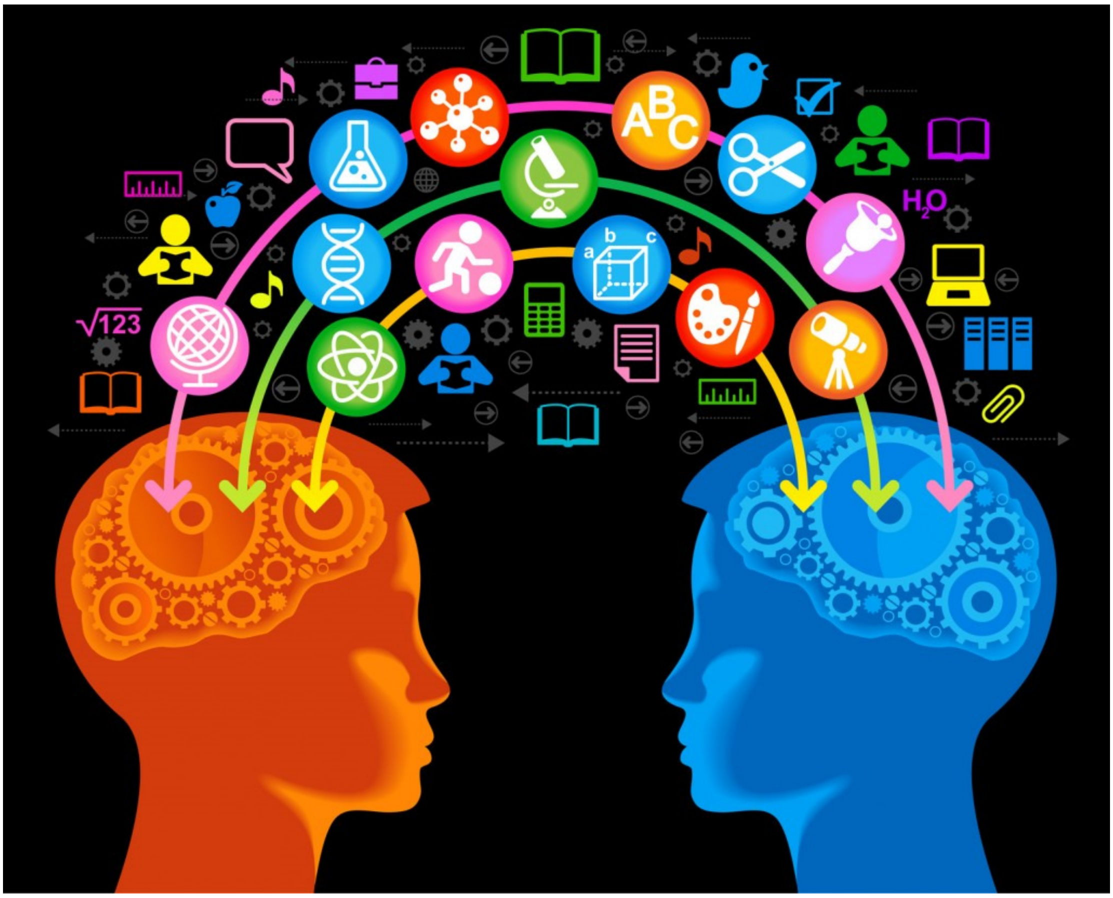
Cyprus Intellectual Property Tax Regime

February 2016



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Background

In recent years, the Republic of Cyprus has introduced a number of schemes that can lead to substantial tax incentives related to licence/royalty payments, deriving from the exploitation of intellectual property rights.

These rights have been widely known as intellectual property rights box (IP BOX).

The Cyprus IP Box features a five year amortisation period. The cost of acquiring or developing of an Intellectual Property Right acquired by a Cyprus Company can be capitalised on a straight line basis over five years, giving an annual write-down allowance of 20%.

In addition, four-fifths (4/5) deduction of revenue from exploitation of IP rights and four-fifths (4/5) of the profit earned from the use of intangible assets (including any compensation for improper use) is deducted for tax purposes.

In effect, only 20% of Intellectual Property income, after deduction of the costs of earning the income (including amortisation), is taken into account.

Tax exemption of dividends and other benefits resulting from IP activities

Any dividend income generated out of royalty income earned by a Cyprus company and paid to its non-resident shareholders is **fully exempt** from Cyprus tax of any description.

