

# CYPRUS FIDUCIARY ASSOCIATION

## **CYFA 2023 Seminar #10: “Local Direct Tax and VAT Developments”**



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and Mr. Andreas Papagavriel**

# TOPICS OF DISCUSSION

- 5% reduced VAT rate on primary residence (new rules)
- Additional services/goods subject to 0% VAT rate and to a super reduced VAT rate of 3%
- 0% zero VAT rate on certain goods until 30 April 2024
- Amendment of 'table A' of the 7<sup>th</sup> Schedule of VAT Law
- Tax treatment of income derived from self-catering accommodation rented out via online platforms
- Amendments to article 8(23A) of the income tax law (50% exemption)
- Withholding tax on payments to blacklisted jurisdictions
- Double tax treaty between Cyprus and Netherlands
- Suspension of the double tax treaty between Cyprus and Russia
- DAC 7 – Reporting obligation for digital platform operators
- Transfer pricing legislation in Cyprus

# **5% REDUCED VAT RATE ON PRIMARY RESIDENCE (NEW RULES)**

### Old provisions applicable until 15 June 2023

Based on the old provisions of the VAT Law (95(I)/2000), the reduced rate of 5% VAT was applicable to the first 200 sqm of the buildable area, in accordance with the architectural plans submitted to the competent authority irrespective of the total buildable area of the property or the total value of the transaction.

### Transitional provisions (applicable until 31 October 2023)

In the cases where planning permission has been obtained or an application for such permission has been submitted to the competent authority until 31 October 2023, the old provisions will be applicable.

Thus, the reduced rate of 5% VAT will be applicable to the first 200 sqm of the buildable area, irrespective of the total buildable area of the property or the total value of the transaction.

*\*Requirement to file the application for the reduced rate of 5% VAT within 3 years from 16 June 2023*

### New provisions applicable as of 16 June 2023

Based on the new provisions of the VAT Law (95(I)/2000) which are applicable as of 16 June 2023, the reduced VAT rate of 5% will apply to the first 130 sqm of a primary residence, up to a value of €350,000, provided that :

- The total value of the property does not exceed €475,000; and
- The total buildable area does not exceed 190 sqm.

As an exception to the above, people with disabilities can apply for the reduced VAT rate of 5% on the first 190 sqm of buildable area, irrespective of the total buildable area of the property.

Furthermore, for families with more than three children (i.e. at least four children), the total buildable area is increased by 15 sqm for each child above the three children (relevant provisions to be covered by a circular).

### Application of the reduced VAT rate of 5% for another property within a period of 10 years

Based on the new provisions of the VAT Law (95(I)/2000), a person can apply for the 5% VAT on another property before the lapse of 10 years, provided that:

- The person notifies the Commissioner within thirty (30) days from the date that he/she ceased using the first property as a place of residence; and
- He/she pays the difference between the VAT which resulted from the application of the reduced VAT rate of 5% and the standard VAT rate of 19% attributable to the remaining period of the 10 years for which the property will not be used as the primary place of residence (except in the case of death of the beneficiary or in the case of transfer by the beneficiary to any adult child, provided that the said child is a beneficiary at the time of transfer).

### Example 1:



- Building area: 160sqm
- Total Value: €370.000
- People with disabilities: No
- Large Family (number of children): No

### Calculations

Transaction value subject to 5% VAT → €284.375 (i.e. (130 sqm./160 sqm.) × €350.000)

Transaction value subject to 19%VAT → €85.625 (i.e. €370.000 - €284.375)

VAT 5% × €284.375 = €14.219

VAT19% × €85.625 = €16.269

Total VAT                    €30.488

### Example 2:



- Building area: 220 sqm
- Total Value: €475.000
- People with disabilities: No
- Large Family (number of children): 5

### Calculations

Transaction value subject to 5% VAT → €254.545 (i.e. (130sqm.+15sqm.+15sqm.)/(190sqm.+15sqm.+15sqm.) × €350.000)

Transaction value subject to 19%VAT → €220.455 (i.e. €475.000 - €254.545)

VAT 5% × €254.545 = €12.727

VAT19% × €220.455 = €41.886

Total VAT                    €54.613



### Example 3:



- Building area: 230 sqm
- Total Value: €475.000
- People with disabilities: Yes
- Large Family (number of children): No

### Calculations

Transaction value subject to 5% VAT → €392.391 (i.e. (190sqm./230sqm.) × €475.000)

Transaction value subject to 19%VAT → €82.609 (i.e. €475.000 - €392.391)

VAT 5% × €392.391 = €19.619

VAT 19% × €82.609 = €15.696

Total VAT                    €35.315

**ADDITIONAL SERVICES/GOODS SUBJECT TO 0% VAT RATE TO  
A SUPER REDUCED VAT RATE OF 3%**

## ADDITIONAL SERVICES/GOODS SUBJECT TO 0% VAT RATE TO A SUPER REDUCED VAT RATE OF 3%

The Official Gazette of the Republic published on 21 July 2023 introduced certain amendments to the VAT legislation. These amendments established a super-reduced VAT rate of 3% for certain goods and services and extended the application of 0% VAT rate on goods used by people with disabilities.

The super-reduced VAT rate of 3% applies for the following **services**:

- Right of entry from debut performance of theatrical, musical, dance or classical plays.
- Street cleaning, waste collection and waste treatment services performed by private entities, excluding the services provided by national and local bodies or public interest entities.
- Disposal and treatment of wastewater and emptying residence and industrial tanks.

## ADDITIONAL SERVICES/GOODS SUBJECT TO 0% VAT RATE TO A SUPER REDUCED VAT RATE OF 3%

The super-reduced VAT rate of 3% also applies to the following **goods**:

- Supply of books, newspapers and magazines in hardcopy or electronic format (including brochures, prospectuses, children's books, colouring books, printed or handwritten sheet music, hydrographic and similar maps), excluding publications which are intended wholly or mainly for advertising purposes, publications which are wholly or mainly comprised of video content or acoustic music and publications of non-profit organizations as well as any related services.
- Special lifting devices (stairs, lifts, similar lifting equipment) for people with disabilities.
- Wheelchairs and other vehicles for people with disabilities with or without a motor or other propulsion mechanism.
- Orthopedic items and appliances including medical surgical belts, bandages and crutches.
- Splints, supports and other goods or devices intended for fractures.
- Prosthetic items.
- Devices for the facilitation of hearing for the deaf and other handheld devices, carried by persons or introduced into the human body for the purpose of filling a deficiency or treating a disability.

