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Amendments to the Intellectual Property Tax Law

On 14 October 2016, the House of Representatives enacted into law significant amending proposals to the tax laws on the exploitation of Intellectual Properties.
The amendments introduced in the Income Tax Law (ITL) provide for the gradual phase out of the current IP regime and the introduction of the new IP regime that is in line with the latest international developments on the taxation of IP income and OECD's action plan on fighting base erosion and profit shifting (BEPS). The ITL amendments are supported by regulations which provide detailed guidance in the calculations and application of the new IP regime.

A. Existing IP regime in Cyprus

The Cyprus IP Box regime was put in effect on 1st January 2012 and it applies to a wide range of IP rights falling within the meaning of the Patent Law, the Intellectual Property Rights Law and the Trademarks Law. The Cypriot IP Box regime includes intangible assets as:

- **Copyrights** taking the form of literary works, dramatic works, musical works, scientific works, artistic works, sound recordings, films, broadcasts, published editions, databases, publications, software programs, etc.
- **Patented inventions** etc.
- **Trademarks** and service marks, designs, models, etc.

Tax Incentives

- 80% of any income generated from IP owned by Cypriot resident companies

(net of any direct expenses) is exempt from income tax.

- 80% of profit generated from the disposal of IP by Cypriot resident companies

(net of any direct expenses) is exempt from income tax.

- Any expenditure of a capital nature for the acquisition and/or development of IP can be claimed as a deduction in the tax year in which it is incurred and the immediate four following years on a straight-line basis.

For an entity to secure the above benefits it should be the owner of the IP rights through official registration either in Cyprus or abroad, and the intangible asset should be used in the production of income.
In the case of a resulting loss, only 20% of the loss can be set off with the company's other taxable income of the current year or to be carried forward to subsequent years and set off with the company's future taxable profits.

B. Transitional arrangements for existing IP regime

There are transitional provisions for persons who have entered the existing IP Box regime, which enable them to continue claiming the benefit until 30 June 2021 with respect to intangible assets, which:

- were acquired before 2 January 2016, or
- were acquired directly or indirectly from a related person during the period from 2 January 2016 until 30 June 2016 and which assets at the time of their acquisitionwere benefiting under the IP Box regime or under a similar scheme for intangible assets in another state, or
- were acquired from an unrelated person or developed during the period from 2 January 2016 until 30 June 2016.

There are also transitional provisions until 31 December 2016 for intangible assets purchased from a related party which prior to their purchase were not under the same or a similar IP regime.

C. Provisions for the new IP regime

Under the new IP regime, 80% of the **qualifying** profits which are generated from the qualifying assets will not be taxable. In calculating the qualifying profits, the new regime adopts the 'Nexus' approach. According to this approach, the level of the qualifying profits is positively correlated to the extent the claimant performs R&D activities to develop the qualifying asset.

The taxpayer may choose to forego the whole or part of the deduction. Furthermore, where the calculation of qualifying profits results in a loss, only 20% of this loss can be set off with the company's other taxable income of the current year or to be carried forward to subsequent years and set off with the company's future taxable profits.

Qualifying intangible asset (QA) means an asset which was acquired, developed or exploited by a person in furtherance of his business, (excluding intellectual property associated with marketing) and which is the result of research and development activities and includes intangible assets for which only economic ownership exists.

These assets are:

- Patents as defined in the Patents Law.
- Software Computer programs
- Other IP assets that are non-obvious, useful, and novel, where the person which utilizes them in furtherance of a business does not generate annual gross revenues exceeding €7.500.000 (in case of a group of companies not exceeding Euro 50.000.000).

Business names (including brands), trademarks, rights to public presence, image rights and other intellectual property rights used to market products and services are not considered as qualifying intangible assets.
In contrast to the previous application of the law, the current application offers a tax benefit only on qualifying profits which are calculated using the nexus formula taking into consideration the value of the qualifying profits arising from qualifying assets, and the qualified expenditures.

Other amendments relating to intangible assets

- Any person who claims benefit under the above regime is obligated to maintain proper books of account and records of income and expenses for each intangible asset.
- The cost of acquiring intangible assets can be amortised over the period of the useful life of the asset in accordance with accepted accounting principles, with the maximum period being 20 years.
- Upon the disposal of such an intangible asset, a balancing statement should be prepared with any balancing addition being subject to Income Tax and any balancing deduction being tax deductible. The taxpayer has the option not to claim capital allowances for such intangible assets in a particular tax year.

This information has been prepared for the general information only and is not intended to be relied upon as accounting/tax or other professional advice.

Taxman
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