



# Grammarro Accounting Services Ltd

Member of Andreas Sofocleous Group of Companies

## The Amended Cyprus IP Box Regime

In late 2016, the Cypriot Parliament approved the laws amending the Income Tax Law with respect to the application of the Cypriot Intellectual Property Regime (IP Box Regime). The legislation has now been aligned with the provisions of the OECD BEPS Action 5 of the Base Erosion and Profit Shifting (BEPS) plan on Countering Harmful Tax Practices more effectively, taking into account Transparency and Substance.

The new legislation is effective as from 1 July 2016, but it also includes transitional provisions for assets which qualified under the old IP Box Regime.

### [I] Transitional Arrangements For Assets Qualifying Under the Old IP-BOX Regime

Under the old IP Box Regime, a notional deduction of 80% was applied to net income and gains derived from patents, copyrights and trademarks as defined in the relevant Cypriot legislation. In the case of a resulting loss, only 20% of the loss could be carried forward to subsequent years or surrendered to other group companies.

There are transitional provisions for persons who have entered the old IP Box Regime, which enables 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 acquisition were 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 which were acquired directly or indirectly from a related person during the period from 2 January 2016 until 30 June 2016 and which do not fall under the above categories.

Intangible assets qualifying for the transitional rules are those which as at 30 June 2016 either generated income or their development has been completed.

#### Limassol Office

Proteas House ,155 Makariou III  
Avenue  
Limassol 3026 ,Cyprus  
P.O. Box: 58159 Limassol 3731

Phone:+357 25 849000  
Fax: +357 25 849100  
E-mail: info@sofocleous.com.cy  
Website: www.sofocleous.com.cy

#### Kiev Office

36-D Saksagavskgov Str.  
Office2 ,Kiev 01033  
Ukraine

Tel: +380-444902003/4/5  
Fax: +380-444902006  
Email: kiev@sofocleous.com.cy



## [II] Provisions For The New IP-Box Regime

The provisions of the new legislation comply with the modified “nexus approach” which intends to ensure that, in order for a significant proportion of IP income to qualify for benefits, a significant proportion of the actual R&D activities must have been undertaken by the qualifying taxpayer itself.

The law allows for an amount equal to 80% of the **qualifying profits** earned from **qualifying intangible assets** to be allowed as a tax-deductible expense.

For each tax year the taxpayer may elect to claim the whole, part or no allowance. In case of a resulting loss, only 20% of the resulting loss could be carried forward or surrendered to other group companies.

### A. Qualifying intangible asset

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.

The provisions of the new IP Box Regime apply only to:

- \* Patents as defined in the Patents Law,
- \* computer software, and
- \* other intangible assets that are legally protected and fall within one of the following categories:
  - a: utility models, intellectual property assets that provide protection to plants and genetic material, orphan drug designations, and extensions to patent protection
  - b: non-obvious, useful and novel, where the person utilizing them in furtherance of a business does not generate annual gross income of more than

€7,500,000 from all intangible assets (€50,000,000 for a group of companies). These assets must be certified by a relevant authority either in Cyprus or abroad.

Business names (including brands), trademarks, image rights and other intellectual property rights used to market products and services are not considered as qualifying intangible assets.

### B. “Qualifying profits (QP)”

Qualifying profits means the proportion of the overall income (OI) corresponding to the fraction of the qualifying expenditure (QE) plus the uplift expenditure (UE) over the overall expenditure (OE) incurred for the qualifying intangible asset.

The amount of qualifying profit can be derived by applying the below formula:

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

### C. Overall income (OI)

Overall income arising from the qualifying intangible asset means the gross income accrued within the tax year, less the direct costs for generating such income.

Direct costs include all direct and indirect costs incurred in earning the income from the qualifying intangible asset, including the amortization of the cost of the intangible, as well as notional interest on equity contributed to finance the development of the qualifying intangible asset.

The overall income includes, but is not limited to the following:

- Royalties or other amounts in connection with the use of qualifying intangible asset.
- Any amount for a license for the operation of qualifying intangible asset.



- Any amount received from insurance or as compensation in relation to the qualifying intangible asset.
- Capital gains and other income from the sale of qualifying intangible asset.
- Embedded income of qualifying intangible asset arising from the sale of products or by using procedures that are directly related to this item.

#### D. Qualifying expenditure (QE)

Qualifying expenditure for qualifying intangible asset is the sum of total research and development costs incurred in any tax year, wholly and exclusively for the development, improvement or creation of qualifying intangible assets and which costs are directly related to the qualifying intangible assets.

Qualifying expenditure includes, but is not limited to:

- wages and salaries;
- direct costs;
- general expenses relating to installations used for research and development;
- expenses for supplies related to research and development activities;
- costs associated with research and development that has been outsourced to non-related persons.

#### but do not include:

- cost for the acquisition of intangible assets;
- interest paid or payable;
- costs relating to the acquisition or construction of immovable property;
- amounts paid or payable directly or indirectly to a related person to conduct research and development activities, regardless of whether these amounts relate to cost sharing agreement;

- costs which cannot be proved directly connected to a specific eligible intangible asset.

#### E. Up-lift expenditure (UE)

An uplift expenditure will be added to the above costs, which will be the lower of:

- 30% of the eligible costs or
- the total amount of the cost of acquisition and outsourcing to related parties for research and development in relation to the eligible intangible asset.

#### Overall expenditure (OE)

Overall expenditure which relates to a qualifying intangible asset is defined as the total of:

The qualifying expenditure (QE), and

The total cost of acquisition of the qualifying intangible assets plus the cost of outsourcing from related parties any Research and Development activities in relation to these assets (during any tax year).

#### [III] Maintaining Books And Records

Any person who claims benefit under the above Regime is obligated to maintain books and records for income and expenditure for each qualifying intangible asset.

#### [IV] Assets Which Do Not Qualify For The IP-Box Regime

The cost of acquiring an intangible asset which does not qualify for the transitional provisions or under the new rules and which asset is used in furtherance of the business of the person, can be amortized over the period of the useful life of the asset in accordance with accepted accounting principles with the maximum period being 20 years.