

Answer-to-Question- 1

1) Mr Xing's tax residency position and changes to his personal and economic ties:

In order for an individual to become a Cyprus tax resident, he should be in Cyprus for a period of more than 183 days during a calendar year.

Mr Xing became a tax resident in Cyprus for 2016 as he was for seven months (i.e. more than 210 days). However we have no information whether Tigrat may consider him as a tax resident.

As per the article 4(2) of the double tax agreement with Tigrat, when an individual is considered as a dual resident, a tie-breaker test should help us to identify on which State he/she is a tax resident.

The following should be examined:

- He shall be deemed to be a resident only of the State in which he has a permanent home: Although he has a home in Cyprus, his wife is not yet sure whether she will stay in Cyprus or move back to Tigrat. It seems that he has permanent homes in both Cyprus and Tigrat.
- In case he has permanent homes in both States, he should be considered to be a tax resident in the State in which his personal and economic relations are closer: It seems that his personal and economic relations during 2016 had been on both Cyprus and Tigrat. He has a company in X Ltd in Cyprus. However he holds a company in Xing Aviation Co plc in Tigrat.
- In case he has personal and economic relations in both States, he should be deemed to be a resident in the State he has a habitual abode: It seems that he has a habitual abode in Cyprus as he came in Cyprus with his family in 2016.
- Even if he had a habitual abode in both States, he could be considered as a Cyprus tax resident as he became a national in Cyprus.

As a result he should be taxed in Cyprus on his worldwide income. Any tax paid abroad should be claimed against any tax payable in Cyprus.

However, he is not domiciled in Cyprus by origin. He is also not domiciled by choice as he had been for more than 20 years overseas, any passive income arising in Cyprus, could not be taxed at S.D.C.

2) Cyprus Income Tax and Capital Gains tax and Special Defence Contribution.

The following sources of income should be taxable under Mr Xing's hands:

Rental of a hotel to a tour operator - Income tax:

Mr Xing will be taxed on the 80% of the gross rental income in Cyprus which amount to 320.000 euros after the deduction of following:

- Capital allowances should be claimed on the cost of the building of 900.000 euros at 4% and on the renovation cost of 1.6million euros at 7% for the tax year 2016 and at 4% from 2017 onwards on the whole amount. According to the income tax law of Cyprus, capital allowances should be claimed at 7% instead of 4% on any hotels/industrial buildings for the period of 2012-2016. The capital allowances should be claimed on the cost of the building of 900.000 euros. As a result capital allowance of 63.000 euros should be claimed.

- Interest expense on the loan used for the acquisition of the building should also be claimed (if any loan was used).

The result will be taxed under the progressive income tax rates in Cyprus. It should be better if this hotel was under a company in order the gross rental income of 400.000 euros minus capital allowances and any other expenses incurred for the production of taxable income could be taxed at 12,5%. As he is a non-domiciled person, no Special Defence Contribution (S.D.C.) should be deducted at source.

Rental of a hotel to a tour operator - Special Defence Contribution:

No S.D.C. should be deducted at source on the dividend income arising from the rental of the hotel. Even in the case of a company, as the shareholder is a non-domiciled person, no S.D.C. should be deducted at source. A company is deemed to distribute the minimum of the 70% of its after tax accounting profits, at the end of the two year's period from the year those profits were earned, to its shareholders. S.D.C. at 17% is payable on such dividends. In case those shareholders

are non-Cyprus tax residents, or Cyprus tax residents but not domiciled, no S.D.C. should be deducted at source.

Investment in X Ltd:

As he could not earn any salary from X Ltd, no income tax arises on this investment. Dividends are also exempt from S.D.C. due to the non- domicile rule.

Salary earned from Xing Aviation plc:

His salary should be taxed under Cyprus income tax.. Any tax withheld abroad should be claimed against the respective Cyprus tax on the salary.

Interest arising from bonds in Xing Aviation Co plc:

Interest is exempt from Cyprus income tax purposes. Also no S.D.C. should be paid due to the non-domicile rule. However any withholding tax could not be claimed against Cyprus tax.

