CYPRUS

Overview

STI Taxand, Taxand Cyprus

STI Taxand is a tax law firm offering comprehensive legal services focused on taxation matters. This includes advising clients on tax planning, compliance, and disputes. Services cover income tax, corporate tax, international taxation, tax treaties, transfer pricing, Pillar Two and assistance with audits. Expertise in navigating complex tax codes and providing strategic counsel to minimise liabilities is a key aspect of our offerings. We also represent clients in negotiations with tax authorities and handle litigation if disputes arise.

With respect to transfer pricing, we provide guidance on pricing policies, documentation, and compliance. We assist in developing and implementing strategies that align with regulatory requirements, mitigate risks, and optimise tax positions. This includes preparing transfer pricing documentation, conducting benchmarking analyses, planning and strategy, and supporting clients in transfer pricing audits and disputes. More specifically:

- Intra-Group Services Pricing: Advising on the pricing of services provided by one entity to another within the same group.
- Financial Transactions Transfer Pricing: Analysing and advising on the transfer pricing implications of financial transactions, including intercompany loans, cash pooling and guarantees.
- Intellectual Property Valuations: Assessing the value of intellectual property for accurate pricing.
- Business Restructuring: Providing guidance on transfer pricing considerations during business restructuring, including the transfer of functions, risks, and assets among group entities.
- Assistance in Tax Controversy Matters: Supporting multinational enterprises in tax disputes, including obtaining Advance Pricing Agreements ("APAs") and Mutual Agreement Procedure ("MAP") agreements.

General: Transfer Pricing Framework

With effect from 1 January 2003, article 33 of the Income Tax Law of 2002, N118(I), as amended ("ITL"), incorporates the arm's length principle ("ALP") and is in line with Article 9 of the OECD Model. Further, with effect from 1 January 2022, ITL provides for specific documentation requirements that generally follow Chapter V of the OECD Transfer Pricing Guidelines ("OECD Guidelines") for all Cypriot taxpayers entering into controlled transactions unless such taxpayers fall under a de minimis threshold. It should be noted that the OECD Guidelines are specifically incorporated in the ITL; therefore, the transfer pricing rules and arm's length principle are generally in line with the OECD Guidelines. The phrase controlled transactions refers to transactions between associated persons (entities or individuals), who, in a broad context, have a direct or indirect relationship of 25% or more.

Accepted Transfer Pricing Methodologies

Given that the OECD Guidelines have been legislatively incorporated into the ITL, all transfer pricing methods approved by the OECD should be equally applicable.

Considering that the ITL does not provide for a hierarchy between the 5 OECD-approved methods, the guidance provided in the OECD Guidelines with respect to the selection of the most appropriate transfer pricing method to the circumstances of the case should be followed. Notably, Cypriot taxpayers should provide justification for why the selected method is deemed suitable, taking into account the pertinent facts and circumstances. Generally speaking, the Cyprus Tax Department ("CTD") favours the CUP method, however, due to challenges in finding comparable uncontrolled transactions, in practice, the TNMM has become the most widely used transfer pricing method.

Transfer Pricing Documentation Requirements

The CTD requires taxpayers to be able to substantiate all related party/intercompany transactions in transfer pricing documentation. Yet, according to the ITL Cypriot taxpayers involved in controlled transactions with an arm's length value in aggregate more than EUR 750,000 annually in each of the following five transaction categories (as defined in the summary information table) are required to prepare a Cyprus local file:

1) sale/purchase of goods;
2) provision/receipt of services;
3) financing transactions;
4) receipt/payment of IP licensing/royalties; and
5) others.

It is important to note that an announcement published on 1 February 2024 by the Ministry of Finance, together with the CTD, has set the arm's length thresholds at EUR 5,000,000 for intragroup financing transactions and EUR 1,000,000 for all other transaction categories. These thresholds are applied retroactively, effective from 1 January 2022.

Therefore, all Cypriot taxpayers who are involved in controlled transactions should prepare a local file unless they fall in the above small size exemption. The content of the local file is generally aligned with Chapter V of the OECD Guidelines. It should be noted that a person holding a practising certificate from ICPAC or any other recognised institute of certified accountants in Cyprus should conduct a Quality Assurance Review for the local file. Further, the local file should be prepared by the deadline for submitting the Income Tax Return for the relevant tax year. Following the preparation deadline, the taxpayer must provide and submit the local file to the tax authorities within 60 days upon request. Under the Assessment and Collection of Taxes Law (1978, 4/78), as amended ("ACTL"), failure to submit the local file after receiving a request from the CTD will result in penalties ranging from EUR 5,000 to EUR 20,000. Finally, Cypriot taxpayers must also file the summary information table ("SIT") by the submission deadline of the tax return of the specific year of assessment. Failure to submit the SIT, a penalty of EUR 500 will apply.

With respect to the master file, the obligation to prepare and maintain a master file applies exclusively to Cypriot taxpayers who serve as the ultimate parent or surrogate parent entity for an MNE group subject to Country-by-Country reporting. All other entities are exempt from this requirement. Like with the local file, the content of the master file is generally aligned with Chapter V of the OECD Guidelines and the taxpayer must provide and submit the master file to the tax authorities within 60 days upon request. Failure to submit the master file after receiving a request from the CTD will result in penalties ranging from EUR 5,000 to EUR 20,000.

