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TAX BRIEFING: Monthly Insight

Recent Developments in Tax Legislation

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A. Ministerial Circular POL. 1145/2018 Provides Clarifications on the Tax Treatment upon Capitalization of Tax Free Reserves

1. The Ministry of Finance provided clarifications with regard to capitalization of reserves formed under special tax incentive laws.

2. In particular, Article 353 of Law 4512/2018 introduced three new articles to the Income Tax Code (ITC - Law 4172/2013), namely Articles 71A, 71B and 71C, which incorporate into the ITC provisions from various existing laws.

3. Article 71A incorporates the provisions of Article 71 of Law 3842/2010 and provides for incentives related to the use of patents:

   a. Pursuant to this Article, the profits of a Company that uses internationally recognized patents, developed by and registered in its own name and for the production of its own products, may be exempted from income tax for three consecutive years, commencing from the year in which revenues from the sale of these products were made for the first time.

   b. An exemption is also granted when products are produced on third-party premises.

   c. Under the same conditions the said exemption also applies to profits from the provision of services.

   d. These incentives benefit legal entities and persons, as well as natural persons engaged in business.

   e. The timing of the exemption is linked to the tax year in which revenues from the sale of goods or the provision of services produced with or relating to the use of an internationally recognized patent are generated, provided that the registration process of the international patent has been completed.

   f. Consequently, revenue generated in fiscal years before the completion of the international patent registration are not taken into account for the commencement

of the three-year period.

g. Moreover, in the case of loss-making results, a company cannot benefit from the exemption, unless it is able to form a special reserve. Any exempted profits are posted in a special reserve account and calculated on the basis of the net profits declared in the income tax return and as depicted in the accounts and reflected in the balance sheet of the legal entity or person.

h. Tax exempted profits, profits from participation in other enterprises, any amounts reserved for the formation of the ordinary reserve, as well as any profits of the fiscal year that are actually distributed or withdrawals by the partners, as well as the tax-free deductions of investments provided for in tax incentive laws, should be deducted from net profits when calculating the reserve.

i. In the case of Sociétés Anonymes and Limited Liability Companies (*ΕΠΕ*), statutory reserves and distributed profits are grossed up by adding the corresponding tax. For legal entities keeping revenues-expenses books, the reserve is formed from the net earnings declared in the original statement after deduction of the withdrawals.

j. Special reserves formed as above are subject to taxation in accordance with the general provisions of the ITC, in so far as they are distributed, capitalized or withdrawn each time (currently at 29%).

k. For the purposes of taxation of the reserve upon distributions or capitalization, the respective amount is included in the profits from business activities. The above applies only to legal entities which keep double entry books.

l. It should be noted that ministerial decisions issued under Article 71 of Law 3842/2010 shall continue to apply until any new decisions are adopted. However, on 16 May 2018, the Joint Ministerial Decision of the Ministers of Economy and Development, Finance and the Governor of the AADE (Prot. No. 52738 / DEKN55 / 2018) was issued, setting out the terms, conditions and procedures for the application of Article 71A.

m. As a result, any accession firm should rely on the Joint Ministerial Decision, rather than the previous Decision no. 11970/2010.

4. Article 71B provides that:

   a. Listed legal entities may capitalize tax free reserves from numerous tax incentive laws such as Law 3299/2004, Law 2601/1998 and Law 1262/1982, at the reduced rate of 5% with the exemption of reserves formed pursuant to Article 18 of Law 942/1949.

   b. However, this rate does not apply to tax free reserves for which no time limit is provided for their capitalization or to concession agreements for road network construction ratified by various laws such as Law 3605/2007, Law 3555/2007 and Law 3597/2007.

   c. For the reserve capitalization, no cash contribution is required by the shareholders and new shares are issued on a pro rata

basis.

5. Article 71C provides that:

   a. Both listed and unlisted Sociétés Anonymes which have formed reserves deriving from goodwill of shares within the framework of a merger, spin off or capitalization of assets revaluation, may capitalize such reserves without further taxation.

   b. However, zero rate taxation does not apply where the legal entity is dissolved or the capitalized reserve is refunded to the shareholders before the lapse of 10 years from its capitalization. In this case, ordinary corporate income tax will apply (currently at 29%). Exceptionally, reduced rates apply in the case of mergers or acquisitions. Capitalization may be effected only by way of issuance of new shares.

   c. Reserves capitalized within the 2019 tax year are subject to income tax at 10%. This rate increases to 20% if the capitalization takes place within the 2020 tax year.

   d. Unlisted Sociétés Anonymes and Limited Liability Companies (ΕΠΕ) may capitalize tax free reserves, with the exception of reserves formed pursuant to Article 18 of Law 942/1949, on condition that the share capital will increase within the tax year of capitalization by way of cash contributions. New shares will be issued for the shareholders or partners.

   e. The capitalization of the tax free reserves is subject to income tax at the reduced rate of 10% (which is higher compared to the rate of 5% applicable to the capitalization of listed companies' tax free reserves). Tax free reserves capitalized within the 2020 tax year are subject to income tax at the rate of 20%.

6. Both Articles 71B and C provide that:

   a. The resulting tax is payable in 4 installments within one month from registration with the General Commercial Registry (*ΓΕΜΗ*). It is not deductible for tax purposes and cannot be set-off against ordinary corporate income tax.

   b. After payment of this tax, no further tax liability arises for the shareholders. Nevertheless, the respective income from this capitalization is subject to the Solidarity Contribution provided for by the ITC.

   c. This favourable treatment does not apply in the case that the legal entity is dissolved or the capitalized reserve is refunded to the shareholders before the lapse of 10 years from its capitalization. In this case, ordinary corporate income tax will apply (currently at 29%). Exceptionally, reduced rates apply in the case of mergers or acquisitions. The favourable treatment also does not apply to State subsidies where the specific provisions of Article 8 par. 6 of Law 3299/2004 apply.

B. Opinion no. 147/2018 of the Legal Council of State on the Applicable Time Limit in the Case of Late Submission of Income Tax Returns

1. The Legal Council of State, sitting in plenary session, opined that a limitation period of 15 years applies only in cases of non-submission of

tax returns or payment of withholding tax and that in cases of late submission of tax returns, the ordinary 5 years limitation period applies. This is extended by three additional years in cases where the late tax return is submitted within the fifth year.

2. This development will impact tax audits scheduled for 2018 to the extent that taxpayers who file late tax returns may not be subject to audit due to the application of the ordinary limitation period of 5 years.
3. Opinion no. 147/2018 resolves the conflict created by two previous Council of State rulings. By way of Opinion no. 173/2006, the Legal Council of State had held that late submission of tax returns is equivalent to non-submission when applying the 15 year limitation period. The second department of the Legal Council of State subsequently held by way of Opinion no. 111/2018 that the 15 year limitation period applies only to cases of non-submission and not in the case of late submission of tax returns. Opinion no. 147/2018 has ruled in favour of the 5 year limitation period applying to late filing of tax returns.

Contacts

Panayotis Bernitsas
Managing Partner
E pbernitsas@bernitsaslaw.com

Fotodotis Malamas
Senior Associate
E fmalamas@bernitsaslaw.com

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