## ADDITIONAL SERVICES/GOODS SUBJECT TO 0% VAT RATE TO A SUPER REDUCED VAT RATE OF 3%

The 0% VAT rate applies to the following goods:

- Typewriters with Braille characters and special electronic typewriters for people with disabilities.
- Wheelchairs and other vehicles with or without a motor or other propulsion mechanism, intended exclusively for personally use by people with disabilities.

**0% VAT RATE ON CERTAIN GOODS UNTIL 30 APRIL 2024**

On 2 May 2023, the Council of Ministers decided to implement a temporary amendment to the VAT Law, to apply a 0% VAT rate on certain essential goods, which will be applicable until 31 October 2023.

On 13 September 2023, the Council of Ministers decided to extend the temporary application of the 0% VAT rate on the relevant goods. Furthermore, coffee and sugar were also added to the list of those goods. The extension will be effective until 30 April 2024.

The essential goods affected by the temporary reduction in the VAT rate are the following:

*From 5 May 2023 until 30 April 2024*

- Bread – all types of fresh or frozen bread with or without yeast (e.g., white, black, wholegrain, multigrain, rustic, rye, cornbread, baguette, ciabatta, sliced bread, bread roll, Cypriot pita bread). Pastries, dried bread and any bread with additional ingredients, such as raisins, nuts, aromatics, are not included.
- Milk – fresh milk (e.g., cow's milk, goat's milk, sheep's milk), sweetened, condensed, long-life, flavored milk (e.g., chocolate, banana), organic milk (e.g., almond, soy, rice).

- Eggs.
- Baby Food – in powder, dry, or liquid form intended for consumption by children. Snacks (e.g., chips, nuts, sweets, chocolates, ice cream) are not included.
- Baby diapers.
- Women's hygiene products – (tampons, sanitary pads and incontinence pads).
- Adult diapers.

### From 1 November 2023 until 30 April 2024

- Coffee - unroasted, roasted whole beans, ground, powdered, instant coffee, flavored coffee, caffeinated or decaffeinated, in any packaging. (Excludes ready-to-drink or beverage products prepared using coffee as raw material which are consumed cold or hot).
- Sugar - crystalline (white, brown, black), fine (powdered), coarse, in cubes, in sachets.



# **AMENDMENT OF 'TABLE A' OF THE 7<sup>TH</sup> SCHEDULE OF VAT LAW**

### Additional transactions that are exempt from VAT

On 13 October 2023, the Council of Ministers has amended 'table A' of the 7<sup>th</sup> Schedule of VAT Law, by adding the following to the exempt transactions for VAT purposes:

- Education of all levels, professional education, training, retraining, as well as the provision of services and delivery of goods closely related to these, provided by trainers (including training centres) that are certified by the Cyprus Human Resources Development Authority ("HRDA").

*\*The view of the Tax Department is that the above only covers seminars that are reimbursed by the HRDA. Official guidance is expected regarding this.*

# **TAX TREATMENT OF INCOME DERIVED FROM SELF-CATERING ACCOMMODATION RENTED OUT VIA ONLINE PLATFORMS**

On 13 September 2023, the Cyprus Tax Authorities issued Circular No. 10/2023 to clarify the tax treatment of income derived from self-catering accommodation rented out via online platforms (such as Airbnb, Booking.com etc.).

In case all the following conditions are met, the income that property owners will be generating by renting out their property through online platforms will be considered as income falling in their ordinary business activities and it should only be subject to income tax (and not subject to special defence contribution):

- The property which generates the rental income is registered or had to be registered in the Register of Self-Service Accommodations; and
- The owner of the property is VAT registered (or had to be registered) and imposes VAT at the rate of 9% on the income generated from the property; and
- The rental of the property is short-term, recurring and generally it is made to different persons each time.

# TAX TREATMENT OF INCOME DERIVED FROM SELF-CATERING ACCOMMODATION RENTED OUT VIA ONLINE PLATFORMS

*(i) The owner (individual or legal entity) manages the immovable property for the purpose of renting it out as described above*

Subject to Income Tax (Rental Income less expenses incurred).

Not subject to Special Defence Contribution ("SDC").

Owners who are individuals are subject to General Health System ("GHS") contributions.

*(ii) The owner (individual or legal entity) assigns the management of the immovable property to manager for the purpose of renting it out as described above*

Subject to Income Tax (Rental Income less expenses incurred, including agent fees).

Not subject to Special Defence Contribution ("SDC").

Owners who are individuals are subject to General Health System ("GHS") contributions.

# TAX TREATMENT OF INCOME DERIVED FROM SELF-CATERING ACCOMMODATION RENTED OUT VIA ONLINE PLATFORMS

*(iii) The owner of the property (individual or legal entity) rents out the property for a fixed rental amount to a tenant, who has the exclusive exploitation rights on the immovable property, for a short-term or long-term basis **AND** the tenant sub-leases the property as described above (the tenant bears all the expenses on the immovable property as well)*

## Subject to Income Tax:

- For individuals – gross rental income less the 20% deduction on gross rents, capital allowances and interest expense.
- For legal entities – gross rental income less the expenses incurred wholly and exclusively for the generation of the rental income, capital allowances and interest expense.

## Subject to Special Defence Contribution (“SDC”):

In case the owner is an individual who is tax resident and domiciled in Cyprus or a legal entity tax resident in Cyprus, the gross rental income reduced by 25% is subject to 3% SDC.

Owners who are individuals are subject to General Health System (“GHS”) contribution.

