifying ship manager, derived from Ship Management Services; or
- upon the **dividend** paid to the shareholders or the members of a qualifying ship manager, out of profits made from Ship Management Services, or upon the dividend paid to the shareholders or the members of a qualifying ship manager, out of its share in profits made from the rendering of the relevant ship management services; or
- upon the **dividend** paid to the shareholder or member of any other corporation recipient of such dividend, and which originates **directly or indirectly** out of profits made by a qualifying ship manager from Ship Management Services; or
- other than interest on moneys kept for investment, upon any **interest earned on working capital** and/or revenue earned by a qualifying ship manager from the provision of crew management services and/ or technical management services to any qualifying ship on bank accounts, if such working capital and/or revenue is used to pay expenses relevant to the management of those ships.

## 6. CHARTERERS

### 6.1 Qualifying Charterers

Charterers (bareboat, demise, time or voyage) of ships, have the right to opt to be taxed in respect of any particular fiscal year with Tonnage Tax calculated on the basis of the *net* tonnage of the ships they charter. A Qualifying Charterer must *inter alia* be tax resident and the chartered ship a qualifying ship engaged in a qualifying shipping activity. Again there are 3 categories: Charterers of Cyprus flag, Community flag, and of a fleet comprising Community and non - Community ships (similar Community flag link requirements apply as per shipowning).

### 6.2 Minimum charter to ownership ratio

The total net tonnage of ships chartered-in and included in the tonnage tax system may *not exceed* for more than three consecutive tax periods, 75% of the total net tonnage of all ships chartered- in or operated by a qualifying charterer and included in the tonnage tax system.

The total net tonnage of ships chartered-in and included in the tonnage tax system may *not exceed* for more than three consecutive tax periods, 90% of the total net tonnage of all ships chartered-in or operated by a qualifying charterer and included in the tonnage tax system, provided that every chartered-in ship is either registered in a register of a Member State, or its crew management and its technical management are carried out from the territory of a Member State.

### 6.3 Exemption from Income Tax

For a Qualifying Charterer operating a Qualifying Ship in Qualifying Shipping Activity (hereinafter “**Chartered Ship**”) **no tax is charged, levied or collected** on the following:-

- upon the **income** derived from the Chartered Ship; or
- upon the **dividend** paid to the shareholders or the members of a qualifying charterer, out of profits made from a relevant qualifying shipping activity, and/or upon the dividend paid to the shareholders or the members of a qualifying charterer, out of its share in profits made from a relevant qualifying shipping activity; or
- upon the **dividend** paid to the shareholder or member of any other corporation recipient of such dividend, and which originates **directly or indirectly** out of profits made by a qualifying charterer from a Chartered Ship; or
- other than interest on moneys kept for investment, upon any **interest earned on working capital** and/or revenue earned by a qualifying charterer from a relevant qualifying shipping activity on bank accounts, if such working capital and/or revenue is used to pay expenses arising out of the Charterparty.

**For further information, please contact:**

**Michael McBride**

Partner

[michael@demetriades.com](mailto:michael@demetriades.com)

Disclaimer: This document is for general guidance only and does not constitute definitive advice. We do not accept any liability to anyone who relies on the contents of this document.

© Chrysses Demetriades & Co LLC 2010

© Chrysses Demetriades & Co LLC 2010. All rights reserved. Extracts may be reproduced with our prior consent, provided that the source is acknowledged.