

# The New Cyprus Tonnage Tax System

The Cypriot maritime industry is one of the largest in the European Union, and 10<sup>th</sup> largest Worldwide. Cyprus is also the biggest ship management centre in the EU.

The European Commission approved under EU State Aid rules a scheme proposed by the Cyprus Government which allows shipping companies to opt to be taxed on the net tonnage of the fleet they operate (Tonnage Tax System – TTS) rather than corporation tax, which they would otherwise have to pay. Under certain conditions the TTS applies also to tug boats, dredgers and cable layers. The EU authorised the scheme until 31 December 2019. (EU Press Release IP/10/352 of 24.03.2010).

On 29 April 2010, the Cyprus Government passed the Merchant Shipping (Fees and Taxing Provisions) Law - No.44(I) 2010 (MSL). The Law is applicable from 1 January 2010. Since that date a number of Statutory Instruments (SI) and Circulars have been issued.

Cyprus now has a European Union approved “Open Registry” and the TTS allows for mixed activities subject to tonnage tax and corporation tax.

The main provisions of the MSL are:

- **Tonnage Tax System** – Under this system a qualifying owner, qualifying charterer or qualifying ship manager of a Cypriot or foreign ship is subject to an annual tax known as tonnage tax which is calculated on the basis of the net tonnage of ships.

Ref: MSL S2, S5 and SI 137/2012

- **Fees and Dues of Cyprus Ships** – For every Cyprus ship a fee of €300, referred to as “Cyprus Registry Maintenance Annual Fee”, is payable each year. This fee is payable in advance at the time the ship is registered, and subsequently it is paid at 31 March together with the tonnage tax.

Ref: MSL S4 and SI 352/2010,3

- **Maritime transport** means the carriage of goods or passengers by sea outside the territorial sea of the Republic, between a Cyprus port and a foreign port or an off-shore facility, or between foreign ports, or off-shore facilities. This definition includes:
  - a. The following ancillary activities to maritime transport:
    - i. In relation to the carriage of passengers by sea, all hotel, catering, entertainment and retailing activities on board a qualifying ship, provided that

these services are performed as ancillary activities to the activity of carriage of passengers by sea by that ship and are all consumed or used on board that ship;

- II. The provision of loading and unloading of cargo on a qualifying ship operated by the qualifying owner or the qualifying charterer, including the moving of containers within a port area immediately before or after the voyage;
  - III. The operation of ticketing facilities and passenger terminals in connection with shipping activities subject to tonnage tax;
  - IV. The operation of office facilities in connection with shipping activities subject to tonnage tax;
- b. The following other eligible for tonnage tax activities:
- I. Towage activities and dredging activities under conditions determined by Notification, in compliance with the applicable Community policy-guidelines on State aid to maritime transport, as adopted from time to time by the European Commission;
  - II. By analogy cable-laying activities.

Ref: MSL S2

- **Cyprus Ship** means a ship registered in the Cyprus Register, under the provisions of the Merchant Shipping (Registration of Ships, Sales and Mortgages) Laws of 1963 to 2005, and it also includes a foreign registered ship registered in the Special Book of Parallel Registration, under the provisions of Part VA of the same Law.

Ref: MSL S2

- **Qualifying Ship** means a seagoing vessel,
  - a. Certificated in accordance with the applicable international or national rules and regulations, and
  - b. Registered in the ship register of any member of the International Maritime Organisation (IMO) / International Labour Organisation (ILO) which is recognised by the Republic. This definition includes also any vessel which is engaged in the transportation of any United Nations (UN) or European Union (EU) humanitarian aid or is involved in any UN or EU humanitarian relief operation; The following ships are excluded from this definition:
    - I. Fishing and fish factory vessels;
    - II. Vessels used primarily for sport or recreation;
    - III. Vessels constructed exclusively for inland waterway navigation;
    - IV. Harbour, estuary and river ferries and tug boats;
    - V. Fixed offshore installations which are not used for maritime transport;
    - VI. Non self-propelled floating cranes;
    - VII. Non ocean-going tug boats;
    - VIII. Stationary vessels employed for hotel and / or catering operations (floating hotels or restaurants);

- IX. Vessels employed mainly as gambling facilities and /or casinos (floating or cruising casinos).

Ref: MSL S2

- **Qualifying Shipping Activity** means any commercial business or activity which constitutes maritime transport, or crew or technical management of qualifying ships.

Ref: MSL S2

- **A Qualifying Owner** is:
  - a. An owner of a Cyprus ship, or
  - b. A tax-resident owner of a Community ship, or
  - c. A tax-resident owner of a fleet of ships comprising community and non-community ships which are all qualifying ships engaged in qualifying activities.

