



Tax Circular 27 December 2010

AMENDMENTS TO THE CYPRUS TAX LEGISLATION

The Cyprus Parliament voted amendments to certain laws on the 14th December 2010 with the aim to introduce new VAT rules, simplify certain regulations of the Cyprus tax legislation and strengthen the anti avoidance and anti evasion provisions contained therein.

1. Amendments to The Income Tax Law

With effect from 1 January 2011 the following apply:

(a) Expenses disallowed

Any expenditure which is not supported by invoices and relevant receipts or other supporting documents as required by relevant Regulations will not be treated as deductible expenses for income tax purposes.

(b) Loans to directors or shareholders

When a company that is controlled by no more than five persons, grants a loan or any other financial facility to any of its directors or shareholders who are individuals (or to their relatives up to a second degree), notional interest at the rate of 9% per annum is imposed. When the loan is granted to corporate shareholders, the provisions of the law apply under which a market rate of interest should be charged on financing between related parties.

Furthermore, the following amendment will take effect 6 months after the publication of the relevant amending law in the official Gazette of the Republic:

- Tax withheld on payments to non Cypriot residents

In case of the following categories of income derived by non-tax residents of Cyprus from sources within Cyprus, the payer of the income is obliged to withhold tax at source and pay such tax to the Inland Revenue department by the end of the following month. In the event that the withholding tax is not paid within the deadline, an additional tax of 5% will be payable on the amount of the tax withheld in addition to the interest that is imposed and which is currently at the rate of 5,35% per annum:

- (1) copyrights for use within Cyprus
- (2) rights for cinematographic films
- (3) income of an individual for professional services, artists and athletes fees

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2. Amendments to The Special Contribution for Defence Law

The following amendments will take effect 6 months after the publication of the relevant amending law in the official Gazette of the Republic:

(a) Deemed dividend distribution

Whenever a company disposes an asset to its shareholder who is an individual or to his or her spouse or to his or her relative of up to second degree relationship, for a consideration which is below the market value of the asset, the balance of the fair market value less the amount of the consideration shall be deemed as dividend distributed to the individual shareholder and taxed accordingly. This provision will not apply in the case where the asset was acquired by the company through a donation from the shareholder, the spouse or a relative of up to second degree relationship.

(b) Definition of “taxation”

For the purpose of determining the accounting profit for the purposes of applying the provisions of deemed dividend distribution, the following taxes suffered by the company for a specific tax year will be taken into account:

- (1) income tax
- (2) special defence contribution
- (3) capital gains tax and
- (4) any amount of foreign tax that has not been credited against income tax and/or special defence contribution for the relevant year

(c) Calculation of deemed dividend distribution

It has been clarified that for the purposes of calculating the deemed dividend distribution, the following will be taken into consideration:

- (1) the actual dividend distributed during the two preceding years and
- (2) any actual dividend distributed during the tax year to which the profits relate

(d) Voluntary dissolution or liquidation

Companies that are under voluntary dissolution or liquidation are obliged to submit within one month from the date of the approval of the resolution, a deemed dividend declaration and pay any special defence contribution in relation to the profits of the specific tax year and the two preceding years. The deemed dividend distribution of such profits may not exceed the value of the net assets distributed to the shareholders.

If the assets of the company are not sufficient for the repayment of its creditors and no amount is available to be distributed to the shareholders, the accounting profits arising during a voluntary dissolution or liquidation will not be subject to a deemed dividend distribution.



If the assets of the company which are distributed to the shareholders during a voluntary dissolution or liquidation, have a market value exceeding the cost of their acquisition by the company, the deemed distribution provisions will apply, i.e. it will be deemed that the difference between the fair market value of such assets and their cost of acquisition shall be deemed as dividend distributed to the shareholders.

(e) Reduction of capital

In the case of a company's capital reduction, any amounts paid to the shareholder in excess of the amount of the share capital that was actually paid by the shareholder will be treated as distributed dividend.

(f) Withholding special defence contribution on rents

Companies, partnerships, the Government or any Municipal Authority that pay rents are required to withhold special defence contribution equal to 3% of the 75% of the rent and submit such tax to the Inland Revenue department together with a statement containing full particulars of the Lease as a result of which the deduction has been made and how the special defence contribution has been calculated. The amount of special defence contribution is payable to the Inland Revenue department on the 30th June and 31st December of each year.

3. Amendments to The Assessments and Collection of Taxes Law

The following amendments will take effect 6 months after the publication of the relevant amending law in the official Gazette of the Republic:

(a) Registration with the Inland Revenue department

Companies which are incorporated or registered or become tax resident in Cyprus have an obligation to register with the Inland Revenue department and obtain a tax identification code (T.I.C.) within 60 days from their incorporation or registration or from the date that they become tax residents in Cyprus.

Companies which are already registered with the Inland Revenue department have an obligation to inform the Commissioner of any changes that may affect the records of the Inland Revenue within 60 days from the date that the relevant change occurred.

Existing companies which are not yet registered with the Inland Revenue department may register by 30th June 2011 without suffering any penalties.

