

Cyprus Yacht Leasing Scheme

An Appealing VAT Regime

On 11th September 2014 by its Circular 188, the Tax Department amended its policy on the leasing of pleasure yachts.

The Tax Department has reduced to 5% of the yacht's value (from 8% that was applying before) the percentage profit that the lessor is expected to make. The Tax Department has also reduced to 2.5% of the yacht's value (from 4% that was applying before) the amount of the final payment that the lessee may pay to purchase the yacht at the end of the lease period, which is subject to the normal VAT rate of 19%.

We deem it important for the reader to call to mind the framework of the Tax Department's policy as was initially introduced on 13th March 2012 («the Policy»). The general guidelines of the Department's policy on the treatment of pleasure yacht leases for vat purposes, are now contained in the Circular 181 of 30th January 2014.

What is a Yacht Lease Agreement for the purposes of the Policy?

For the purposes of the Policy, the Yacht Lease Agreement is an agreement pursuant to which the lessor (the owner of the yacht) enters into a contract with the lessee (the person who lease the pleasure yacht from the owner) for the use of the pleasure yacht for an agreed consideration. The parties to the Yacht Lease Agreement may agree that the lessee shall have the right/option to purchase the pleasure yacht at the end of the lease period by paying an amount equal to a percentage over the total value of the pleasure yacht (as shall be seen further below in more detail). It must be stressed that the purchase of the pleasure yacht is a right/option granted to the lessee which must be exercised at the end of the lease period, in exchange of an additional consideration.

VAT treatment of the Yacht Lease Agreement

For VAT purposes, the leasing of the pleasure yacht is deemed as a “supply of services” and thus a taxable transaction at the basic rate of 19% to the extent that the pleasure yacht is used within the EU territorial waters. The lessor has the right to claim deduction of its VAT input pursuant to the provisions of the VAT Law.

Calculation of the EXTENT that the pleasure yacht is used within the EU territorial waters

Due to the objective difficulties in calculating the time that the pleasure yacht sails within or outside the EU territorial waters, the Tax Department has preset the percentage rates which reflect the part of the leasing term that the pleasure yacht is deemed to sail within the EU territorial waters, based on the length and type (distinguished to motor or sailing yachts) of the yacht. The length categories and rates have recently been amended by the Tax Department and the new rates are now contained in the Circular 191 of the Tax Department dated 29th April 2015.

Tables indicating the preset VAT rates

Table A: Motor Boats

Length of yacht	Percentage of use within the EU	VAT rate applicable on lease payments	Effective Cost in terms of VAT rate
Length over 65 meters	10%	1.90%	2.42%
Length between 45,01 and 65 meters	15%	2.85%	3.396%
Length between 24,01 and 45 meters	20%	3.80%	4.37%
Length between 14,01 and 24 meters	30%	5.70%	6.32%
Length between 8,01 and 14 meters	50%	9.50%	10.21%
Length up to 8 meters	60%	11.40%	12.16%
Vessels allowed to sail only within protected waters	100%	19%	19%

Table B: Sailing Boats

Length of yacht	Percentage of use within the EU	VAT rate applicable on lease payments	Effective Cost in terms of VAT rate
Length over 65 meters	10%	1.90%	2.42%
Length between 45,01 and 65 meters	15%	2.85%	3.396%
Length between 24,01 and 45 meters	20%	3.80%	4.37%
Length between 20,01 and 24 meters	30%	5.70%	6.32%
Length between 10,01 and 20 meters	50%	9.50%	10.21%
Length up to 10 meters	60%	11.40%	12.16%

Conditions for applying the special VAT rates to Yacht Leasing Agreements

For the application of the special VAT rates to the Yacht Leasing Agreement, the below conditions must apply collectively:

