Taxation of Cyprus International Trusts

November 2012

Introduction

This information sheet explains how Cyprus International Trusts are taxed in Cyprus and how to ensure the obtaining of Cyprus Double Tax Treaty and applicable EU Directive benefits in cases that this Trust receives foreign income that is subject to foreign withholding taxes (e.g. dividend, interest or royalties).

General

The development of Cyprus as a favourable jurisdiction for the establishment of International Trusts has evolved over the years offering added dynamic benefits. Cyprus has a most attractive tax regime with respect to Trusts and has equally concluded a wide network of favourable double tax treaties. Non tax related benefits include that Cyprus does not impose any exchange control limitations, enables the relocation of a Trust and does not impose any registration or reporting requirements.

Cyprus International Trusts ("**CITs**") may efficiently be utilised for asset protection and wealth management, for estate planning, as a will substitute and as the means to preserve confidentiality on the anonymity of the owner of assets, securities and other property that may be vested in the Trust.

Notwithstanding the above, CITs are also commonly used for international tax planning purposes. Indicatively, the use of a Trust can affect the accumulation of profits in another tax efficient and effective jurisdiction.

Note: *In brief, qualifying Cyprus International Trusts at the time of establishment must meet the following criteria: The Settlor and Beneficiaries are non-Cyprus residents, the Trust does not own immovable property situated in Cyprus and there is at least one Cyprus resident trustee.*

Cyprus taxability of CITs

All incomes of qualifying CITs are tax neutral in Cyprus, provided the beneficiaries remain non-Cyprus residents and the CIT does not have Cyprus-sourced income or immovable property situated in Cyprus.

Application of Double Tax Treaty and EU Directive benefits

Cyprus has concluded a wide network of favourable Double Tax Treaties ("**DTTs**") and has access to applicable EU Directives, the benefits of which can be utilized by tax residents of either of the contracting states.

However, Trusts are not expressly included within the definition of a tax resident pursuant to the DTT provisions and equally do not qualify as persons or bodies of persons. As such, Trusts do not generally qualify for such DTT benefits.

On the other hand, Cyprus tax resident trustees, whether physical or legal persons, qualify as ‘persons’ for DTT purposes and would also be considered as taxable persons.

Furthermore, international case law generally supports the extension of DTT benefits to trustees conditional upon the satisfaction that the place of effective management of the Trust is essentially the place of tax residency of the trustee. Respectively, preservation of the effective management and control of the Trust in Cyprus is crucial. Care should be taken in order to avoid any direct or implied control of the Trust by the Beneficiaries and/or Settlor.

Given all these, CITs should generally be able to obtain DTT and applicable EU Directive benefits based on the Cyprus resident trustees who own the Trust property and are effectively managing the Trust.

Notwithstanding the aforementioned and as there are non-Cyprus resident beneficiaries to the Trust, some jurisdictions may still not consider the trustees as qualifying persons for obtaining the DTT and EU Directive benefits.

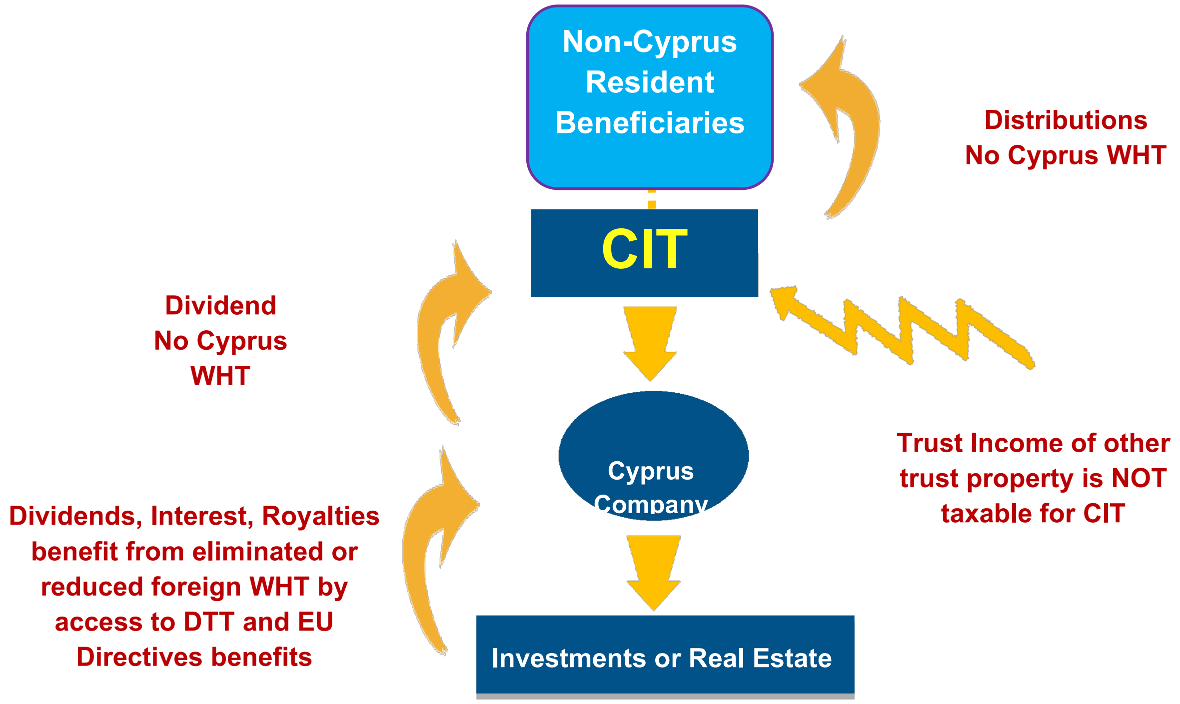
How to secure DTT and EU Directive benefits

In order to ensure the obtaining of DTT and EU Directive benefits and mitigating inherent risks that may exist in this respect, a carefully planned and implemented structure should be considered.

Provided that the use of a Trust cannot guarantee treaty protection in all cases, the use of an underlying Cyprus resident company could be considered for activities that could benefit from DTT and EU Directive provisions. Such activities could be transferred to this underlying Cyprus company which will carry out these activities. In line with this, a company is considered to be tax resident of Cyprus, and respectively be eligible for DTT and EU Directive benefits, provided the effective management and control of the company is exercised in Cyprus (e.g. by Cyprus resident directors).

REFER TO THE OUTLINE DIAGRAM BELOW

Outline Diagram



Abbreviations used:

WHT = Withholding Tax - CIT = Cyprus International Trust - DTT = Double Tax Treaty

NOTES:

The above is intended to provide a brief guide only. It is essential that appropriate professional advice is obtained. Our company will be glad to assist you in this respect. Please do not hesitate to contact us.