Dividends arising from Xing Aviation Co plc:

Dividends are exempt from Cyprus income tax purposes. Also no S.D.C. is payable on these dividends due to the non-domicile rule. However any withholding tax could not be claimed against Cyprus tax.

Capital gains tax arising from the sale of perperty in Cyprus:

Capital gains tax at 20% is payable on the sale of the houls in central Limassol.

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According to the Double tax agreement between Cyprus and Grevandia (article 5 paragraph 2), a construction or installation project constitutes a permanent establishment only if it lasts more than twelve months.

A permanent establishment as per the article 5 paragraph 1 is a fixed place of business through which the business of an enterprise is wholly or partly carried on.

1) Direct and indirect tax implications for ADC in Cyprus if only Project 1 is undertaken:

Project 1 does not constitute a permanent establishment in Cyprus as it lasts for less than twelve months in Cyprus. Any profits attributable to the project should be taxed in Grevandia.

As the project is in Cyprus, VAT registration should be made if the services provided exceed the threshold of 15.600 euros. However a voluntary registration for VAT could apply to claim any VAT on the expenses incurred.

VAT also should apply for the imports made in Cyprus.

2) Direct and indirect tax implications for ADC in Cyprus if only Project 2 is undertaken:

Project 2 does not constitute a permanent establishment in Cyprus as it lasts for less than twelve months in Cyprus. Any profits attributable to the project should be taxed in Grevandia.

VAT registrations should only be made if the services provided exceed the threshold of 15.600 euros. However a voluntary registration for VAT could apply to claim any VAT on the expenses incurred.

VAT also should apply for the imports made in Cyprus.

3) Direct and indirect tax implications for ADC in Cyprus if Project 3 is also undertaken in addition to Project 1 and/or Project 2:

Project 3 will by itself create a permanent establishment in Cyprus as it will last for more than twelve months. If it is taken in addition to another project, then it should also create a permanent establishment in Cyprus. As a result any profits attributable to the projects should be taxable in Cyprus.

VAT registrations should be made if the services provided exceed the compulsory threshold of 15.600 euros. Compulsory registration for VAT in Cyprus could be made if the services provided exceed that threshold for the period of the last twelve months or they are expected to exceed that threshold during the next 30 days.

4) The most tax efficient way of structuring ADC operation in Cyprus if only project 3 is undertaken

As Project 3 will last for two years, it should be better for the incorporation of a company instead of a permanent establishment(PE).

If a permanent establishment exists, the profits of the PE should be taxed in Cyprus at 12,5%. However such income will also be taxed in Grevandia at 13,5% (26% - 12,5%).

In case a company is incorporated, such profits will be subject to tax at 12,5% only.

As far as dividends, any dividends payable from a Cyprus company to an overseas company are not subject to withholding tax in Cyprus.

However such dividends will be taxed at 10% in Grevandia which will be less than in case of an existence of a permanent establishment in Cyprus.

As per the EU parent subsidiary directive no tax will be withheld in either State if a company has control of more than 10% in its subsidiary.

5) Social security obligations in relation to both its Grevandian and Cypriot employees:

ADC should pay the following social security contributions on the gross salaries of the local employees in Cyprus if these are below 65 years old:

- 7,8% social insurance;
- 3,7% other funds; and
- 2% social cohesion

ADC should also withhold social insurance of 7,8% of the employees' salaries.

6) Personal tax position of the Grevandian employees in each of the projects:

Under project 1, Grevandian employees should not be considered as a tax residents in Cyprus given that they were for less than 183 days in a calendar year in Cyprus. As a result they will be taxed on their worldwide income in Grevandia.

Under project 2, Grevandian employees should be considered as a tax residents in Cyprus only if they have been in Cyprus for more than 183 days in Cyprus during a calendar year. If they have been Cyprus tax residents, they will be taxed on their worldwide income in Cyprus. However the Double tax agreement must be taken into consideration to avoid dual residency.

Under project 3, Grevandian employees should be considered as a tax residents in Cyprus as they have been in Cyprus for more than 183 days in Cyprus during a calendar year.