1. The lessor, owner of the pleasure yacht, must be a Cypriot company having a VAT number (i.e. registered for VAT purposes). The lessee can be any individual or a body corporate, irrespective of its place of origin;
2. The yacht must arrive in Cyprus within one month from the date that the Yacht Leasing Agreement enters into force. The VAT Commissioner may extend the aforementioned deadline, which in any event must not exceed the time by which the right/option of the lessor to buy the pleasure yacht must be exercised;
3. The lessee must pay to the lessor at the inception of the Yacht Leasing Agreement an initial payment amounting to 40% of the yacht's value and for which VAT must be paid at the applicable rate;
4. The term of the Yacht Leasing Agreement must not be less than three (3) months (90 days) and not more than 48 months;
5. The lease payments shall be paid on a monthly basis. For each monthly payment, VAT must be recorded and declared on the company's VAT form;

6. The lessor is expected to make a profit from the Yacht Leasing Agreement of at least 5% of the yacht's total value, as has been initially estimated by the Customs and approved by the VAT Commissioner;
7. At the inception of the Yacht Leasing Agreement, the total amount of the lease payments corresponding to the value of the yacht (less the 40% which has already been paid at the inception of the Yacht Leasing Agreement as per item 3 above) shall be increased by 2.5% which represents half (1/2) of the profit that the lessor is expected to make as per item 6 above.
8. The final payment at the end of the Yacht Leasing Agreement pursuant to which the ownership of the pleasure yacht passes to the lessee, must not be less than 2,5% of the yacht's value. This final payment is charged with the normal VAT rate (since 13.01.2014, the normal VAT rate in Cyprus is 19%).

Other Procedural Requirements

1. The above scheme must be approved by the VAT Commissioner from the outset. The VAT Commissioner shall also approve the value of the pleasure yacht and the VAT rate to be applied on the basis of the yacht's length and percentage of use within the EU (as per the above tables);
2. A certificate/documentation determining the value of the pleasure yacht and a copy of the Yacht Leasing Agreement must accompany the application to the VAT Commissioner for the approval of the scheme. The VAT Commissioner may request further information or documentation with regards to the use of the pleasure yacht;
3. If the lessee exercises the right to purchase the pleasure yacht at the end of the lease, the Tax Department shall issue a certificate to the lessee evidencing the payment of the VAT input, provided that the total of the payable VAT under the Yacht Leasing Agreement has been fully settled.

Other Considerations

It should be noted that the total profit of the lessee generated from the Yacht Leasing Agreement, namely 5% of the yacht's approved value, will be subject to income tax at the rate of 12.5%.

Example

A Cypriot resident and VAT registered company wishes to purchase a yacht and lease it to an individual. The yacht is motor powered and has a length of 40m. Purchase and valuation price is set at €10,000,000.

Yacht Information	
Value of the yacht	€10,000,000
Length	40 meters
Type of yacht	Motor
Lease period	48 months
Percentage of use within the EU (as per table A above)	20%

Calculations	
Yacht Value [A]	€10,000,000
Required Profit [B] = [A] x 2.5%	€250,000
Total Value [C] = [A] + [B]	€10,250,000
Initial contribution by lessee [D] = [A] X 40%	€4,000,000
Total Lease Instalments [E] = [C] – [D]	€6,250,000
Monthly Lease Instalments [F] = [E] / 48	€130,208.33
Final Payment [G] = [A] X 2.5%	€250,000
Taxable Income [H] = A x 5%	€500,000

VAT & Tax							
VAT Calculations	Amount	VAT Applicable Rate	Year 1	Year 2	Year 3	Year 4	Total
Initial Contribution	€4,000,000	3.8%	€152,000				€152,000
Monthly Lease Instalments	€130,208.33	3.8%	€59,375	€59,375	€59,375	€59,375	€237,500
Final Payment	€250,000	19%				€47,500	€47,500
Total VAT Paid							€437,000
Effective VAT Rate	4.37% (Total Vat Paid / Yacht Value)						
VAT benefit	€1,463,000						
Tax Calculations	Amount	Applicable Income Tax Rate	Year 1	Year 2	Year 3	Year 4	Total
Taxable Profit	€500,000	12.5%	€15,625	€15,625	€15,625	€15,625	€62,500