# **AMENDMENTS TO ARTICLE 8(23A) OF THE INCOME TAX LAW (50% EXEMPTION)**

## Income Tax Law - 50% exemption (Article 8(23A))

### Provisions applicable until 30 June 2023

Based on the initial provisions of article 8(23A) that were applicable until 30 June 2023, the 50% exemption from income tax on the remuneration from employment will be granted to individuals that take up first employment in Cyprus, subject to the following:

- The exemption will be granted in any tax year in which the remuneration from employment in Cyprus exceeds the amount of €55.000, provided that during the first or second year of employment the remuneration exceeded the amount of €55.000 per annum.
- The exemption will be granted if the individual was not a resident of Cyprus for 10 consecutive years prior to his/her employment.
- The exemption will be granted in the cases where the first employment in Cyprus will commence on or after 1 January 2022.
- The exemption will be granted for a period of 17 years starting from the year of employment in Cyprus.



## Income Tax Law - 50% exemption (Article 8(23A))

### Amended provisions published on 30 June 2023

The amendments that were made to article 8(23A) on 30 June 2023 and are applicable retrospectively as of 1 January 2022 are the following:

- The exemption from income tax will be granted if the individual was not a resident of Cyprus for 15 consecutive years (previously 10 years) prior to any employment in the Republic.
- The exemption will be granted for a period of 17 years from the date of employment (or until the termination of the provisions of article 8(23A)), irrespective of whether the individual changed his/her employer during the 17 years. Previously, the exemption was only granted for the first employment of the individual in Cyprus.
- It should be noted that the above amendments also apply to the transitional provisions that were initially introduced for article 8(23A) when the legislation was published in the Official Gazette of the Republic on 26 July 2022.

# AMENDMENTS TO ARTICLE 8(23A) OF THE INCOME TAX LAW (50% EXEMPTION)

	<b>8(23A) – up to 30 June 2023</b>	<b>8(23A) – after 30 June 2023</b>
<b>Employment eligible for the exemption</b>	First employment in the Republic (from 1 January 2022 until 30 June 2023)	Any employment in the Republic (from 1 January 2022 onwards)
<b>Exemption rate</b>	50% exemption	50% exemption
<b>Remuneration</b>	Above €55.000	Above €55.000
<b>Period of exemption</b>	17 years from the year of first employment (or until termination of the first employment, if this is earlier)	17 years from the year of employment
<b>Period during which the individual was not a tax resident of Cyprus prior to commencement of employment</b>	≥ 10 and < 15	≥ 15
	<b>Transitional Provisions</b>	
<b>Individuals that were eligible for the provisions of Article 8(23)</b>		
<b>Employment during the years 2016-2021 with remuneration &gt;€55.000</b>	Eligible for the exemption only on remuneration from first employment in the Republic for a period of 17 years from the year of first employment (or until termination of the first employment, if this is earlier)	Eligible for the exemption on remuneration from any employment in the Republic for a period of 17 years from the year of employment
<b>Employment during the years 2016-2021 with remuneration ≤€55.000 that was increased to &gt;€55.000 up to 26 January 2023</b>		

# **WITHHOLDING TAX ON PAYMENTS TO BLACKLISTED JURISDICTIONS**

1. As of 31 December 2022, Cyprus applies withholding tax (“WHT”) on certain outbound payments of dividends, interest and royalties, in the cases where the recipient is a Company which is tax resident in an EU blacklisted jurisdiction (or incorporated in such jurisdiction but is not considered as tax resident anywhere).
2. The provisions are only applicable to payments made by Companies and are summarized below:
  - Dividends → 17% provided that there is more than 50% participation/entitlement to profits by the receiving company, with the exception of dividends paid by Cypriot tax resident companies listed on a recognized stock exchange.
  - Interest → 30% with the exception of interest relating to securities listed on a recognized stock exchange.
  - Royalties → 10% irrespective of whether the asset for which the royalty is paid is for use in Cyprus or abroad.
3. There is also an intention to apply WHT (or to deny deductions) on outbound payments made to low tax jurisdictions (expected to come into force by the end of 2024).

# **DOUBLE TAX TREATY BETWEEN CYPRUS AND NETHERLANDS**

## Double Tax Treaty (“DTT”) between Cyprus and Netherlands

On 18 April 2023, the Dutch Parliament approved the DTT between Cyprus and Netherlands, which was signed on 1 June 2021. The DTT is expected to be effective from 1 January 2024.

The main provisions of the DTT are summarised below:

- Dividends → No withholding tax (“WHT”) if the beneficial owner is:
  - a) a company that holds directly at least 5% of the capital of the company paying the dividends, throughout a 365-day period that includes the day of the dividend payment; or,
  - b) a recognised pension fund which is generally exempt under the other Contracting State

\*Otherwise, the treaty provides for a 15% WHT.

- Interest → No WHT, provided that the recipient is the beneficial owner of the income.
- Royalties → No WHT, provided that the recipient is the beneficial owner of the income.
- Immovable-property rich company clause for disposal of shares → gain may be subject to capital gains tax in the Contracting state where the property is located.
- Limitation of Benefits clause → benefits may be denied if principal purpose test (“PPT”) is met.

# **SUSPENSION OF THE DOUBLE TAX TREATY BETWEEN CYPRUS AND RUSSIA**

## **Suspension of the DTT between Cyprus and Russia as of 8 August 2023**

On 8 August 2023, Russia published a presidential decree suspending the validity of certain provisions of DTTs concluded by Russia with countries it considers "unfriendly" states, including Cyprus.

From the date of issue of the decree, the application of reduced WHT or tax exemptions in relation to income covered by DTT is suspended. This covers the following:

- Reduced WHT 15% on interest (instead of 20%)
- WHT 0% on royalties (instead of 20%)

It should be noted that the suspension of the DTT is done unilaterally, as Cyprus continues to honour and implement the provisions of the DTT.



