EVIDENTRUST

FINANCIAL SERVICES

Cyprus Taxation | Intellectual Property Regime

One of the most valuable and hard to develop assets of any corporation is the Intellectual Property ("IP"). Therefore, corporations should choose their IP's locations taking into account their business strategy, the level of protection and tax optimisation. An ideal location for registering and managing your IP is Cyprus as the geographical location, common law framework, and full EU membership in addition to the fact that Cyprus offers a highly educated workforce and a well-developed Financial Services Sector, puts itself forward as a prominent choice.

Following the amendments in the Cyprus Income Tax Law passed in October 2016, Cyprus now offers a tax efficient new IP Regime which is fully aligned with the OECD's Base Erosion and Profit Shifting ("BEPS") Action 5 report.

The New IP Regime

Under the new IP Regime, an intangible asset to qualify for the benefits of the regime, there needs to be a direct link between the qualifying income and the own qualifying expenses contributing to that income.

In brief, **80%** of the **qualifying profits** generated from **qualifying assets** will be deemed to be tax deductible expenses.

Qualifying Assets

Those assets which were acquired, developed or exploited by a person within the course of carrying out his business (with the exception of intellectual property related to marketing), which is the result of research and development (R&D) activities, and which includes intangible assets for which only economic ownership exists.

Examples of QA assets:
- patents, as defined in the Patent Law;
- computer software.

Qualifying Profits

QP are calculated based on the "nexus approach" which specifies the 80% tax exception on the eligible profits will depend on the level of R&D expenditure carried out by the taxpayer to develop the qualified asset. The qualified profits are calculated based on the following fraction:

$$OI \times \frac{QE + UE}{OE}$$

Definitions:
- OI : Overall Income derived from the QA;
- QE: Qualified Expenditure on the QA;
- UE: Uplift Expenditure on the QA; and
- OE: Overall Expenditure on the QA.

Overall Income (OI)

OI derived from qualifying assets is defined as the gross profit from the assets (i.e. gross income less any direct expenditure). Overall Income includes, but not limited to:

- Royalties or any other amounts relating for the exploitation of the qualifying assets;
- Any amount for the grant of a license for the exploitation of the qualifying assets;
- Any amounts relating to the insurance or compensation for the qualifying asset;
- Trading income from the disposal of the qualifying asset; and
- Embedded income on qualifying assets, which is derived from the sale of goods, the provision of services or use of any processes that are directly related to the qualifying assets.

Capital gains arising from the disposal of a qualifying asset under the new IP regime are not included in qualifying profits and are fully exempt from income tax.

Qualifying Taxpayers (QT)

QT that are eligible for the new IP regime include Cyprus resident persons, permanent establishments (PEs) of non-resident persons and foreign PE that are subject to tax in Cyprus.

Qualifying Expenditure (QE)

QE relating to a qualifying asset is the sum of all R&D expenditure incurred in any tax year wholly and exclusively for the development, enhancement or creation of a qualifying asset which is directly related to that asset.

QE includes, but is not limited to:
- Salaries and wages;
- Direct costs;
- General expenses associated with R&D activities;
- Commission expenditure associated with R&D activities; and
- R&D expenditure outsourced to unrelated parties.

QE does not include:
- The acquisition cost of a specific intangible asset;
- Interest paid or payable;
- Expenditure relating to the acquisition or construction of immovable property that has been paid or is payable directly or indirectly to a related person carrying out R&D, regardless of whether the amount relate to a cost sharing agreement;
- Costs that cannot be shown to be directly associated with a specific asset.

Uplift Expenditure (UE)

UE of a qualifying asset is the lower of:
i. 30% of the QE; and
ii. the total acquisition cost of the qualifying asset and any R&D costs outsourced to related parties.

Overall Expenditure (QE)

QE of a qualifying asset is the sum of:
i. qualifying expenditure; and
ii. the total acquisition cost of the qualifying asset and any R&D costs outsourced to related parties incurred in any tax year.

Contact us

Our team is available to answer any questions you may have and provide further details of our range of services. We are readily available to explore the best options for your organisation.

We look forward to helping you thrive in an efficient and effective professional environment.