(b) Banking secrecy

The Commissioner has the right, in relation to a tax examination of any person, to request from a bank to provide the Commissioner with any information that is in the bank's possession for a period of 7 years preceding the date of the request. The Commissioner must have the relevant approval from the Attorney General of the Republic.



The Commissioner is required under the law to inform the bank and the office of the Attorney General about the following:

- (1) the identification of the person under investigation
- (2) the nature and the form of information requested
- (3) the reasons the Commissioner believes that the bank is in possession of the information
- (4) the period to which the information relates
- (5) the Commissioner's declaration that he has exhausted all available means for collecting the information
- (6) the justified tax reasons for which the information is requested.

(c) Electronic submission of tax returns

The tax returns of companies or other persons that prepare audited accounts may be submitted electronically. In such a case, the deadline for submission is extended by three months.

(d) Tax assessments issued by the Commissioner

In the case that a person (individual or company) omits to submit a tax return within the time limit specified in the provisions of the Assessment and Collection of Taxes Law or a person omits to keep proper books and records or to provide the Commissioner with information that will facilitate the verification of the correctness of the submitted documents, the Commissioner may decide to issue an assessment that will be based on information available to the Commissioner as a result of the findings of the review or an examination occurred in a prior year.

(e) Objections

Any objections submitted against assessments raised by the Commissioner should state the specific reasons for the objection and include supporting documentation where appropriate and a computation of the amount of tax as per the taxpayer's position.

(f) Exchange of information between the Inland Revenue department and other governmental departments

The Commissioner has the right to request information for the purpose of imposing taxation, from any other governmental departments, local authorities and semi-governmental organizations, excluding the Central Bank of Cyprus and the Department of Supervision and Development of Cooperative Companies.

(g) Field audits

The Commissioner has the right during the normal working hours of a business to enter into any space used by the business and inspect any goods and documents that are used for business purposes. Private residences are excluded from these provisions.



(h) Updating of accounting records

Companies which have an obligation to keep books and records for every tax year are obliged to update those books and records within 4 months from the date of the transactions. Companies are also required to issue invoices within 30 days from the date of the transaction unless a written approval of the Commissioner has been obtained for the purpose of issuing the invoices at a later stage. Companies which maintain stocks should carry out a stock-take during the year end and the results of the stock-take should be made available to the Commissioner upon request.

(i) Payment of disputed tax in the case of a court appeal

In the case of petition at the Supreme Court against an assessment raised by the Commissioner, the payment of the disputed amount of tax only (and not of the total amount of tax) will be postponed until the issuance of the decision of the Court.

4. Penalties

The new amendments stipulate that the following additional penalties are imposed and are applicable to the Income Tax, Assessment and Collection Taxes, Special Contribution for Defence, Capital Gains Tax and Immovable Property Tax Laws:

- (1) any person who refuses, fails or neglects to submit any notification or tax return or provide any information requested or does not perform any of his duties as those are explicitly prescribed by law with the deadline expressly prescribed by law is liable to a penalty of €100.
- (2) any person who refuses, fails or neglects to submit any notification or tax return or provide any information requested or does not perform any of his duties as those are explicitly prescribed by law and the Commissioner has duly served a written notice on such person requesting the compliance with a deadline expressly mentioned therein (regardless of whether the law specifies a deadline or not) is liable to a penalty of €200. The deadline set by the Director should not, however, be less than a period of 60 days.
- (3) any person who refuses, fails or neglects to submit any notification or tax return or provide any information requested or does not perform any of his duties as those are explicitly prescribed for by law for which no deadline is prescribed by the relevant tax law, and these notices, returns, information or duties relate to a third party and the Commissioner has duly served a written notice on such person requesting the compliance with a deadline expressly mentioned therein, is liable to a penalty of €200. The deadline set by the Director should not, however, be less than a period of 60 days.
- (4) following the 2010 amendments, in the event of non-payment within the deadline set by legislation or in a written notification by the Commissioner, an additional penalty of 5% will be payable on the amount of the tax due.

The above amendments relating to penalties will take effect 6 months after the publication of the relevant amending law in the official Gazette of the Republic:



5. Changes to the VAT legislation

The following amendments will take effect as from 10 January 2011:

The VAT rate of 5% apply on foodstuffs including beverages which are intended for human consumption (with the exception of alcoholic beverages, beer, wine and soft drinks) and on pharmaceutical products and vaccines that are used for health care, prevention of illnesses and as treatment for medical or veterinary purposes.

Every taxable person has an obligation to proceed with a stock-take of the goods for which the VAT rate changes at the end of the business day prior to the change of the VAT rate.

The term restaurant and catering services will include the supplies of prepared and unprepared foodstuffs and beverages that are accompanied by sufficient support services that enable the immediate consumption of the foodstuffs and beverages supplied and will be subject to the VAT rate of 8% (for example the supply of alcoholic beverages, beer, wine and soft drinks). The supply of foodstuffs and beverages to which the provision of support services is not the most important component element of the overall supply will be subject to the VAT rate of 5% (for example foodstuffs and beverages that have been heated in order to render them suitable for consumption at a temperature higher than that of the environment or that their temperature is higher than that of the environment).