# **DAC 7 – REPORTING OBLIGATION FOR DIGITAL PLATFORM OPERATORS**

### What is DAC 7

- DAC7 introduces reporting obligations for EU and non-EU Digital Platform Operators (“DPOs”) that connect certain ‘Reportable Sellers’ to buyers.
- DAC7 **only covers the intermediation services** provided by DPOs and therefore it does not apply in the cases of e-shops where sellers own their own products/services.
- DPOs have the option to register in only one Member State (also applicable to DPOs located outside EU).
- The objective is to provide information to EU Member States to conduct accurate income tax and VAT assessments for ‘Reportable Sellers’.
- The information is reportable by 31 January of the year following the calendar year in which the seller is identified as a ‘Reportable Seller’ and the first information should be reported for 2023 (the first reporting should therefore take place by 31 January 2024).
- DAC7 has been transposed into the Cyprus legislation on 3 November 2023 and the first reports must be filed with the Cypriot Tax Department no later than 31 January 2024 to avoid any penalties for non-compliance. DPOs must register with the Cypriot Tax Department by 31 December 2023 the latest (more details on the registration process are expected).

### Key Definitions

- ‘Reportable Seller’ – a platform user (individual or entity) that carries out a ‘Relevant Activity’ and is resident in an EU Member State OR rents out immovable property located in an EU Member State.
- ‘Relevant Activity’ – Any activity (domestic or cross-border) carried out for a consideration and being any of the following:
  - Rental of immovable property (i.e. residential, holiday, commercial)
  - Personal services (i.e. time or task-based work such as freelancing)
  - Sale of goods (i.e. new or used, B2B or B2C)
  - Rental of any mode of transport (i.e. cars)

### Key Definitions

- The following **platforms** are outside the scope of DAC7:
  - Platforms exclusively allowing users the processing of payments in relation to a ‘Relevant Activity’.
  - Platforms exclusively allowing users to list/advertise a ‘Relevant Activity’.
  - Platforms exclusively redirecting/transferring users elsewhere.
- The following **entities** are outside the scope of DAC7:
  - Governmental entities.
  - Listed entities.
  - Entities for which the DPO facilitated more than 2.000 relevant activities in a calendar year, relating to the **rental of immovable property** units located at the same street address, owned by the same owner and offered for rent on a platform by the same seller.
  - Entities for which the DPO facilitated less than 30 relevant activities in a calendar year, relating to the **sale of goods** for which the total consideration did not exceed €2.000.

## Transfer Pricing

## Amendment to Article 33 of Income Tax Law – Related parties

- On 30 June 2022, the Cypriot parliament approved amendments to Article 33 of the Cypriot Income Tax Law (ITL) and the issuance of the relevant Transfer Pricing Regulations
- Amendments are applicable from 1 January 2022
- Alignment of local rules with **OECD Transfer Pricing Guidelines**

### Introduction of a **25% relationship threshold** for connected parties

- Two companies are considered **related parties** if the following conditions are met:
  - A. Hold 25% of the voting rights or share capital of both companies
  - B. Have the right to at least 25% of the income of both companies
- A company is considered related to a **person** if the following conditions are met:
  - A. The person holds directly or indirectly at least 25% of the Company's voting rights or share capital
  - B. The person has a right to a share of at least 25% of the income of the Company

## **Cont. - Amendment to Article 33 of Income Tax Law – Related parties**

### **Transfer Pricing documentation requirements:**

1. Master File
2. Local File
3. Summary Information Table (SIT)

### **Introduction of Advance Pricing Arrangement (APA) framework**

*\*Requirements are fairly in line with the recommendations of the OECD on Transfer Pricing Guidelines for MNE and Tax Administrations (OECD TP Guidelines).*

## Master Documentation File

### Master File is intended to provide a high-level overview of an MNE group including:

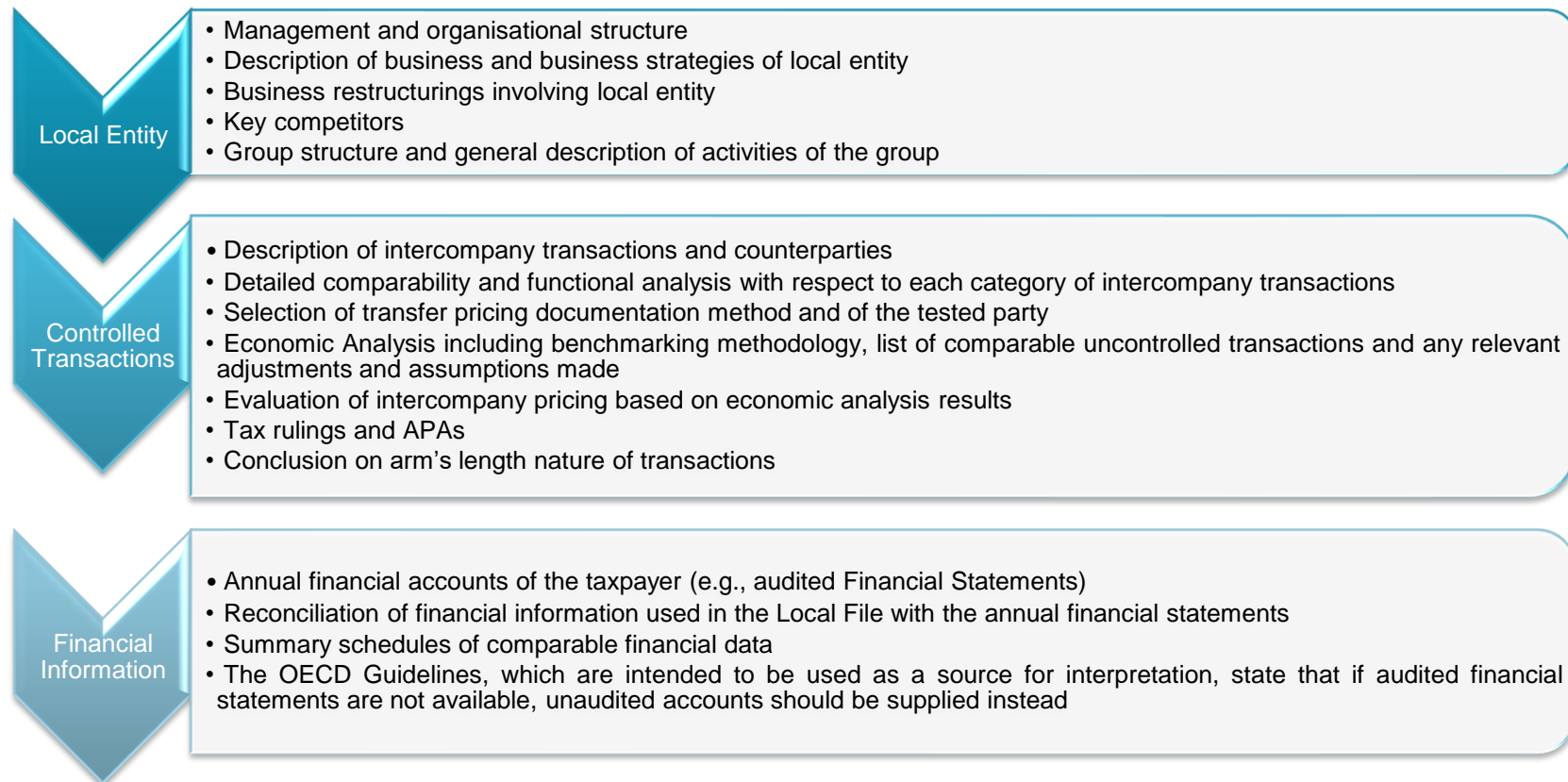
- Overview of the MNE group business
- Nature of its global business operations
- Its overall transfer pricing policies, and
- Its global allocation of income and economic activity in order to assist tax administrations in evaluating the presence of significant transfer pricing risk
  
