

Cyprus Tax Alert

Limassol, 11th September 2018

NON-RETURN CAPITAL CONTRIBUTIONS

The Commissioner of Taxation has issued Circular 25, dated 3 September 2018, in which clarifications on the tax treatment for non return capital contributions **without the issue of shares** to non Cyprus tax resident legal entities are given.

Non application of Article 33 of Income tax Legislation

Article 33 (on Related Party Transactions) of the Income Tax legislation refers to transactions between related parties being at an arm's length.

As regards the non-return capital contributions without the issue of shares, application of the Article 33 may lead to imposition of notional interest on debit balances from related companies.

The Circular clearly states that Article 33 does not apply on non-return capital contributions when all the following conditions are met:

- The contributing party does not have a legal right to claim repayment of the contribution at any given time
- Any repayment of the capital contribution is only effected as a result of reduction of capital or dissolution/liquidation of the recipient company. Kindly note that where applicable legislation in the country of the recipient does not constitute obligatory the reduction of capital to repay the contribution, such a requirement is waived, with the production of supporting documentation.
- Any repayment of the capital contribution can not be effected within a period of two years after the year end in the year it was contributed
- The contributing party has a direct shareholding in the recipient's capital
- The recipient company is not benefited out of notional tax deductions out of the non-return capital contribution

Application of Articles 9 and 11 of Income tax Legislation

If all the above conditions are met, then the non-return capital contributions are considered as non-business assets for the purposes of the above articles. They will be considered as investments.

Hence, the cost of the non-return capital contribution will be considered for the restriction of administration and financial expenses and interest expenses.

Any direct expenses related to the non-return capital contribution are not tax deductible.

Effective date

The Circular applies for all non-return capital contributions to non Cyprus tax resident legal entities in existence as at 1 January 2017 and onwards.

Any previous tax rulings on this subject with conditions other than the ones described by the Circular become void as from 1 January 2017.

In case of any further clarification please do not hesitate to contact us.

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