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Answer-to-Question- 3

1) Tax residency position of Pear Corp and the direct tax implications of the company's setup and operations:

Under the Cyprus Income Tax Law, a company in order to be a registered in Cyprus, it could be managed and controlled in Cyprus. Although there is no exact definition of the management and control, the following should be implied:

- The majority of the board of directors should be Cyprus tax residents;
- The board meetings should be held in Cyprus;
- The general policy of the company should be formulated in Cyprus.

In the case of Pear Corp it seems that the following apply:

- The majority of the board of directors are non Cyprus tax residents as the Company's directors are local professional directors. Mr Andreou who is a key director is a Cyprus tax resident.
- The board meetings take place in the country of incorporation of the company which is not Cyprus. However no important decisions are taken.
- The general policy of the company is formulated by the main shareholders and directors of the company. Mr Andreou and Ms Murat formulate the business strategy of the company. However they do not participate in the board of directors. Mr Andreou is a Cyprus tax resident. As he holds the 60% of the company's shareholding, he may be considered as the person formulating the business strategy of the company.

As a result the company may be considered as a Cyprus tax resident and it will be taxed in Cyprus on its profits arising worldwide except in case of profits arising from permanent establishments.

The Cyprus branch which in such case is considered as a Cypriot company is subject to tax on the profit arising from Cyprus at 12,5%.

The Teshland branch which is considered as a permanent establishment is subject to tax on the profits arising from the permanent establishment. A permanent establishment is a fixed place of business through which the business of an enterprise is carried on.

Such profits will not be taxed in Cyprus according to the Cypriot Income Tax Law.

As per the provisions of the Cypriot Income tax law, any profits arising from a permanent establishment is exempt from Cyprus tax purposes.

The Umland branch is a loss-making permanent establishment.

According to the provisions of the Cypriot Income Tax Law any losses arising from a permanent establishment abroad will be allowed for tax purposes. However in case those permanent establishment incur profits in the following years, those profits will be subject to recapture rules and as a result the amount of profit equal to the amount of the loss previously allowed, will now be subject to income tax in Cyprus.

It should be noted that such losses should be apportioned as other costs to the other parts of the company as they are incurred for the production of taxable income in the other parts of the company.

Mr Andreou as a Cyprus tax resident, will pay 17% Special Defence Contribution on the

dividends received. The company will withhold S.D.C. from this dividend. No such obligation exists for Muran as she is not a Cyprus tax resident.

2) Business restructuring options available to Pear Cors:

Pear Corp should incorporate companies in all the countries it is operating. Such companies should be subsidiaries of Pear Corp. As a result the following will apply:

- Dividend payment will be deferred.

A company is deemed to distribute the minimum of 70% of its after tax accounting profits in a two year period after the year those profits were earned and pay Special Defence Contribution at 17% on such dividends. As the payment of the actual dividends from a company to a company are exempt from Special Defence Contribution in a two-year period, Special Defence Contribution is paid when those dividends are payable on the Cyprus individual tax resident and as a result this will become payable in a 4-year's period.

3) VAT Compliance obligations:

As the company provides services, then the transactions could be considered Business-to-business (B2B) transactions. As a result the place of supply of services is the place where the recipient is situated.

As a result the company should register in the countries where the recipient is situated if the services are provided within EU.

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BEPS project is known as the project initiated by the OECD in 2015. BEPS is called for the Base Erosion and Profit Shifting.

Multinational companies identified ways to shift their profits in low-tax jurisdictions or no-tax jurisdictions, resulting thus in paying much less tax than the tax it should actually be owed by them. Such no-tax jurisdictions or low-tax jurisdictions are where no substance is created and no economic activity occurs.

As a result governments were harmed as they earned less tax revenues, individual tax payers felt that they paid unfair share of tax and the Multinational companies (MNEs) lost their reputation as being involved in such situations.

BEPS project is comprised of fifteen action plans, Those Action Plans were discussed by the OECD Member States and they made recommendations.

Following the recommendations made in 2015, most of these plans should be implemented in the domestic tax legislations of the States.

Cyprus has taken the following measures in response to the BEPS project:

- Neutralise the effects of Hybrid Mismatch arrangements (BEPS Action Point 2):

According to the latest amendments of the Income Tax Law, where dividend income is received from a Cyprus resident company from an overseas company and where such dividends is treated as an allowable expense in the payer company's accounts, such dividends are subject to corporation tax in Cyprus at 12,5%. In this case no Special Defense Contribution applies on those dividends.