- Only Cyprus tax resident entities that are the ultimate or surrogate parent entity of an MNE group falling under the scope of Country-by-Country reporting have an obligation to prepare and maintain a Master File.
  
- Prepared annually by deadline of submission of the TD4, submitted upon request (within 60 days)
  
- Contents in line with BEPS Action 13
  
- Content of Master File:
  1. Organizational structure
  2. Description of MNE's business
  3. MNE's intangibles
  4. MNE's intercompany financial activities
  5. MNE's financial and tax position
  6. CbC Report



## Local Documentation File

- Local File is intended to provide **more detailed information** relating to specific intercompany transactions affecting a specific jurisdiction
- Cyprus tax resident persons and PE in Cyprus of non-Cyprus tax residents are exempted if arm's length value of transactions in aggregate is less than EUR750.000 per category (e.g., sale/purchase of goods, provision/receipt of services, financing transactions)
- Prepared annually by deadline of submission of the TD4
- Submitted upon request (within 60 days)
- Contents in line with BEPS Action 13 / Quality Review by local auditor

## Contents of Local File



## Summary Information Table (SIT)

- A return that contains a list of intercompany transactions for specific tax years
- Not to be considered as a complete and extensive documentation
- Electronically submitted on an annual basis to the tax authorities
  
- Content of SIT >>

Taxpayer information	Counterparty information	Description of transactions
Name TIC Tax Year Contact Details	Name TIC Tax Jurisdiction	<b>Categories</b> <ul style="list-style-type: none"><li>• Goods</li><li>• Services</li><li>• Intellectual Property</li><li>• Financing transactions</li><li>• Other types</li></ul> <b>Amount per transaction</b>



## Thresholds, Deadlines & Penalties

	Master File	Local File	Summary Information Table (SIT)
<b>Threshold</b>	<ul style="list-style-type: none"> <li>Consolidated revenues exceeding EUR 750,000,000</li> <li>Ultimate or Surrogate Parent entity is a Cypriot tax resident, subject to CbCR</li> </ul>	<p><b>Obligation only if:</b></p> <ul style="list-style-type: none"> <li>Aggregated value of controlled transactions falling within a particular category* &gt; EUR 750,000</li> </ul> <p><i>*(goods, services, IP related or financial transactions)</i></p>	<ul style="list-style-type: none"> <li>Obligation exists as long as long there is an obligation for a Local File</li> </ul>
<b>Preparation Deadline</b>	By the Income Tax Return submission (e.g., 15 months following calendar year-end)		
<b>Submission Deadline</b>	Upon request should be made available within 60 days, starting from receipt of request		Concurrently with the Income Tax Return
<b>Annual preparation or update requirement</b>	Yes	Yes	Yes
<b>Local sign-off requirement</b>	No	Yes	N/A
<b>Penalties</b>	<p><b>If notice from CTD to provide TPD (within 60 days) and taxpayer fails to do so:</b></p> <ul style="list-style-type: none"> <li>If submitted between 61 and 90 days after request date: <b>€5,000</b></li> <li>If submitted between 91 and 120 days after request date: <b>€10,000</b></li> <li>If not submitted or submitted after the 120th day: <b>€20,000</b></li> </ul>		<p><b>€500</b> (for late or non-submission)</p>

# **Transfer Pricing Circular: Simplification Measures / Safe Harbour Rules**

- On 6 July 2023, the Commissioner of Tax issued circular 6/2023 providing clarifications and guidance on the applicability of the Transfer Pricing (TP) Legislation effective as of 1 January 2022, on categories of transactions which do not exceed the threshold of €750.000, and thus do not create the obligation for the preparation of a Cyprus Local File.
- The circular provides guidance on the minimum requirements and the approach to be applied for documenting these transactions, along with the pricing methods to be applied. In short, the taxpayer will have the option to proceed with a “simplified” transfer pricing study for such transactions/ categories of transactions or in specific cases, apply simplification measures.

With regards to the simplification measures these are applicable in the following cases:

1. Financing arrangements with related parties involving borrowings (e.g., back-to-back loans).
2. Financing arrangements to related parties financed out of equity.
3. Financing obligations/ arrangements of which the funds are used in the business.
4. Low value-added services.



