



# TALIADOROS AUDIT FIRM

CHARTERED CERTIFIED ACCOUNTANTS

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## Notional Interest Deduction

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## Notional Interest Deduction (NID)

Further to the article 9B of the Income Tax Law 118(1)/2002, as amended by Law 116 (1) 2015, and which is applicable from 1 January 2015 a tax deduction is allowed following the application of the NID to the amount of new equity injected to Cyprus tax resident companies and used for business purposes.

The Cyprus Tax Department has published a number of clarifications on the application of NID, through its Circular 2016/10, dated 18 July 2016.

### Main provisions of the Law

- i. A deduction (NID) is allowed against the taxable income of:
  - A company tax resident in Cyprus, or
  - A company not tax resident in Cyprus but with a permanent establishment in Cyprus, or
  - A company which changes its tax residency to Cyprus on or after 1 January 2015 (but not necessarily redomiciling to Cyprus)
- ii. The NID is allowed against the taxable income for that specific year and is equal to= **reference interest rate X new equity**
  - **reference interest rate** is the higher of the following two yields which existed as at 31 December of the previous tax year:
    - a) yield of the 10-year government bond of the state in which the new equity is invested in, increased by 3%
    - b) yield of the 10-year government bond of the Cyprus Government, increased by 3%
  - **new equity** is the equity that has been introduced in the business on or after 1/1/2015

The NID is granted for that period within the year during which the new equity belongs to the business

According to Circular 2016/10 the term **new equity** also includes:

- Unpaid share capital on which actual or deemed interest is imposed subject to corporation tax is considered as new equity which has been fully paid for the purposes of the Circular
- Issue of shares relating to the capitalization of realizable reserves which were created after 1/1/2015
- Issue of shares relating to the capitalization of realizable reserves which existed on 31/12/2014 and that can be proved that those are associated to assets generating taxable income
- Capitalization of loans payable, shareholders credit balances, or other liabilities through the issue of shares
- Issue of shares relating to a non-reciprocal capital contribution.
- New equity relating to a Cyprus permanent establishment represents the average balance for the finance of the permanent establishment's operations for the specific tax year and does not include any balances between the head office and the permanent establishment which were incurred from trading or temporary financial transactions.

- iii. The **reference interest rate** cannot be less than the yield of the 10-year Cyprus government bond as at the 31 December of the previous tax year, increased by 3%
- iv. The **new equity** does not include amounts that have been capitalized and derived from the revaluation of movable or immovable property
- v. **Old equity** takes the meaning of equity that existed as at 31/12/2014
- vi. In case of companies changing their tax residency to Cyprus, **new equity** includes the equity of those companies before the change of tax residency
- vii. The amount of NID cannot exceed 80% of taxable income before allowing for the NID
- viii. In the case of a taxable loss in a tax year then no amount of NID is allowed to be deducted

#### **Anti-abuse provisions**

The Commissioner may not allow the granting of any NID in the case where, based on his judgement:

- Actions or transactions have taken place without substantial economic or commercial purpose which aim for the claim of NID or
- the **new equity** on which the NID is claimed emanate from equity that existed before 1/1/2015 but presented as new equity through actions or transactions between related parties with the main purpose being the claim of the NID

In the case where **new equity** is introduced in the form of **in-kind contribution of assets**, then:

- the amount of this equity, for the purposes of granting of the NID, cannot be more than market value of these assets on the date they were introduced in the business, and
- no NID is allowed if the market value of these assets is not substantiated to the judgement of the Commissioner

***We remain at your disposal should you require any information of clarification on the above.***