Ref: MSL S6, S15

- **Taxation of Owners**
  - a. An owner of a Cyprus ship that is a qualifying ship engaged in qualifying shipping activity will be taxed under the TTS.
  - b. Owners of foreign ships have the right to opt to be taxed in respect of any particular year under the TTS but then must remain in the TTS for at least 10 years.

Ref: MSL S9, S7

- **A Qualifying Charterer** is:
  - a. The charterer of a Cypriot ship provided he is tax-resident and opts to be taxed under TTS, or
  - b. The charterer of a Community ship provided he is tax-resident and opts to be taxed under TTS, or
  - c. The charterer of a fleet comprising Community and non-Community ships who opts to be taxed under TTS provided that quotas relating to the number of Community ships is complied with.

In all the above cases the chartered ships/fleet are qualifying ships engaged in qualifying shipping activity.

Ref: MSL S18 & S25

- **Right of Charterers** – Charterers have the right to opt to be taxed under TTS for any financial year, but must then remain in the TTS for at least 10 years.

Ref: MSL S19

- **Parallel registrations** – Ships parallel registered-in (bareboat charter-in) and also ships parallel registered-out (bareboat charter-out) are considered Cyprus ships and covered by the TTS.

Ref: DMS Circular 42/2010

- **Additional requirements of charterers**

The total net tonnage of ships chartered-in and included in the TTS may not exceed 75% of the total net tonnage of all ships chartered-in or operated by a qualified charterer for more than 3 consecutive years. The percentage can be increased to 90% in cases where the chartered ships are either (a) registered in a maritime register of EUMS, or (b) their crew management and technical management are carried out in a EUMS.

Ref: MSL S47

- **Tonnage tax rates on owners and charterers** – Qualifying owners and qualifying charterers are subject to annual tonnage tax calculated in accordance with the rates published in the first Schedule of the MSL. Tonnage Tax is payable in advance on 31 March each year.

Ref: MSL S9 & S21 and SI 352/2010,3

- **Tonnage tax reductions** – owners of Cyprus ships and charterers of Community ships pay only 25% of the tonnage tax due in cases of lay-up, or being rendered inoperable due to judicial arrest, an act of piracy, armed robbery or force majeure.

Ref: MSL S11, S12, S24

- **Qualified Ship Manager** – A ship manager must satisfy the following conditions to become ‘qualified’ :

- a. must be a tax-resident of Cyprus who has opted to be taxed under the tonnage tax system and providing ship management services to qualifying ships of any nationality (flag), and
- b. must have a fully-fledged office in Cyprus and employ a sufficient number of qualified personnel. At least 51% of persons employed ashore are citizens of EUMS.
- c. qualifying ship managers may benefit from the tonnage tax system only with respect to qualifying ships entirely managed from the territory of any EUMS, irrespective of whether their management is provided in-house by the ship owner or whether it is partially or totally outsourced to one or more ship managers.
- d. Qualifying ship managers providing crew management services and / or technical management services, as the case may be, are eligible for the tonnage tax system if all the ships and crews they manage comply with relevant international standards and Community law requirements are fulfilled, in particular those relating to maritime security, safety, training and certification of seafarers, environmental performance and on-board working conditions.
- e. Every qualifying ship manager must also satisfy the following requirement:
  - I. At the time of opting to be taxed under the tonnage tax system, at least sixty percent (60%) of the fleet managed by the ship manager in terms of tonnage are Community ships, or
  - II. If at the date of opting to be taxed under the tonnage tax system the Community ships managed by the ship manager are less than sixty per cent (60%) of the fleet under his management in terms of tonnage, the following conditions must be satisfied:
    1. a share of the fleet managed by the ship manager are Community ships; and

2. the Community flagged share shall remain unchanged or increase within a period of three years from the date of opting to be taxed under the tonnage tax system.
- f. A qualifying crew manager must ensure that on all ships under its crew management the provisions of the Maritime Labour Convention 2006, of the International Labour Organisation (MLC), are fully implemented by the sea farer's employer, be it the ship owner or the crew manager.
  - g. A ship manager who performs technical management services only, must be certified under the ISM Code (Document of Compliance- DOC) by the competent authority of the flag States of the ships under its management and must be mentioned as the management company on the relevant Safety Management Certificates (SCM) of those vessels.

Ref: MSL S28, S32,S33,S34,S35,S36,S37,S39

- **Commercial ship management** – Commercial management services are not covered by the TTS as they do not fall under the definition of “ship management services”. Such services will be taxed under the income tax law at the rate of 12,5% on net profits. The terms “commercial management services” and “ship management services” are defined in the Law.

Ref: MSL S28, S2

- **Right of ship manager to opt for TTS** – Ship managers that are subject to the provisions of S28 have the right to opt to be taxed in respect of any year under TTS, but must remain in the TTS for at least 10 years.