The simplified TP study should include the following sections:

1. Short functional and risk analysis.
2. Entity characterization.
3. Method of documentation selected and basis of selection.
4. Economic analysis with comparability search results based on OECD guidelines.

The application of the simplification measures will require the following:

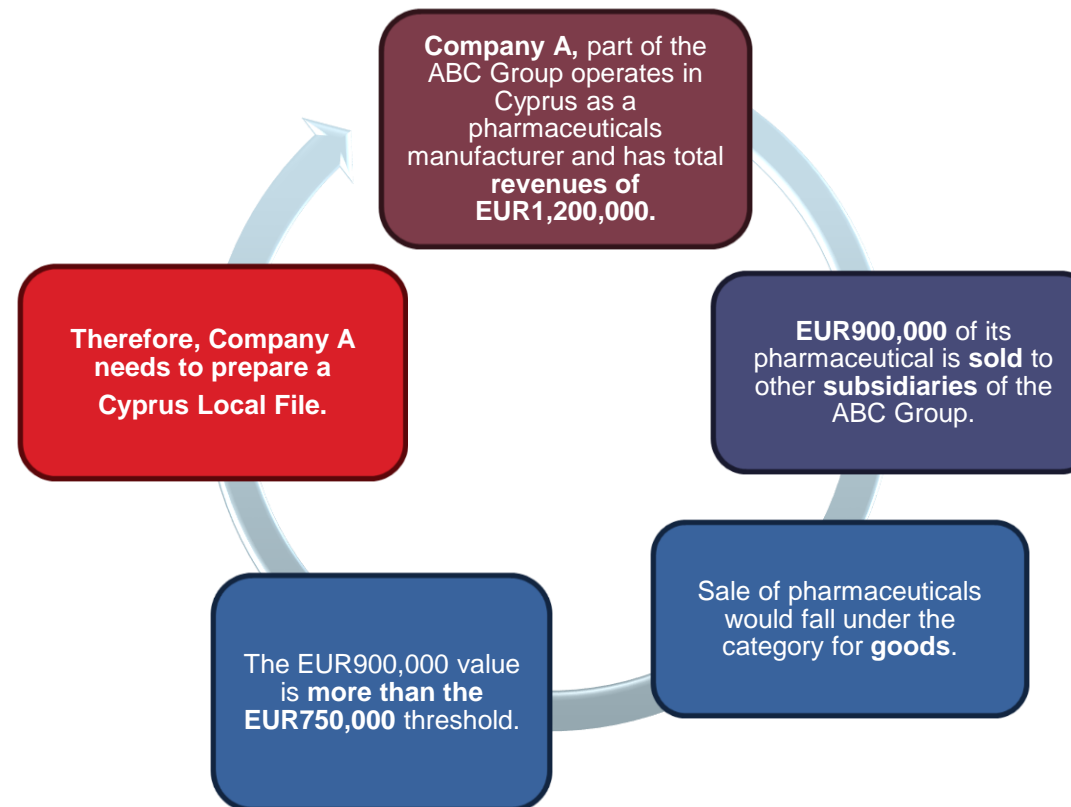
1. Preparation of documentation as per A1 and A2 above.
2. For back-to-back loans the required **net** return (before tax) has been set at 2,5% on the average principal of the loan receivable during the year, including any accrued interest.
3. For loans/ arrangements financed out of equity/ own funds, the minimum return has been set as being equal to the 10-year government bond yield of the country of residence of the borrower plus 3,5% (before taxes). The return is calculated based on the average principal of the loan receivable during the year, including any accrued interest.

4. For financing arrangements in which the Cypriot entity is the borrower, and the funds have been used for business purposes, the maximum allowable borrowing cost will be calculated based on the 10-year government bond yield of Cyprus of the tax year under consideration, plus 1,5% (before taxes). The calculation will be based on the average principal of the loans during the year (plus any accrued interest).
5. For low value-added services, as these are defined in the circular and the TP guidelines as issued by OECD, a minimum return of Cost-Plus 5% will be accepted in the cases where the Cypriot entity is the provider of the services. In the cases where the Cypriot entity is the receiver of the services, then the Cost-Plus 5% will be the maximum expense to be allowed.

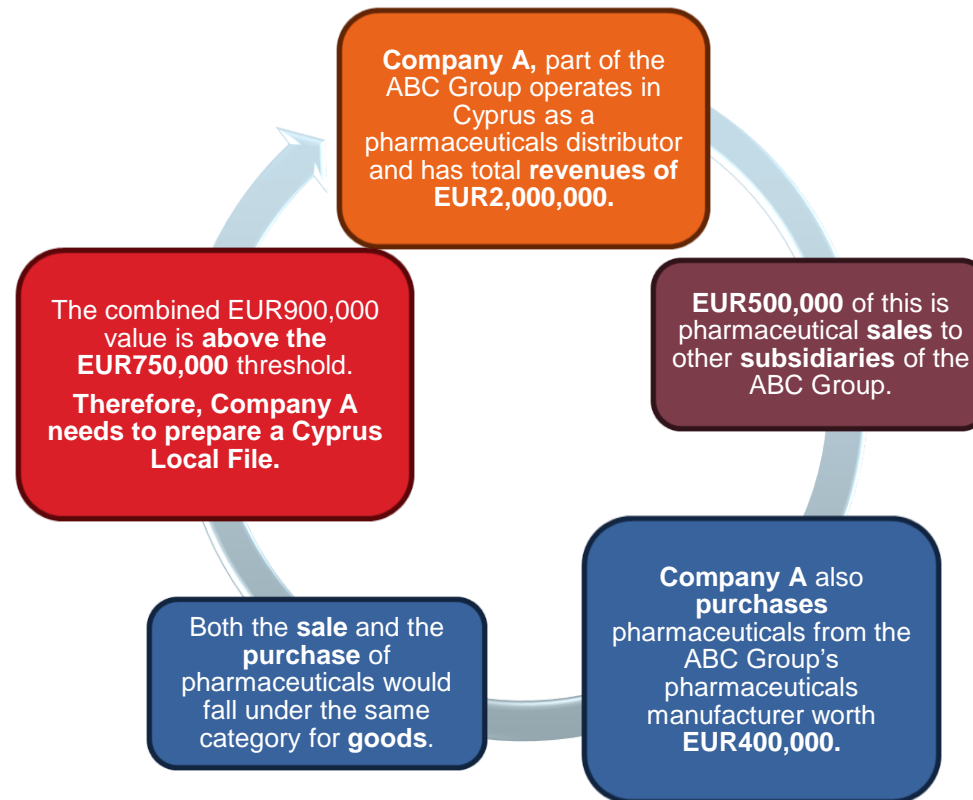
- Circular 7/2023
- As per Circular 7/2023 issued on 7 July 2023 effective from 2023 onwards:
  - Back-to-back financing arrangements:
    - In the cases where the entity under consideration undertakes the relevant risks and functions in the financing arrangement under review (in terms of equity and other factors), the only documentation method to be accepted for the purposes of TP will be the (Comparable Uncontrolled Price) CUP method and specifically interest rate benchmarking.