Four-fifths (4/5) deduction of profits on disposal of IP rights or other relevant intangible assets.

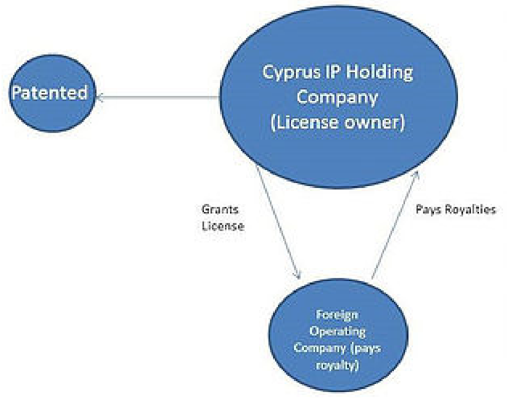
While this is a more generous exemption than is available under any competing regime, in most cases a more beneficial result from the taxpayer's viewpoint can be achieved by holding the assets concerned in a separate company and disposing of the shares in that company, rather than the assets themselves.

This route would result in full exemption of the gain, as well as stamp duty savings, since gains on disposals of qualifying securities are exempt from all forms of taxation in Cyprus except to the extent that they derive from the disposal of immovable property located in Cyprus.

VAT

The acquisition of intellectual property rights from anywhere in the world by a Cyprus company is treated as a service rendered to the company which will create an obligation for it to register for VAT and to account for VAT on services received in accordance with the reverse charge mechanism. If the company charges royalty fees to taxable persons within the European Union area it will also have to register for the EU VAT Information Exchange System (VIES).

The Cyprus IP box provides attractive opportunities for structuring the exploitation of IP assets through Cyprus and in particular through the use of Cyprus-resident IP owners, especially in conjunction with Cyprus's extensive network of double tax treaties, under which withholding tax on royalty income is either eliminated altogether or substantially reduced.



BEPS REFORMS ACTION 5 - Plan by the G20 Summit

There is an important opportunity to promote the current Cyprus tax provisions for exploitation of Intellectual Property ('IP Box') before the benefits of the IP Box become much more restrictive. In a nutshell, it is expected that IP benefitting from the Cyprus IP Box **prior to 1 July 2016** should continue to get the benefits until 30 June 2021 (i.e. for a further 5 years). Whereas, due to international / EU tax developments, it is expected that there will be much less scope to benefit as from 1 July 2016 if the IP is not already in the Cyprus IP Box. Given that 1 July 2016 is very close, it is important to act now.

Under the new suggested rules by BEPS, the IP regime focuses on establishing a nexus between expenditures, these IP assets, and income. In accordance to the new regulations the range of qualifying IP is expected to be narrowed as from 1 July 2016.

In addition, the new regulation limits the amount of income that can be claimed under the IP regime.

Under the BEPS - Action 5 regulations the IP income is limited to the nexus ratio which is calculated using the formula:

(a+ b) / (a + b + c +d) where:

a represents R&D expenditures incurred by the taxpayer itself (can be uplifted by 30% from actual numbers),

b represents expenditures for unrelated-party outsourcing,
c represents acquisition costs, and
d represents expenditures for related-party outsourcing.

Qualifying expenditures must have been incurred by the qualifying taxpayer, and they must be directly connected to the IP asset.
Having said the above we have to note that no guidance has yet been published in relation to the implementation of the BEPS – Action 5, and the implementation also depends on the legal reforms that Cyprus will implement to its current IP regime.

Why is the Cyprus IP Box so beneficial?

- Effective rate of tax is maximum 2,5%.

- Very wide range of qualifying IP types.

- IP does not need to be developed in Cyprus, R&D can take place anywhere in the world.

- Also applies to acquired IP and not just self-developed IP.
- The registration of the IP in Cyprus is not required. The IP can be registered anywhere in the world, however, the registered holder should be a Cyprus Company.
- Includes not only royalty incomes but also gains on disposal.
- No cap on the amount of income/gains which may benefit.

May be combined with the newly introduced notional interest deduction (**NID**).

	Approximate Effective Tax Rate
Cyprus	**2.5%**
Netherlands	**5%**
Luxemburg	**5.9%**
UK	**10%**
Ireland	**10%**

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