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All About Nexus: Link your IP asset to Cyprus

Introduction

As of the 1st of July 2016, a new Intellectual Property (IP) tax regime is applicable in Cyprus. The Cyprus IP tax legislation is now fully OECD compliant and it was actually amended as per the recommendation of the Base Erosion and Profit Shifting (BEPS) action 5 on Harmful Tax Practices.

As will be demonstrated below, the Cyprus IP regime provides great incentives for IP companies to transfer their seat, offices and personnel in Cyprus. Since 80% of the profits qualifying for the regime are exempt from tax, with an applicable corporate tax rate of 12.5% this can result in an effective tax rate of as low as 2.5%. Furthermore, other incentives also exist rendering Cyprus an attractive jurisdiction for the establishment of fully-fledged offices for IP companies.

Nexus approach explained

The new Cyprus IP regime follows the nexus approach. But what this nexus approach really is? The word 'nexus' indicates a connection linking two or more things. When referring to IP assets the nexus approach requires a link between the income taking advantage of the relevant IP rules and the extent to which the taxpayer has actually performed the underlying research and development (R&D) that generated the IP asset. Therefore, a direct link between the qualifying income and own qualifying expenses is essential for the IP to qualify. The level of the qualifying profits is positively correlated to the extent that R&D activities are performed by the same entity. To put it in simple terms if someone wishes to benefit from the Cyprus IP regime, R&D should be largely undertaken by that same person in Cyprus.

Cyprus IP regime

Under the previous IP regime an overall 80% deduction on profits was granted. Under the new rules 80% of the overall income derived from the qualifying intangible asset is treated as a deductible expense.

Grandfathering rules are offered under the new IP provisions to those that benefited from the old "IP Box", allowing them to continue relying on the previous legislative provisions, provided that the IP generated taxable income or its development was completed as at the 30th of June 2016 and also provided that it was acquired/developed prior to the introduction of the new provisions.

Under the new regime, qualifying intangible asset is an asset which has been acquired, developed or exploited by a person within the course of carrying out their business which is the result of research and developments activities. Such assets specifically comprise of (a) patents, (b) computer software, and (c) other intellectual property which is legally protected and comprises of utility models, IP assets, which provide protection to plants and genetic material, orphan drug destinations and extensions of protection for patterns or non-obvious, useful and novel (which are certified as such by an appropriate authority) where the person utilizing such does not generate annual gross revenues in excess of Euro 7.5 million from all intangible assets (or Euro 50 million for groups).

Qualifying intangible assets specifically exclude trademarks, business names, brands image rights and other IP rights used for the marketing of products and services. Persons that may benefit from the Cyprus IP regime include Cyprus tax resident taxpayers, tax resident permanent establishments (PEs) of non-tax resident persons as well as foreign PEs that are subject to tax in Cyprus.

Moreover, the new regime introduced the nexus fraction for the purposes of determining the amount of qualifying profits used to determine the relevant tax deduction. For the calculation of the qualifying profits the overall income (being the gross income derived from qualifying intangible assets minus any direct costs), the qualifying expenditure, uplift expenditure and overall expenditure are taken into consideration. The nexus approach is additive in that the calculation requires that expenditure includes all expenses incurred by the taxpayer over the life of the IP asset.

To move or not to move?

As explained above the Cyprus IP regime gives considerable benefits to IP companies wishing to transfer their offices and personnel in Cyprus. Apart from such tax benefits, other advantages also exist rendering Cyprus an attractive jurisdiction for the establishment of fully-fledged offices.

A number of incentives are available for managers, higher officers and employees of a company wishing to re-locate on the island. Apart from obtaining the tax resident non-domiciled status (conferring exemptions from the Special Defence Contribution tax), expatriate relief is also available, whereby 50% of the gross emoluments are allowed to be deducted from taxable income for individuals that were not tax residents of Cyprus prior to the commencement of their employment in Cyprus. This deduction applies when income exceeds EUR 100,000 per annum and is available for a period of ten (10) years, commencing from the date of employment.

Furthermore, Cyprus is an EU member state since 2004, with all relevant EU regulations and legislation applicable, while its currency is the Euro. Recently it has been designated as one of the safest countries in the world to visit, travel and live. Also, English is widely spoken and it is considered to be the primary business language, while multilingual and highly skilled workforce is available as well. In addition, the availability of suitable office spaces for rent, the reasonable cost of living in comparison with other European countries, the high-level infrastructure and the quality of life offered, are additional factors that render Cyprus an appealing jurisdiction for the relocation of IP companies.

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