## Practical Scenarios

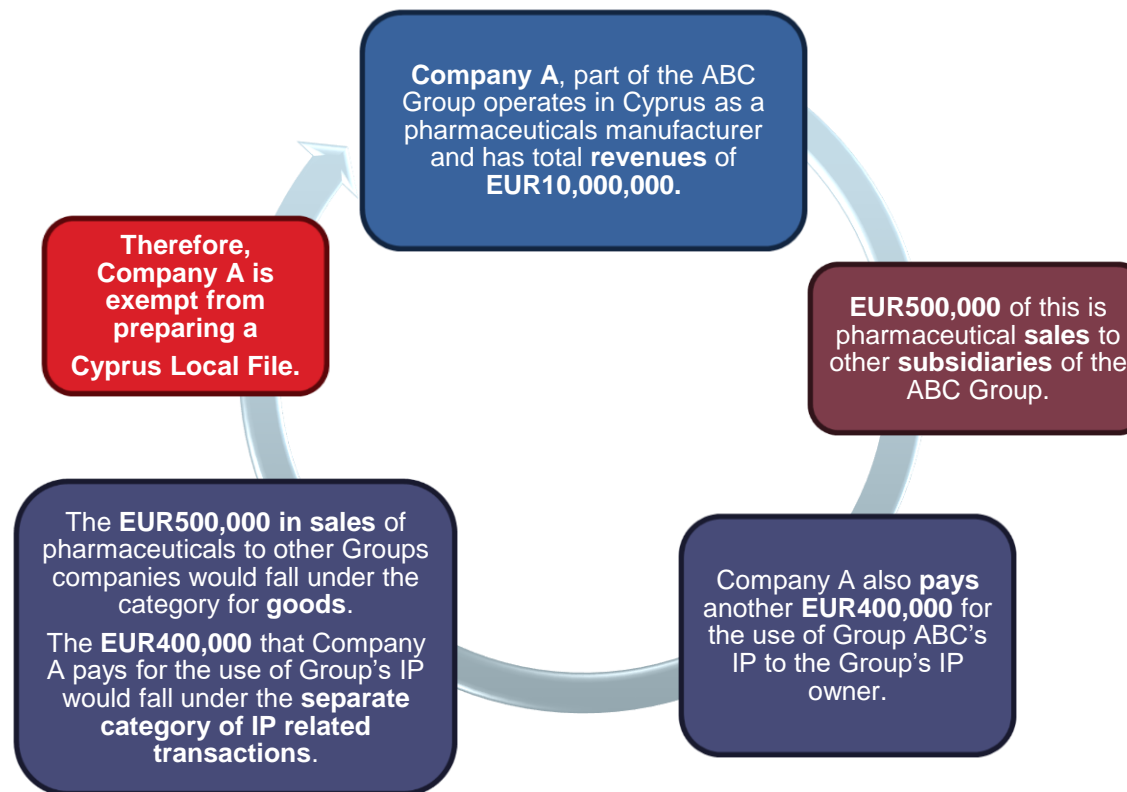
## Scenario 1: Is Company A obliged to prepare a Local File in Cyprus?



## Scenario 2: Is Company A obliged to prepare a Local File in Cyprus?



## Scenario 3: Is Company A obliged to prepare a Local File in Cyprus and for which transactions?





## Frequently Asked Questions

## Question 1

If the controlled transactions in category "A" cumulatively exceed €750,000 or shall exceed €750,000 on the basis of the arm's-length principle as described in article 33(9)(a) of the Income Tax Law (ITL), and at the same time the controlled transactions in category "B" cumulatively do not exceed the €750,000 threshold in a tax year, is there an obligation to include the controlled transactions of category "B" in the Cyprus Local File?

- No, there is no obligation to include category "B" controlled transactions in the Cyprus Local File.
- Only, the controlled transactions of a category which cumulatively exceed or shall exceed €750,000 on the basis of the arm's-length principle during a tax year must be documented and analyzed in the Cyprus Local File.
- In this specific example, it would be category "A" controlled transactions only.

## Question 2

How is the €750,000 threshold determined in the context of rental income activities during each tax year?

- The threshold is determined by reference to the total rental income on the basis of the arm's-length principle in a tax year.

## Question 3

Do purchases and sales need to be aggregated for the purposes of assessing whether the threshold has been exceeded?

Yes, the threshold refers to the absolute values of the controlled transactions for each category occurring in a tax year. For example, if total purchases and total sales amount to €400,000 and €500,000, respectively, the cumulative amount in this category is €900,000. Therefore, the threshold in this category has been exceeded.

## Question 4

Are the Cyprus Local File and Summary Information Table prepared using the tax year or the accounting year of the company?

The Cyprus Local File and Summary Information Table are prepared with respect to the tax year.

## Question 5

Under which category of the Summary Information Table should financial guarantees be reported?  
Financial guarantees should be reported under the category "Financial Transactions."

## Question 6

Should a benchmarking study be prepared every tax year, or only if something changes with regards to the intra group loans?

