On October 7, 2010, during the official visit of Russian Federation President Medvedev to Cyprus, a Protocol to the Cyprus-Russia Double Taxation Avoidance Agreement was signed in Nicosia. This followed a period of intense negotiation between the respective governments. The business communities of both countries welcome the effects on business brought about by the Protocol.

One key aspect of the Treaty, its provisions on withholding tax rates, has not in any way been affected by the Protocol. Withholding tax rates continue to stand at the most favourable rates of 5% for dividends (for participations over EUR100,000; otherwise 10%) and 0% for interest and royalties for distributions from Russia, and 0% for all distributions from Cyprus, according to local tax legislation.

More importantly, signing this Treaty has paved the way for Cyprus to be removed from the Russian "black list," allowing access to the Russian participation exemption for Russian shareholders receiving dividends from eligible participations in Cyprus subsidiaries.

The move will open up further possibilities for Russian outbound investments through Cyprus, particularly to:

- Countries with which Cyprus maintains favourable treaties, such as countries of the Balkans, Central and Eastern Europe, Scandinavia, Commonwealth of Independent States, South East Asia, the Near and Middle East, India and China; and to
- European Union Member States, by taking advantage of Cyprus’s zero withholding tax regimes and the EC Parent-Subsidiary Directive, achieving zero withholding taxes on distributions all the way up to the Russian investors.

Although the modification of the article on exchange of information was initially perceived with some scepticism, it remains clear that information cannot be supplied which is not obtainable under the law or in the normal course of the administration of a contracting state, which in the case of Cyprus, requires the consent of the Attorney General.

Finally, the adjustment to the taxing rights of share disposal gains in property-rich companies also aligns the provisions of the Treaty with the OECD Model Tax Convention. The 4-year grace period allowed by the Protocol for its application allows existing real estate structures as well as proposed ones enough time to mitigate any possible disadvantages arising and to find alternative structuring solutions.
Summary of Main Changes Brought About by the Protocol

- Redefines eligibility for the reduced 5% withholding tax rate on dividends (instead of the general rate of 10%) to participations above EUR100,000 instead of US$100,000.
- Specifies distributions of mutual funds and similar investment vehicles/funds to be subject to normal Treaty withholding tax rates provisions.
- Provides for source state taxation of the income of mutual equity/investment funds investing primarily in immovable property.
- In general, the exclusive taxing right on gains on the disposal of shares remains with the country of residence of the seller.
- However, the Protocol provides for source state taxation of gains from the sale of shares in property-rich entities. This provision is to come into effect 4 years after the Protocol is fully ratified.
- Furthermore, the exclusive taxing right remains in the state of residence of the seller when the seller is a pension or provident fund, or when the relevant shares are listed on a recognized stock exchange, or when the share disposal is part of a qualifying reorganization.
- The exchange of information article has been modified and is now aligned with article 26 of the OECD Model Tax Convention on Income and Capital and with Cyprus legislation enacted since 2008.

Finally, the Protocol provides for limitation of treaty benefits to entities that are not registered within a contracting state but are nevertheless considered to be tax residents of that contracting state.

Amicorp and You

Amicorp Cyprus is available to:

- Assist with any queries you might have;
- Help you understand the effects of the Protocol’s provisions on your business;
- Assist in the set-up and maintenance of Cyprus entities;
- Coordinate with Amicorp offices worldwide and present you with a truly global choice in fulfilling your structuring requirements for investments inbound to and outbound from the Russian Federation.

For further information and assistance in structuring investments to and from Russia, contact your nearest Amicorp office or Amicorp Cyprus directly.

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New Developments

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