Local Jurisdiction Benchmarks

The CTA considers local and pan-European benchmarks acceptable, given that they adhere to comparable search strategy standards of the OECD Guidelines. Generally, the CTA relies on contemporaneous and multiple-year data and uses the interquartile range for benchmarking. Importantly, the ITL provides that the local file should be updated on a yearly basis, and any significant changes in the market conditions that may impact the information and data should be documented in the local file.

Advance Pricing Agreement "APA"/Bilateral Advance Pricing Agreement "BAPA" Overview

Cypriot taxpayers have the option to present APAs to the CTD to pre-determine pricing methodologies. These APAs can be applied unilaterally, bilaterally, or multilaterally and remain valid for a duration of up to four years.

Transfer Pricing Audits

Random transfer pricing audits can be conducted by the CTD and all Cypriot taxpayers are subject to audit for any open tax year (the ordinary statute of limitation is six years). In identifying areas of interest, the SIT serves as a risk assessment tool for the CTD in selecting the taxpayers for transfer pricing audit. This is because the SIT includes various useful information, such as an overview of the controlled transactions, specifying the counterparties' identity, their tax residency jurisdiction, and describing the nature of the controlled transactions (i.e. services, intangible, financial transactions, sale of goods, and other). Additionally, the corresponding values of these controlled transactions should be explicitly stated. Hence, tax inspectors are inclined to incorporate the SIT into their criteria for selecting taxpayers for audits, recognizing the significant role these factors play in the selection process. Currently, there seems to be more attention on financial transactions, in particular to intra-group loans.

The Burden of Proof in Transfer Pricing: Theory versus Practice in Cyprus

Under Article 33 of the ITL, taxpayers are required to maintain transfer pricing documentation for transactions that fall under specified categories and exceed certain thresholds—or would have exceeded those thresholds if the transactions were conducted at arm's length. When taxpayers meet these documentation requirements, the burden of proof primarily rests with the tax authorities to demonstrate that the transactions are not conducted at arm's length.

However, if taxpayers fail to meet the minimum documentation requirements, the burden of proof shifts to them. In such cases, it becomes the taxpayer's responsibility to substantiate that the pricing of intragroup transactions adheres to the arm's length principle.

It is worth noting that the first deadline for preparing transfer pricing reports and submitting the Summary Information Table, under the ITL, is May 31, 2025. As a result, there have been relatively few transfer pricing disputes thus far. In time, we will see how the burden of proof evolves in practice and whether it aligns with the theoretical framework outlined by the law.

Additionally, Circular 6/2023, published on 6 July 2023, outlines the measures to be taken if transactions fall below the established thresholds, offering simplification options. The circular specifies that, even for transactions below the threshold, taxpayers should either maintain simplified documentation to demonstrate arm's length pricing or apply the safe harbour rules. This further underscores that, under Cyprus' legal framework, the burden of proof lies with the taxpayer.

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Transfer Pricing Penalties

In addition to the penalties noted above, the ACTL outlines penalties for any additional taxes resulting from transfer pricing adjustments. Specifically, if the temporary income declared (including any revised estimated returns) is lower than 75% of the income as finally determined and shown in the tax return filed by the taxpayer or amended by the CTD by issuing additional assessment, in addition to the balance of the tax due an additional amount of tax equal to 10% is also payable. Further, interest is imposed where the tax due is not paid by the prescribed dates, either when the payment is made under a self-assessment or when the payment is made on the basis of an assessment raised by the Tax Commissioner. Finally, in case a person fails to pay the tax due by the due date or within the period prescribed by a notice issued by the Tax Commissioner, there is a penalty equal to 5% of the tax due.

Local Hot Topics and Recent Updates

In Cyprus, it seems that the CTA has focused strongly on financial transactions and the application of arm-length interest rates over the last few years. Nevertheless, considering the implementation of the new documentation requirements and the annual submission of the SIT, it is anticipated that the scope of transfer pricing audits will extend to encompass additional controlled transactions.

Documentation threshold

Master file	Consolidated revenue exceeding EUR 750 million
Local file	Cumulatively, per category (as defined in the SIT) exceeds the arm's length amount of EUR 5,000,000 for intragroup financing transactions and EUR 1,000,000 for all other transaction categories. per tax year.
CbCR	Consolidated revenue exceeding EUR 750 million

Submission deadline

Master file	To be submitted to the CTD upon request within 60 days.
Local file	Local file To be submitted to the CTD upon request within 60 days. Further, the local file should be readied by the deadline for submitting the Income Tax Return for the relevant tax year.
CbCR	Submission to the CTD must occur within 12 months following the conclusion of the MNE group's reporting fiscal year.

Penalty Provisions

Local file and master file	Ranging from EUR 5,000 to EUR 20,000
Tax return disclosure – late/incomplete/no filing	EUR 100 and penalties imposed under ACTL noted above.
CbCR – late/incomplete/no filing	Ranging from EUR 500 to EUR 20,000
SIT	EUR 500 for late submission

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