A benchmarking study should be prepared when an intra group loan is initiated, and updated when:

- New loans are provided or received by the company; or
- Significant terms of the existing loans change or are amended; or
- The functional profile of the company changes; or
- The market and economic conditions change significantly (if applicable).

The above list is indicative and not exhaustive. Further guidance is provided in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.

Please note that in accordance with article 33(10) of the ITR, the master file (where applicable) and the local file must be updated every tax year.

## Question 7

Who is responsible for the completion and submission of the summary information table?  
It is the responsibility of the taxpayer to complete the Summary Information Table.

The Summary Information Table is to be submitted by the statutory auditor or tax consultant.

## Question 8

Is the circular dated 30 June 2017 with title "Tax treatment of intra group back-to-back financing transactions" still applicable following the enactment of the new TP legislation and regulations?

The back-to-back circular was revoked as from 1 January 2022.

## Question 9

How is the €750.000 threshold in the context of loan financing activities being determined in a tax year?

- The threshold in the category of loan financing transactions is determined only by reference to the loan principal including interest charged but not paid.

## Question 10

Continuing from question 9 above, which balance is relevant in the case of loan financing activities (e.g. year end, average balance for the year, facility amount)?

- The maximum loan balance (i.e. only the loan principal including interest charged but not paid) during the tax year should be used to determine the threshold in the respective tax year and be reported in the Summary Information Table.

## Question 11

- Should the loans or any other monetary facilities including cash withdrawals (but excluding any balances arising from commercial transactions) granted by companies to the persons described in article 5(1)(z) & 5(2)(z) of the Income Tax Law L. 118 (I)/ 2002 be taken into account for the purposes of assessing whether the threshold of €750.000 has been exceeded in the category of financing activities?
- No, provided the company which is granting the loans or any other monetary facilities including cash withdrawals to its directors or to its shareholders who are individuals or their spouses or to their relatives up to and including the second degree of kinship *does not have as a taxable activity the provision of financing*.
- In this specific case only, such balances should not be taken into account for the purposes of assessing whether the threshold of €750.000 has been exceeded in the category of financing activities and as such should not be reported in the Summary Information Table. No documentation with respect to these specific transactions in the local file is required.

## Question 12

Company A borrows from a related Company B or a related individual B, the amount of €1.000.000 to buy shares of the same amount.

The shares with acquisition cost of the amount of €1.000.000 fall under the definition of “titles” as per article 2 of the Income Tax Law L. 118 (I)/ 2002 and circular 2008/13.

Should the transaction as described above:

12.1 be documented in the Cyprus local file?

12.2 be excluded from the Summary Information Table?

- In the case of Company A only (i.e. the Borrower), the transaction shall not be documented in the Cyprus local file and it shall be excluded from the Summary Information Table to the extent that the interest incurred does not constitute a tax-deductible expense in accordance to the provisions of articles 11(15) and 11(16) of the Income Tax Law L. 118 (I)/ 2002 and any other related Tax Circular that is in force.



## Question 13

A taxpayer has controlled transactions in Category “A” which cumulatively exceed €750.000 in a tax year, or should exceed €750.000 on the basis of the arm’s length principle as stipulated in article 33(9)(a) of the Income Tax Law L. 118(I)/2002, as amended, such that the said transactions in Category “A” need to be documented in a local file and at the same time the taxpayer in that tax year has controlled transactions in category “B” which cumulatively do not exceed or should not exceed the €750.000 threshold on the basis of the arm’s length principle.

### Does Circular 06/2023 apply to the Transactions in Category “B” in that tax year?

- Yes, Circular 06/2023 is applicable to the transactions in Category “B” in that tax year and thus the taxpayer should either:
  - a) prepare simplified transfer pricing documentation with the contents as described in the Circular 06/2023 or
  - b) opt for a safe harbour and maintain the prescribed supporting documentation in respect of the use of the safe harbour provided that the controlled transactions in Category “B” belong to one of the subcategories of transactions for which a safe harbour is available under the circumstances permitted in the Circular 06/2023.

## Question 14

Do all persons as defined in article 33(7) of the ITL need to complete the Summary Information Table of Controlled Transactions and submit it electronically every tax year together with the Income Tax Return as per article 33(10) of the ITL?

- Yes.
- All persons as defined in article 33(7) of the Income Tax Law need to complete and submit the Summary Information Table of Controlled Transactions as long as controlled transaction(s) arise within a tax year and irrespective of the value of the said controlled transaction(s).

## Illustrative example of SIT and Local File threshold

TIC	Counterparty Name	Tax Jurisdiction	Goods (€)		Services (€)		Financing (€)	
			Income	Expense	Income	Expense	Receive (Loan Principal)	Provide (Loan Principal)
U1	ABC Ltd	Ukraine	300,000	500,000	100,000		100,000	300,000
R1	XYZ Ltd	Russia				200,000	750,000	
C1	DIY Ltd	Cyprus				50,000		200,000
<b>Total Amount</b>			300,000	500,000	100,000	250,000	850,000	500,000
<b>Aggregate Amount per Category</b>			800,000		350,000		1,350,000	
<b>Local File Requirement?</b>			Yes		No		Yes	

# **Advance Pricing Arrangements**

## Advance Pricing Agreements (APA)

A voluntary agreement between the taxpayer and one or more tax authorities that allows the parties to **agree in advance** on the transfer pricing methodology for any given intercompany transaction for a specific timeframe.

### There are three types of agreements:

1. Unilateral
  2. Bilateral
  3. Multilateral
- The agreements are valid for period of up to **four years**
  - Tax commissioners should accept or reject the agreement request **within 10 months** of submission (extendable up to 24 months upon notification)
  - Mechanisms with respect to the amendment, cancellation or revocation of an APA subject to conditions
  - APA may be revised either via taxpayer or Commissioner, e.g., in case critical assumption prove to be erroneous or material change in circumstances
  - APA may be revoked or cancelled, e.g., in case assumptions prove to be erroneous or taxpayer failed to comply with fundamental condition/obligation

## Questions

Thank you.

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