



TAX

## Taxation of Investment Funds - New Tax Law Amendments

October 23<sup>rd</sup> 2009

### **Cyprus Tax Laws have been amended to provide further tax incentives for the set up and operation of Collective Investment Schemes.**

The Cyprus taxation laws have been amended mostly in relation to the tax treatment of open-ended and close-ended collective investment schemes.

The enacted amendments facilitate the setting up and operation of investment schemes in Cyprus as well as simplify the tax regime in respect of taxation of interest and of dividends received from abroad.

#### **Disposal of Securities**

The Cyprus Income Tax Law N.118(I)/2002 has been amended to make clear that proceeds derived on the disposal of a unit, shall be exempt under s.8(22) of the Cyprus Income Tax Law, which exempts profits derived on the disposal of securities from Corporate Income Tax in Cyprus.

Therefore, profits derived on the disposal of a unit in a collective investment scheme will be exempt from tax in Cyprus.

#### **Redemption of Securities**

The redemption of a unitholding in a collective investment scheme does not constitute a reduction of capital under the Deemed Distribution provisions of the Special Contribution for Defence Law (SCD) and, therefore, there will not be any tax implications on the distribution arising from the redemption.

#### **Interest Income**

The **Cyprus Income Tax Law** has been amended abolishing the existing rules on taxation of interest income and introducing a uniform treatment in relation to the taxation of interest income derived by natural and legal persons. Interest income derived by a person will be exempt from corporate income tax unless such interest is closely connected or related to the taxpayer's trading activities, in which case such interest income will be taxed under Income tax.

*Note: In the case of companies, such interest income will be taxed under Corporate Income Tax at the rate of 10%. In the rare occasions where an individual may derive "active" interest income; such income will be taxed at the escalated personal tax rates.*

The amendment goes on to make clear that interest income derived by a collective investment scheme is considered to be "active" interest income and taxed only at 10% corporate income tax.

The **Special Contribution for Defence Law** has been amended accordingly to make clear that interest derived by a collective investment scheme is not considered to be interest for SCD purposes and therefore is not subject to Defence tax.

#### **Dividend Income**

The **Special Contribution for Defence Law** has been amended in order to abolish the minimum participation requirement of 1% when it relates to dividends received from abroad by a Cyprus tax resident Company.

### **AUDIT ■ TAX ■ ADVISORY**

## Taxation of Investment Funds - New Tax Law Amendments

The above amendment will also apply to collective investment schemes that have stakeholdings in various investments that may be less than 1%.

*Note: In order to obtain full exemption, dividends received from abroad should qualify for either one of the following conditions:*

- *The company paying the dividend must not engage directly or indirectly more than 50% in activities which lead to passive income (non-trading income), or*
- *The foreign tax burden on the income of the company paying the dividend is not substantially lower than the tax burden in Cyprus. (An effective tax rate of at least five percent (5%) in the country paying the dividend satisfies this condition).*

### Deemed Dividend Distribution

Collective Investment Schemes will be imposed a 3% taxation under the Special Contribution for the Defence Law [instead of 15%] in the event where the scheme fails to distribute at least 70% of its accounting profits within a period of two years from the tax year to which the profits relate, to the extent that the collective scheme has Cyprus tax resident unitholders.

The above taxation on Deemed Dividend Distribution is not applicable in the event where the unitholders of the Collective Investment Scheme are not tax residents in Cyprus.

### Liquidation of Collective Schemes

On liquidation of a Collective Investment Scheme, the proceeds will be subject to tax under the Special Contribution for Defence Law at the rate of 3% but exempt in the case where the unitholders are not tax residents of Cyprus.

### Enforcement Date

The amendments will apply as of the tax year 2009.

### For further information please contact:

#### Nicosia

**George Markides**

Tel: + 357 22209297

E-mail: [gmarkides@kpmg.com](mailto:gmarkides@kpmg.com)

**Costas Markides**

Tel: + 357 22209246

E-mail: [cmarkides@kpmg.com](mailto:cmarkides@kpmg.com)

#### Limassol

**Sylvia Loizides**

Tel: + 357 25829000

E-mail: [sloizides@kpmg.com](mailto:sloizides@kpmg.com)

**George Nicolaou**

Tel: + 357 25829000

E-mail: [gnicolaou@kpmg.com](mailto:gnicolaou@kpmg.com)

#### Larnaca

**Michael Halios**

Tel: + 357 24200000

E-mail: [mhalios@kpmg.com](mailto:mhalios@kpmg.com)

#### Paphos

**Kyriakos Hadjipaschalis**

Tel: + 35726943050

E-mail: [khadiipaschalis@kpmg.com](mailto:khadiipaschalis@kpmg.com)

#### Paralimni

**Sofoclis Sofocleous**

Tel: + 357 23820080

E-mail: [ssofocleous@kpmg.com](mailto:ssofocleous@kpmg.com)