

Corporate Tax - Cyprus

Department clarifies five-year restriction on carry-forward of losses

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Introduction

On May 30 2013 the Inland Revenue Department issued Circular 2013/8 clarifying the practical application of the new five-year limit for carrying forward losses for relief against future profits. The limit was introduced by Article 13 of the Income Tax (Amendment) (No 2) Law 188(I)/2012, which entered into force on December 21 2012.

Before that date, tax losses could be carried forward indefinitely for relief against future taxable income (ie, income acquired from the ordinary activities of a company or from activities closely connected with the ordinary activities of the company).

For the 2012 tax year and subsequent years, the carry-forward period is limited to five years. Accordingly, only losses incurred in the 2007 tax year and later years are available for relief against taxable income for 2012. Relief is no longer available for unutilised losses relating to 2006 and earlier years.

Taxation on a temporary assessment basis

Under the Assessment and Collection of Taxes Law, companies must submit a provisional self-assessment of taxes for the current year by no later than July 31 and pay the estimated tax liability in instalments before the end of the year. Situations in which a company calculated the provisional tax payable for 2012 on the basis of the old rules (which were the rules in force at July 31 2012, the deadline for submission of provisional assessments) and consequently underpaid tax on the basis of the new rules (as a result of the non-availability of losses relating to 2006 and earlier tax years) are dealt with by Circular 2013/8. In general, the law provides for the imposition of a 10% surcharge on underestimations of the tax payable, but Circular 2013/8 stipulates that no surcharge will be imposed if the underestimation is the result of the inclusion in the provisional assessment of losses relating to 2006 or earlier years.

Losses of permanent establishment overseas

The five-year limit also applies to the carry-forward of losses incurred by an overseas permanent establishment. Article 36(3) of the Income Tax Law provides that the profits of an overseas permanent establishment are exempt from tax, but losses of an overseas permanent establishment may be offset first against profits from the same year derived from other overseas permanent establishments, and then against taxable income in the same year. Such losses are available for group relief. Any unrelieved losses can be carried forward to be offset in the same way.

However, if the overseas permanent establishment subsequently earns taxable income, the loss relief will be clawed back by adding the amount of loss relief obtained in previous years to taxable income for the current year. The circular makes it clear that this clawback applies only to relief that has been obtained, and does not extend to losses that have been claimed, but have not been offset due to the lapse of the five-year limitation period.

In contrast to Cyprus-resident trading companies, the 2012 amendment law has no implications for holding companies, which usually incur minor tax losses consisting of administration costs such as annual fees, audit and other expenses, but whose income in the form of dividends and profits from the disposal of securities is exempt from tax in Cyprus.

Group relief

Although they do not allow for losses to be carried forward to future accounting periods, the group relief rules in Cyprus are highly beneficial, allowing the tax losses of one company to be offset against the profits of others in the same group. Two companies are considered to be part of a group for group relief purposes if either is a 75% subsidiary of the other or both are 75% subsidiaries of a third company. Previously, group relief was available only if all relevant companies were members of the same group for the entire financial year for which tax relief was sought. With effect from January 1 2012, a subsidiary formed (but not one acquired) during a tax year is treated as a member of the group for the entire year, and is therefore eligible for group relief.

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