Ref: MSL S29

- **Tonnage tax on ship managers** – qualifying ship managers are subject to an annual tonnage tax according to the rates in the Second Schedule. The rates are 25% lower than the rates for owners and charterers. Tonnage Tax is payable in advance on 31 March each year.

Ref: MSL S31 and SI 352/2010,3

- **Tonnage tax premium** – qualifying non-Community ships, forming part of a fleet, that are owned, chartered or managed by qualifying persons are subject to an increased tonnage tax as follows:
  - a. By thirty percent (30%) if the flag that they are entitled to fly appears in the Grey List of the Paris MOU;
  - b. By sixty percent (60%) if the flag they are entitled to fly appears in the Black List of the Paris MOU.

Ref: MSL S17, S27 & S40

- **More than one payment of tonnage tax for the same ship** – It can be the case that the owner, the charterer and the manager will pay tonnage tax for the same ship. However, they would then each be entitled to exemptions from all Cyprus taxes, as per the paragraph below.

- **Exemptions from income tax and other taxes** – All income of qualified owners, charterers and ship managers, gains from the sale or transfer of a ship, dividend paid to shareholders including indirect dividends, and interest, except interest on monies retained for investment, are exempt from income tax and all other taxes.

Ref: MSL S8, S20 & S30

Note: The exemptions apply to Cyprus, EU/EEA ships and ships flying other flags. Also applies to owners and charterers belonging to the same group.

There is no stamp duty on documents of purchase or sale, mortgage agreements and other documents relating to ships on the Cyprus Registry.

Ref: The Stamp Duty law

- **Losses**  
Losses arising from qualifying shipping activities under TT cannot be used for reducing the taxable income under the Income Tax Law nor can they be carried forward to future years. TT cannot be a deductible expense for income tax purposes.

Ref: MSL S44

Companies that do not have any other income apart from the income stated above, and who have submitted Form MSTT8 to the Department of Merchant Shipping, are not required to submit income tax returns to the Tax Department.

Ref: DMS Circular 22/2012

Note: We recommend that an income tax return be submitted each year so that a tax certificate can be obtained at any time.

- **Exemptions for crew members** – the salary and/or other benefits from the employment of the Master, the officers and crew of a qualifying Cypriot ship that is engaged in a qualifying shipping activity are exempt from income tax and other Cyprus taxes.

Ref: MSL S55

- **Withdrawal from the TTS** – if an owner of a foreign ship, a charterer of a ship, or a ship manager that opted-in to the TTS elects to withdraw from TTS (except as a result of the disposal of the ship, termination of a charter or termination of the ship management contract of all the ships under its management) it will be liable to corporation tax under the ITL. The tax paid under TTS will be credited against the tax payable under the ITL. If the tax paid under TTS is higher than the tax payable under the ITL no refund will be given.

Ref: MSL S7(3), S19(3) & S29(3)

- **Ring-fencing provisions** – related party transactions between a person subject to tonnage tax and another person must be “at arm’s length”. (The arm’s length principal applies – See CYP1-070(g))

Ref: MSL S41, ITL S33 and SI 136/2012

- **Separate accounting** – qualifying persons who earn income from a qualifying shipping activity and from non-qualifying activities must keep books and records that show each activity's income and expenditure separately, and prepare separate accounts.

Ref: MSL S44

- **All or nothing option** – qualifying persons who opt for the TTS must include all qualifying ships in the TTS. If the company belongs to a group of companies that are tax resident, then all companies of the group must enter the TTS.

Ref: MSL S46

- **Confirmation of qualifying status** – qualifying owners of foreign ships, charterers and ship managers will be taxed under the TTS provided that they first obtain a confirmation of their qualifying status from the Director of the Department of Merchant Shipping.

Ref: MSL S48

- **Date the TTS law comes into force and validity** – The TTS law is applicable from 1 January 2010 and it is valid to 31 December 2019. Subject to approval, it can be extended for another 10 years.

Ref: MSL S66

- **First Schedule**

#### TONNAGE TAX RATES FOR QUALIFYING OWNERS AND CHARTERERS OF CYPRUS AND FOREIGN SHIPS

On each qualifying ship of qualifying owners (ship owners) and charterers there shall be charged, levied and collected an annual tax calculated on the basis of the ship's net tonnage as follows:

- a. From zero to 1.000 units of net tonnage, for every 100 units of net tonnage there shall be charged, levied and collected a tonnage tax of €36,50.
- b. For every additional 100 units of net tonnage from 1.001 to 10.000 units, there shall be charged, levied and collected a tonnage tax of €31,03.
- c. For every additional 100 units of net tonnage from 10.001 to 25.000 units, there shall be charged, levied and collected a tonnage tax of €20,08.
- d. For every additional 100 units of net tonnage from 25.001 to 40.000 units, there shall be charged, levied and collected a tonnage tax of €12,78.
- e. For every additional 100 units of net tonnage in excess of 40.000 units, there shall be charged levied and collected a tonnage tax of €7,30.

