Cyprus | Tax & Legal Services | 16 June 2020 Issue 14/2020

Cyprus Tax News

Amendments to the Notional Interest Deduction (NID) provisions of the Income Tax Law

On 16 June 2020, an amending Income Tax Law (ITL) was published in the Official Gazette with respect to the Notional Interest Deduction (NID).

The revised NID provisions enhance the tax benefits for Cyprus companies financing their operations through new equity, are in line with the recommendations of the European Commission, and offer additional clarity for taxpayers.

RECAP OF THE NID

As from 1 January 2015, Cyprus tax resident companies and Cyprus permanent establishments that employ "new equity" in the production of taxable income are entitled to deduct from their taxable profits, a notional interest deduction.

In brief, the NID is equal to the amount of the new equity multiplied by the relevant "reference rate," and is subject to an annual cap of 80% of the taxable profits (as calculated prior to the NID) arising from the new equity.

NID = New equity x Reference rate (capped at 80% of taxable profit)

KEY AMENDMENTS

- **Reference rate**

  Until 31 December 2019 (pre-amendment)

  The reference rate is the yield of the 10-year government bond (as at 31 December of the year preceding the tax year the NID is claimed) of the country in which the new equity is employed/invested **plus 3%.** The **minimum reference rate** is the yield of the Cyprus 10-year government bond (as at 31 December of the relevant year) plus 3%.

From 1 January 2020 (post amendment)

The reference rate is the yield of the 10-year government bond (as at 31 December of the year preceding the tax year the NID is claimed) of the country where the new equity is employed/invested **plus 5%,** and there is **no minimum reference rate.**

Where the country in which the new equity is employed/invested does not have an issued 10-year government bond as at 31 December of the relevant year, the reference rate is the Cyprus 10-year government bond yield plus 5%.

- **New equity**

  Until 31 December 2020 (pre-amendment)

  "New equity" represents equity introduced into the business on or after 1 January 2015, excluding equity created from the capitalisation of reserves existing on 31 December 2014 (pre-existing reserves), **unless** the equity created from the pre-existing reserves is invested in (business) assets earning taxable income which did not exist on 31 December 2014.

  From 1 January 2021 (post amendment)

  "New equity" is defined as equity introduced into the business on or after 1 January 2015. Therefore, as from 1 January 2021, **the NID can no longer be claimed on equity arising from the capitalisation of pre-existing reserves.**

- **NID cap (80% of taxable profits)**

  Clarification

  The amending law clarifies that for the purposes of calculating the NID cap, the relevant taxable profits are those arising from the employment of the new equity, so that the NID can only be claimed against such profits. It also clarifies that the cap applies separately to the taxable profits derived from each business asset that is financed by the new equity.

  Although the provisions of the law prior to the amendment were not as clear as to the calculation of the cap, the methodology described in the amending law (and the relevant Circular) was generally followed in practice and, therefore, the amendment relating to the NID cap applies retroactively as from 1 January 2015.

How can we help?

We are at your disposal to discuss the above amendments with you and to assess their impact on the provisional corporate income tax calculations for 2020 considering the upcoming deadline (31 July 2020) for the payment of the first provisional tax instalment.

In addition, companies that did not cap their annual NID claim, using the 'matching' concept, would need to consider how the amending law may impact their tax position in prior years.

Get in touch

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