

The EU approved New Cyprus Tonnage Tax System

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The new tonnage tax system for Cyprus merchant shipping was approved by the European Commission on 24th March 2010 (case N. 37/2010), as **compatible with the requirements of the EU acquis**, in accordance with the relevant guidelines on State Aid to Maritime Transport. This simplified tonnage tax system is approved for the first time for an EU Member State, a state with an open registry. It extends the favourable benefits applicable to owners of Cyprus flag vessels and ship managers to owners of foreign flag vessels and charterers. It also extends the tax benefits that previously only covered profits from the operation of vessels in shipping activities, to cover profits on the sale of vessels, interest earned on funds used other than for investment purposes and dividends paid directly or indirectly from shipping related profits.

The Merchant Shipping (Fees & Taxing Provisions) Law was enacted in May 2010 and introduces a new tonnage tax system in Cyprus, applicable as from the fiscal year 2010. Full text of the Law in an English unofficial translation is available on our website www.shipping.gov.cy.

The new tonnage tax system contains most of the favourable features found in tonnage tax systems in other EU countries, and more. The regime, therefore, provides Cyprus with a competitive advantage and is expected to significantly contribute to the improvement of the already strong position of the country in the shipping world.

The main provisions of the new tonnage tax system are described below.

Beneficiaries

The tonnage tax system is available to any owner, charterer or ship manager who owns, charters or manages a qualifying ship in a qualifying shipping activity. The tonnage tax is calculated on the net tonnage of the ship according to a broad range of bands and rates prescribed in the legislation. The rates applicable to ship managers are 25% of those applied for ship owners and charterers.

Qualifying ship

A qualifying ship is any seagoing vessel certified under applicable international or national rules and regulations and registered in the ship register of any member of the International Maritime Organization and/or the International Labour Organization that is recognised by Cyprus.

The regime specifically excludes certain types of ships, such as fishing vessels, ships used primarily for sports or recreation, river vessels, non-self propelled floating cranes and tug boats, among others.

Qualifying shipping activity

Any commercial activity that constitutes maritime transport, crew management and/or technical management is considered a qualifying activity.

The definition of maritime transport includes the traditional carriage of goods and passengers, as well as ancillary services such as all hotel, catering, entertainment and retailing activities on board a qualifying vessel, the loading and unloading of cargo, the operation of ticketing facilities and passenger terminals. Towage, dredging and cable laying are also eligible for tonnage tax.

Ship owners

Ship owners of Cyprus flag ships automatically fall within the scope of the tonnage tax system. Ship owners of EU/EEA flag ships and/or third country flag ships may opt to be taxed under the tonnage system.

Ship owners of third country flag ships must comply with certain requirements to qualify for the option to be taxed under the new regime. These include the requirement that a share of their fleet be comprised of EU flag ships, which share must not be reduced in the three-year period (flag-share requirement) following the exercise of the option and that the commercial and strategic management of the fleet be carried out from the EU/EEA.

Any ship owner opting for the tonnage tax system must remain in the system for 10 years. Early withdrawal will result in penalties, calculated as the difference between the amount paid during the period the ship owner was under the tonnage tax system

and the amount that would have paid had it been subject to corporation tax in the same period. In addition, the ship owner will lose the right to opt for tonnage taxation until expiration of the 10-year period from the date the option was first exercised.

The tonnage tax system covers profits from shipping operations, dividends paid directly or indirectly out of such profits, profits on the sale of the ship and interest earned on funds used as working capital or for the financing, operation and/or maintenance of the ship.

Charterers

Any charterer who charters a ship under bareboat, demise, time or voyage charter is eligible for the tonnage tax system provided the tonnage of the ships under time and/or voyage charters do not exceed 75% of the total tonnage of ships chartered and owned for more than three consecutive years. This eligibility percentage increases to 90% if the ships chartered are EU/EEA ships or their crew and technical management are carried out from the EU/EEA. The charterers of third country flag ships must comply with the additional requirements that apply for third country flag ship owners (i.e. flag-share requirement).

An eligible charterer may opt to be taxed under the tonnage tax system, but once the option is made, it must remain in the system for 10 years. Early withdrawal will result in the penalties outlined above for ship owners.

The tonnage tax system covers profits from shipping operations, dividends paid directly or indirectly out of such profits and interest earned on funds used as working capital or for the payment of expenses arising out of the charter party.

Ship managers

A ship manager who provides crew and/or technical ship management services is eligible for the tonnage tax system provided it satisfies certain criteria. These include the maintenance of a fully fledged office, the employment of a sufficient number of qualified personnel (51% of whom should be EU/EEA citizens) and at least 2/3 of the management is carried out from the territory of the EU/EEA. Further, at least 60% of the fleet under management should be carrying an EU/EEA flag, while all ships and crew under management must comply with international standards and EU law requirements relating to maritime security, safety, training and certification of seafarers, the environment, on-board working conditions, and so on.

Other specific criteria must be complied with, depending on the ship management service provided (i.e. full implementation of the 2006 Maritime Labour Convention for crew managers and the ISM Code certification for technical managers).

The tonnage tax system covers profits from the provision of crew/or technical ship management services, dividends paid directly or indirectly out of such profits and interest earned on funds used as working capital or for the payment of expenses relating to the management of the ships. The 10-year option rule also applies to eligible ship managers and the same penalties apply for early withdrawal.

Tonnage Tax Rates

The following table summarises the applicable rates for the tonnage tax calculation:

Net Tonnage				
0 - 1.000	1.001 - 10.000	10.001 - 25.000	25.001 - 40.000	> 40.000
€ 36,50 per 100 NT	€ 31,03 per 100 NT	€ 20,08 per 100 NT	€ 12,78 per 100 NT	€ 7,30 per 100 NT

Note: The rates applicable to ship managers are 25% of the above.

Sample calculation of the annual tonnage tax for a 19.538 net tonnage vessel:

1.000 NT : 1000/100 = 10 x € 36,50 = € 365,00
 9.000 NT : 9000/100 = 90 x € 31,03 = € 2792,70
 9.500 NT : 9500/100 = 95 x € 20,08 = € 1907,60
 38 NT : 38/100 = 0.38 x € 20,08 = € 7,63

Annual tonnage tax due = € 5072,93