Special contribution for defence - 2013

Cyprus tax residents are liable to Special Defence Contribution (SDC) as follows:

<table>
<thead>
<tr>
<th></th>
<th>Individuals %</th>
<th>Companies %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest income from Cyprus Government Bonds and Loan Stocks</td>
<td>3</td>
<td>30*</td>
</tr>
<tr>
<td>Other interest income</td>
<td>30*</td>
<td>30*</td>
</tr>
<tr>
<td>Dividends from Cyprus resident company</td>
<td>20</td>
<td>-</td>
</tr>
<tr>
<td>Dividends from non-resident company</td>
<td>20</td>
<td>-</td>
</tr>
<tr>
<td>75% of Rental income</td>
<td>3</td>
<td>3</td>
</tr>
</tbody>
</table>

*: 15% prior to 29 April 2013

Dividends

Dividends paid by a Cyprus tax resident company to a Cyprus tax resident individual are paid net of 20% withholding SDC.

Dividends paid by a Cyprus tax resident company to companies or to individuals who are not Cyprus tax residents are paid gross without any deductions for SDC.

Dividends paid a Cyprus tax resident company to another Cyprus tax resident company, are not subject to SDC unless the dividends are paid indirectly (i.e. from an intermediate holding to its holding) after 4 years from the end of the year in which the underlying profits were earned.

Dividends received by companies from non-Cyprus tax resident companies are not subject to SDC. This exemption however does not apply if:

- The company paying the dividend engages in more than 50% of its activities in producing investment income
  
  And
- The foreign tax burden on the company paying the dividend is substantially lower than that in Cyprus. Substantially lower meaning less than 50% of the applicable corporation tax rates in Cyprus (currently 12.5%).
Deemed distribution

Resident companies will be deemed to have distributed to their Cyprus tax resident shareholders (individuals and companies) 70% of their accounting profits after two years from the end of the year in which the profits were generated and must account for 20% SDC thereon.

Accounting profit is the profit after tax, calculated in accordance with acceptable accounting standards and excludes any revaluations of movable or immovable property.

In addition to corporation tax the following taxes are taken into account when calculating accounting profit:

- SDC
- Capital Gains Tax
- Any foreign tax that has not been credited against Cyprus tax

SDC on deemed distributions is paid by the Company, on behalf of its tax resident shareholders. If an actual dividend distribution takes place within the 2 year period then the deemed distribution is reduced by this and hence the SDC is adjusted accordingly. Similarly if a dividend distribution out of the accounting profits of a given year is made after the end of the 2 year period then the withholding SDC is reduced by the SDC paid on the deemed distribution (i.e. no withholding tax for distributions up to 70% of the accounting profits).

Deemed dividend distribution does not apply to non resident shareholders (direct or indirect). In the case when a non tax resident person receives dividends from a Cyprus tax resident company, resulting from profits which at any stage were subject to deemed distribution then the SDC attributable to this person is refundable.

In case of a Company disposes of an asset to an individual shareholder or to a shareholder’s relatives up to second degree (including their spouses) , then the difference between the market value of the underlying asset and any consideration received will be deemed as dividend contribution and SDC will apply. This will not apply in the case that the underlying asset was received by the Company by way of gift by the shareholder or by the shareholder’s relatives up to second degree (including their spouses).

Dissolution of Companies & capital reduction

Companies that decide to proceed with voluntary liquidation, must submit within one month from the date of the relevant resolution, a deemed dividend declaration and pay the SDC in relation to the profits of the current year and the 2 preceding years.

The aggregate undistributed profits of the five years prior to a Company’s dissolution, for which no deemed distribution SDC was applied, are considered as distributed on dissolution and are subject to SDC.

Any profits arising during the liquidation process will not be subject to deemed distribution, provided that such profits will be used entirely for the repayment of creditors and will not be any
balance available for distribution to shareholders. Moreover any SDC cannot exceed the net value of the assets distributable to shareholders.

In case of capital reduction, any amounts paid to individual (i.e. not legal persons) shareholders in excess of the amount paid as capital by the relevant shareholder, will be deemed as dividend and be subject to SDC.

The above provisions do not apply if the shareholders of the Company are not Cyprus tax residents.

**Interest**

Interest derived from the normal carrying on of a business, including interest closely connected with the normal carrying on of a business is not considered interest but profit.

Interest earned by individuals from Government bonds is subject to SDC at the rate of 3%.

Interest earned by provident funds, from sources within the Republic of Cyprus is subject to SDC at the rate of 3%.

Any other interest, whether earned from sources within or outside Cyprus, is subject to SDC at the rate of 30% (15% prior to 29 April 2013).

Bank interest from Cyprus banks is received net of 30% (15% prior to 29 April 2013) withholding tax.

Interest earned by individuals whose total income including interest does not exceed €12,000 is subject to SDC at the rate of 3%. The deduction at source however (if source in Cyprus) will be 30% (15% prior to 29 April 2013) and the individual may apply to the Inland Revenue for a refund of the extra 27% (12% prior to 29 April 2013).

**Rent**

In the cases were the tenant of a property in Cyprus is a legal person, rent is paid net of withholding SDC of 2,25%. The tenant has the obligation to pay the tax withheld on a monthly basis to the Inland Revenue. When the tenants are physical persons the obligation of payment of the 2,25% SDC lies with the landlord.

**Credit in respect of foreign tax**

Credit in respect of any foreign tax paid on any income subject to SDC will be given against the Cyprus tax irrespective of the existence of a double tax treaty.