Any residual tonnage of less than 100 units of net tonnage shall be charged proportionately.

Note: Sample calculation of the annual tonnage tax for a 19.538 net tonnage vessel: Net tonnage of each vessel is broken down into 100 units of net tonnage increments and specific annual rates are applied to each increment:

1.000 NT:	$1000/100 = 10$	$\times$	€36,50	=	€ 365,00
9.000 NT:	$9000/100 = 90$	$\times$	€31,03	=	€2792,70
9.500 NT:	$9500/100 = 95$	$\times$	€20,08	=	€1907,60
38 NT:	$38/100 = 0,38$	$\times$	€20,08	=	€ 7,63

Annual tonnage tax due	----- <u>€5072,93</u>
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Ref: MSL S9, S11, S13, S15, S21, S23 and S25

■ **Second Schedule**

**TONNAGE TAX RATES FOR QUALIFYING SHIP MANAGERS OF CYPRUS AND FOREIGN SHIPS**

On each qualifying ship of a qualifying ship manager there shall be charged, levied and collected an annual tax calculated on the basis of the ship's net tonnage as follows:

- a. From zero to 1.000 units of net tonnage, for every 400 units of net tonnage there shall be charged, levied and collected a tonnage tax of €36,50.
- b. For every additional 400 units of net tonnage from 1.001 to 10.000 units, there shall be charged, levied and collected a tonnage tax of €31,03.
- c. For every additional 400 units of net tonnage from 10.001 to 25.000 units, there shall be charged, levied and collected a tonnage tax of €20,08.
- d. For every additional 400 units of net tonnage from 25.001 to 40.000 units, there shall be charged, levied and collected a tonnage tax of €12,78.
- e. For every additional 400 units of net tonnage in excess of 40.000 units, there shall be charged levied and collected a tonnage tax of €7,30.

Any residual tonnage of less than 400 units of net tonnage shall be charged proportionately.

Note: Sample calculation of the annual tonnage tax for a 19.538 net tonnage vessel: Net tonnage of each vessel is broken down into 100 units of net tonnage increments and specific annual rates are applied to each increment:

1.000 NT:	$1000/400 = 2,50$	$\times$	€36,50	=	€ 91,25
9.000 NT:	$9000/400 = 22,50$	$\times$	€31,03	=	€ 698,17
9.500 NT:	$9500/400 = 23,75$	$\times$	€20,08	=	€ 476,90
38 NT:	$38/400 = 0,095$	$\times$	€20,08	=	€ 1,90

Annual tonnage tax due	----- <u>€1268,22</u>
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Ref: MSL S31

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# Contact us

We will be happy to provide further information.

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## Offices

### Nicosia Office – Headquarters

8 Stassinou Avenue, 1<sup>st</sup> Floor  
Photiades Business Centre  
1060 Nicosia, Cyprus  
PO Box 22545, 1522 Nicosia, Cyprus  
Tel: +357 22755656  
Fax: +357 22452055

mailbox@crowehorwath.com.cy  
www.crowehorwath.com.cy  
Skype name: crowehorwath-cyprus

### Limassol Office

Nicolaou Pentadromos Centre  
Office 801  
3026 Limassol, Cyprus  
PO Box 70726, 3802 Limassol, Cyprus  
Tel: +357 25255550  
Fax: +357 25255551

## Directors



**For tax and structuring advice**  
Ioannis Demetriades, FCCA TEP  
Managing Director  
Nicosia, Cyprus

[YiannisD@crowehorwath.com.cy](mailto:YiannisD@crowehorwath.com.cy)



**For tax and structuring advice**  
Andreas Pifanis, FCCA TEP  
Director  
Nicosia, Cyprus

[AndreasP@crowehorwath.com.cy](mailto:AndreasP@crowehorwath.com.cy)



**For audit and accounting matters**  
Marios Agathangelou, FCA  
Director  
Nicosia, Cyprus

[MariosA@crowehorwath.com.cy](mailto:MariosA@crowehorwath.com.cy)



**For financial advisory services**  
Chrysis Pegasiou, FCA  
Director  
Nicosia, Cyprus

[ChrysisP@crowehorwath.com.cy](mailto:ChrysisP@crowehorwath.com.cy)



**For advice on shipping and energy sectors**  
Emilios Ayiomamitis, ACA  
Director  
Limassol, Cyprus

[EmiliosA@crowehorwath.com.cy](mailto:EmiliosA@crowehorwath.com.cy)