



Tax-Free Reorganisations in Cyprus

Introduction

Companies and corporate groups have traditionally undertaken reorganisations to address business challenges and achieve strategic objectives. Corporate reorganisations enable companies to adapt to changing markets, streamline business operations and processes, improve operational efficiency and reduce costs, and in general align their structure with strategic objectives. In addition, they may be necessary while exploring new opportunities and can be a tool to facilitate expansion in a constantly evolving business environment.

The case for group reorganisations is strong as it has been proven throughout the years that successful reorganisations can have positive long-term effect on profitability and drive long-term success.

In Cyprus, reorganisations occur frequently across all sectors and industries and are usually driven by various factors including group strategy, market conditions and regulatory changes.

To help companies or corporate groups thrive in a competitive and ever-changing business environment, it is important to enable them to reorganise in a tax-efficient manner.

EU Mergers Directive and transposition into domestic law

In 1990, the European Union adopted the so-called Mergers Directive (90/424/EEC) on a common system of taxation applicable to qualifying reorganisations, which was further improved in 2005 through amending Council Directive 2005/19/EEC. The EU Council of Ministers codified in a single text all Council Directives governing this matter through the adoption of [Council Directive 2009/133/EEC](#). The objective of the Mergers Directive is to remove fiscal obstacles to cross-border reorganisations.

Cyprus transposed the Mergers Directive into domestic law in December 2006, effective from 1 January 2007, specifically under Articles 26-30 of the [Income Tax Law](#) (“ITL”) which do not only cover cross-border reorganisations but also domestic ones. Relevant provisions were also introduced in other Cypriot laws. It is important to note that the Companies Law (Cap 113) includes provisions enabling companies and corporate groups to undertake reorganisations.

In essence, qualifying reorganisations are exempt from most Cyprus taxes, including the following:

- Corporate Income Tax
- Capital Gains Tax
- Special Defence Contribution
- Stamp Duty
- Land Registry Transfer Fees

Although respective provisions have not been introduced in the Cypriot VAT Law, qualifying reorganisations are often exempt from VAT, for example when the reorganisation involves the transfer of a business as a going concern.

Types of qualifying reorganisations

Qualifying reorganisations include mergers, divisions, partial divisions, transfer of assets and exchange of shares as well as the transfer of the registered office of a European Company (SE). The relevant definitions for each type of reorganisation are included in [Article 30](#) of the ITL and are reproduced below:

1) Merger

- (i) One or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to another existing company in exchange for the issue to their shareholders, of shares representing the capital of that other company, and, if applicable, a cash payment not exceeding 10% of the nominal value of those shares or, in the absence of a nominal value, of the accounting value of those shares.

- (ii) Two or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to a new company that they form, in exchange for the issue to their shareholders, of shares representing the capital of that new company, and, if applicable, a cash payment not exceeding 10% of the nominal value of those shares or, in the absence of a nominal value, of the accounting value of those shares.
- (iii) A company, on being dissolved without going into liquidation, transfers all its assets and liabilities to the company holding all the shares representing its capital.

2) *Division*

A company, on being dissolved without going into liquidation, transfers all its assets and liabilities, to two or more existing or new companies, in exchange for the pro rata issue to its shareholders, of shares representing the capital of the companies receiving the assets and liabilities, and, if applicable, a cash payment not exceeding 10% of the nominal value of those shares or, in the absence of a nominal value, of the accounting value of those shares.

3) *Partial Division*

A company transfers, without being dissolved, one or more branches of activity, to one or more existing or new companies, leaving at least one branch of activity in the transferring company, in exchange for the pro rata issue to its shareholders of securities representing the capital of the companies receiving the assets and liabilities, and, if applicable, a cash payment not exceeding 10% of the nominal value of those securities or, in the absence of a nominal value, of the accounting value of those shares.

The term 'branch of activity' means all the assets and liabilities of a division of a company which, from an organizational point of view constitute an independent business, that is to say an entity capable of functioning by its own means.

4) *Transfer of Assets*

A company transfers, without being dissolved, all or one or more branches of activity, to another company in exchange for shares representing the capital of the transferee company.

5) *Exchange of Shares*

A company acquires a holding in the capital of another company such that it obtains a majority of the voting rights in that company, or, having acquired such a majority, acquires a further holding, in

exchange for the issue to the shareholders of the latter company, in exchange for their shares, of shares representing the capital of the former company, and, if applicable, a cash payment not exceeding 10% of the nominal value of those shares or, in the absence of a nominal value, of the accounting value of those shares.

6) *Transfer of Registered Office*

A European company (SE) or a European Co-operative company (SCE), without being dissolved or incorporating a new legal person, transfers its registered office from one Member State to another Member State.

Main provisions

The main provisions included in the ITL (Articles 26-27) with respect to qualifying reorganisations are the following:

- Any assets and liabilities, including provisions and reserves, transferred as part of a qualifying reorganisation do not give rise to taxable profits.
- The receiving company shall compute tax depreciation as well as any profits or losses in respect of the assets, liabilities, provisions and reserves transferred, according to the conditions that would have applied to the transferring company or companies, had the reorganisation not taken place. On this basis, with respect to capital allowances, no balancing statement should be prepared for the purposes of the tax computation of the transferring company and the transferee company shall continue to claim capital allowances on the assets received as if the reorganisation had not taken place.
- Any accumulated tax losses of the transferring company can be transferred to the receiving company and the receiving company shall utilise such losses having regard to the relevant provisions of the ITL for the set off and carry forward of tax losses.

Anti-Avoidance Rules

[Article 29A](#) of the ITL includes anti-avoidance provisions in relation to qualifying reorganisations.

For a reorganisation to qualify as tax-free, the Cyprus Tax Authorities (“CTA”) must be satisfied that the reorganisation has genuine commercial and economic purpose. The CTA may not grant the tax exemption of the profits realised due to the reorganisation if they consider that the main purpose or one of the main purposes of the reorganisation was to avoid, reduce or defer the payment of tax or the direct or indirect distribution of assets of any company to any person without paying, or reducing or deferring the payment of tax.

Additionally, when granting the exemption, the CTA may impose certain conditions in relation to the number of shares to be issued under the reorganisation and the period during which the shares issued as part of the reorganisation must be held by the recipient, which may not exceed three years. If the conditions imposed by the CTA are not complied with, any tax not imposed due to the reorganisation becomes immediately payable.

Process of Obtaining Confirmation

Although the ITL does not include a requirement to obtain the official confirmation of the CTA with respect to a qualifying reorganisation, in accordance with [Circular 2008/12](#), in order for the CTA to examine whether the reorganisation qualifies as tax-free, Form T.D.88 along with relevant supporting documentation should be submitted to the CTA.

In many cases a reorganisation would need to be sanctioned by a court, especially where the reorganisation involves dissolution of companies or where creditors' interests need to be safeguarded. It is mandatory to submit the respective court order to the CTA in cases of mergers or divisions.

As part of the examination of the reorganisation, the CTA will also examine the tax filings of the Cyprus companies involved. Once the examination is completed, the CTA issue the respective confirmation which states that the reorganisation was undertaken in accordance with the provisions of the ITL and therefore qualifies as tax-free.

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