



Cyprus releases long-awaited Transfer Pricing guidelines on intra-group financing

As of 1 July 2017, the tax treatment of intra-group financing arrangements has been amended in Cyprus. Intra-group financing transactions refers to finance activities between related parties (as defined in Section 33 of the Income Tax Law), including permanent establishments in Cyprus. Based on the Interpretative Circular issued by the Cyprus Tax Department, intra-group financing arrangements must be taxed from 1 July 2017 onwards under the arm's length principals (transfer pricing rules).

For the purposes of the transactions under the scope of the Circular issued, it must be determined for each intra-group transaction whether it complies with the arm's length principles. A comparability analysis must be performed to determine whether the transaction between independent entities is comparable to transactions between related entities.

The comparability analysis mentioned above should consist of the two following parts:

- Identification of the commercial financial relationship between entities and determining the conditions and economically relevant circumstances attached to those relations to accurately delineate the controlled transaction
- Comparison of the accurately delineated conditions and economically relevant circumstances of the controlled transaction with those of the comparable transactions between independent entities

It should be noted that the group financing company should be controlling the risk if it has the decision-making power to enter a risk-bearing commercial relationship. To justify the risk control and further validate that the management and control are exercised in Cyprus, it is essential that the group financing company has an actual presence in Cyprus.

In case of companies with a profile comparable to the entities subject to Regulation (EU) No 5/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) NO 64/2012, a return on equity of 10% after-tax can be observed in the market and be considered as reflecting arm's length remuneration for the financing and treasure functions in question.

Simplified procedures exist, per which the transactions of financing companies pursuing a purely intermediary activity are deemed to comply with the arm's length principle if the company under review receives a minimum return of 2% after tax on assets. To benefit from this simplification measure, the use of it should be communicated to the Tax Department.

The above-mentioned percentages are valid as of the date of issuance of the Circular and will be reviewed by the Tax Department based on relevant market analysis and – if required - will be changed accordingly.

Minimum requirements for the transfer pricing analysis exist and are necessary for the analysis to be in compliance with the principles of the new circular.



Finally, any tax rulings relating to the matters of the Circular which were issued prior to 1 July 2017 will no longer be considered valid.

The above changes will have an immediate impact on all Cyprus financing companies with intra-group financing transactions and it is imperative that such structures are examined to ensure that their tax treatment is correct and their tax risk exposure is mitigated.

Our transfer pricing team of professionals can assist you in evaluating the tax implication of the above changes on your structures.

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