- Limit Base Erosion via interest deduction and other financial payments (BEPS Action Point 4):

No amended law was voted with regards to that Action Point. However the groups having companies which are Cyprus tax residents may be aware of this action point as the respective interest income that arises in Cyprus may be restricted by the Tax Authorities of teh company paying that interest.

- Creating substance (BEPS Action Point 5):

Cyprus has recently voted a law providing for new IP regime. Under the new IP regime,

intangible asset is considered an asset which is owned by a Cyprus tax resident and it is a result of research and development made. The new IP regime may provide a statutory deduction of 80% of its taxable profits in Cyprus.

- Avoiding Treaty Abuse (BEPS Action 6):

Cyprus has recently ratified the multilateral instrument. The countries ratifying the multilateral instrument will add to the double tax conventions the LOB (Limitation of Benefits) provision. Under this provision, the benefits of a treaty could be given only to the beneficial owner of the income.

- Transfer pricing should be aligned with value creation (BEPS ACTION 8-10):

Cyprus has recently published a circular requesting a transfer pricing study in case of embedded income arising from an intangible asset included in the new IP regime.

- Country-by-Country Reporting (BEPS Action 13)

Cyprus has published a decree through which any Cyprus tax resident company that belongs to a multinational group should declare its income, tax payable, employees and its profit before tax if its revenue exceed 750 million euros. Such a report should be submitted by either the parent company of a group or a surrogate parent company.

- Ratification of a multilateral instrument (BEPS Action 15):

Cyprus has recently ratified the multilateral instrument providing thus an update of its double tax conventions.

Cyprus is significantly behind other countries in relation to the below BEPS measures:

Transfer pricing (BEPS Action 8-10):

In relation to the transactions made between the associated enterprises, section 33 is included in the Income Tax Law. However it does not give much guidance for the tax treatment of the intercompany transactions.

Dispute resolution (BEPS Action 14):

No reference is made by the Cypriot Tax Law with regards to the dispute resolution in case of an adjustment is made to the taxable income of an associated enterprise in another Contracting State.

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Answer-to-Question- 5

Domicile is according to the Wills and Success Law. A Cypriot domiciled person is any individual who has his domicility in Cyprus due to either a domicile of origin or a domicile by choice.

A domicile person of origin is any individual who has his father born in Cyprus.

A domicile person by choice incurs if an individual elects to live in Cyprus.

An individual who stays for more than 183 days in Cyprus is considered as a Cyprus tax resident. As a result his worldwide income is taxable in Cyprus.

According to the Special Contribution for Defence Law such individual could not be liable for the payment of Special Defence Contribution in case he/she has not his/her domicility in Cyprus.

In case a person is domiciled of origin, then he could be liable for Special Defence Contribution on any passive income (rental income, interest income, dividend income)

In case a person is no domiciled by origin, he could be domiciled by choice. As a result we should examine whether he had stayed abroad:

- For a period of twenty years prior to that individual comes to Cyprus; or
- For a period of twenty years prior to 16th July 2015 which was the date that this law was voted.

In case any of the above conditions apply, such individual could be considered as a non-domiciled person and thus no Special Defence Contribution should be paid by him/her.

However in case that individual had been in Cyprus for a period of 17 years out of the last twenty

years, then he/she could be considered as a domiciled person and as a result Special Defence Contribution could be paid on either dividend, interest and rental income at the applicable rates.

A non-domiciled person should submit a form declaring that he/she is not a domiciled person for Cyprus and thus be exempted from the S.D.C. obligations.

The bank in which an account is held by that person and any companies on which a shareholding is held by that person should also be aware of this fact in order no S.D.C. to be deducted at source. The relevant form should be in place in order to support this.

The companies that rent any property from that individual should also be aware of this in order no any S.D.C. should be paid on the Tax Authorities by them on behalf of that individual.

An anti-avoidance provision also exists in the S.D.C. law which states that in case a property is transferred by a domicile person to a non-domicile person with the purpose to avoid any tax payable, then the Tax Authorities will disregard such transfer and may request the payment of S.D.C. from the domicile person.