

TAX BRIEFING: Monthly Insight

Tax Deduction of Business Expenses

The Ministry of Finance issued Ministerial Circular POL. 1113/2015 pertaining to the requirements for deduction of business expenses from gross revenues of legal entities or persons.

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Deduction of Business Expenses

Ministerial Circular III3/02.06.2015 (the "Circular") provides clarification regarding the right of businesses to deduct business expenses from their gross income (Articles 22, 22A and 23 of the Income Tax Code, pertaining to deductible and non-deductible expenses for tax purposes).

A. The Basic Rule

The basic rule is that all expenses:

1. realized for the benefit of a business or in the course of its ordinary commercial transactions;
2. referring to an actual transaction the value of which is not considered to be lower or higher than the market value on

the basis of information available to the tax authorities; and
3. booked in the period of their realization and evidenced by appropriate supporting documentation, may be deducted from a business' gross revenues.

However, the basic rule does not apply to non-deductible expenses provided in Article 23 of the Income Tax Code (please see below under C), as well as to tax exempt intercompany dividends based on Article 48 of the Income Tax Code.

In particular:

1. Expenses realized for the benefit of a business or in the course of its ordinary commercial transactions

These expenses include any expense that a business considers necessary for its business purpose, the development of its operations or the improvement of its market position, on condition that it is effected within the scope of the economic purposes or in the course of its ordinary commercial transactions and may contribute to the creation of income, or aims at the expansion of operations and the increase of income, or is related to actions within its corporate social responsibility. The tax authorities may not challenge the purpose and amount of the above expenses unless this is specifically permitted by law, for example in the case of intragroup transactions.

2. Expenses referring to an actual transaction the value of which is not considered to be lower or higher than the market value

Deduction of expenses that are fictitious in whole or in part or realized is not permitted. However, the receiver of a fictitious invoice who is in good faith as regards the issuer of such invoice may deduct the relevant expense from its gross income. Any loss arising from the valuation of titles, securities, liabilities etc. is not deducted as it is not realized. Any expense will be realized upon the transfer of the titles etc. or the payment of the relevant liability.

3. Expenses booked in the period of their realization and evidenced by appropriate supporting documentation

Business expenses must be posted in the tax year during which they were realized and supported by appropriate documentation.

4. Time of deduction

Business expenses are deducted from the gross income of the tax year to which they refer, with certain exceptions mentioned in Article 23 of the Income Tax Code, for example in the case of insurance contributions etc. (please see below under C). Business expenses that:

- a. are supported by documentation issued or received before the closing of the balance sheet; and
 - b. refer to the fiscal year being closed,
- are also deducted from the gross income of the year to which they refer.

B. Research and Development

Until the issuance of a relevant Presidential Decree, Ministerial Circular I2962 POL/ 2029/013.II.1987 will apply, providing criteria for the characterization of expenses as expenses realized for research and development ("R&D").

Deductible R&D expenses are those *actually* effected, minus any subsidy or allowance received by a business for the implementation of research programs. R&D expenses are deducted from a business' gross income at the time of their realization. An off-the-book additional 30% of the amount of R&D expenses is also deducted from the net profits of a business, upon submission of income tax returns.

Deduction of expenses for fixed equipment is achieved by depreciating these expenses equally in the 3 years following the year in which the expenses were made. The respective 30% discount increases the amount of R&D expenses deducted each year.

It is noted that upon submission of tax returns, a business should also submit all relevant supporting documentation to the General R&D Secretariat of the Ministry of Education in order for R&D expenses to be approved.

Any losses arising after the deduction of the above percentage will be transferred to be offset against future profits.

C. Non-Deductible Expenses

The Circular mentions the following categories of non-deductible expenses restrictively:

- i. *Interest payments for loans received by third parties*, with the exception of bank loans, interbank loans and bond loans issued by Sociétés Anonymes, to the extent that they exceed the amount of interest that would arise if the interest rate was

equal to the interest rate imposed on debit-credit account loans to non-financial businesses published in the Bank of Greece Bulletin of Conjunctural Indicators. Interest payments for bank loans, interbank loans and bond loans issued by Sociétés Anonymes are deducted in total, with the exception of cases of thin capitalization. Loans between affiliated persons are exclusively subject to the rules implementing *the arm's length principle* and the OECD's guidelines on intragroup transactions, as well as thin capitalization rules. It is further clarified that default interest is included in payments made on the basis of loan agreements. Any loss arising from the assignment of claims, e.g. to factoring companies, does not fall under the definition of loan interest and therefore is deductible if the conditions of Article 22 of the Income Tax Code are met.

2. *Any expense for the purchase of goods or services*, with the exception of payroll payments, lease payments for real properties and interest payments that do not constitute a provision of services, exceeding €500 paid in whole or in part without the use of bank means of payment.
3. *Insurance contributions*, including employers' and employees' contributions, that are not paid. Insurance contributions paid before the lapse of the *respective deadlines*, even those paid in a following tax year, are deductible from the income of the fiscal year to which they relate. Late payments of insurance contributions relating to the years from 2014 onwards, whether subject to a payment scheme or not, are deductible during the year that they are paid, irrespective of the year to which they refer. The Circular further analyses the way insurance contributions and remunerations of companies' members and administrators are deducted.
4. *Provisions*, with the exception of bad debt provisions provided in Article 26 of the Income Tax Code. It is noted that by virtue of Ministerial Circular No I056/02.03.2015, the amount of bad debt provisions which may be formed for tax purposes depends on the amount of the respective due and payable claims and the time for which such claims remain unpaid.
5. *Fines, penalty payments and any additional amounts charged for late payment* in the case of breach of contractual obligations or legal provisions including, among others, breach of tax or insurance legislation, penal clauses in contracts, redemption of penal sanctions imposed by the Court, default interest for late tax payments, payment of interest (i.e. additional taxes and fines) upon return of state aid amounts received on the basis of Law 3220/2004.
6. *Provision or receipt of remuneration in cash or in kind that constitutes a criminal offence*, for example, amounts from money laundering or bribery.

7. *The following taxes:*

- a. income tax;
- b. entrepreneurship duty (*telos epitidevmatos*);
- c. Special Levy imposed on profit from business activity (*ektakti eisfora*). It is noted that the special solidarity tax (*eidiki eisfora allilegiis*) is deducted through a lump sum payment;
- d. VAT on non-deductible expenses, if such input VAT is not deductible from output VAT. It is noted that:
 - VAT which may not be deductible from output VAT is deducted from gross profit, if it refers to expenses that are deductible under the Income Tax Code;
 - VAT on expenses made for expansions, additions or improvements of assets used in operations that are not subject to VAT increases the acquisition value of the assets, such value being depreciated according to Article 24 of the Income Tax Code; and
 - similarly VAT for the purchase of tangible assets which is not deductible from output VAT, increases the acquisition value of the asset and is deducted through depreciation of the total value of such asset according to Article 24 of the Income Tax Code; and
- e. taxes that are not deductible according to the provisions of special legislation.

Taxes re-charged to a counterparty business are deductible expenses of a business that re-charges them, on condition that the amount re-charged is included in the taxable income of the re-charging business. Taxes not mentioned above are deducted upon payment, with the exception of road tax (*teli kykloforias*), which is deducted in the following tax year, and advertising duty which is deducted in the year to which it refers.

8. *Deemed lease payments (tekmarto)* in the case of self-use (*idiorhisimopiisi*) of real property, to the extent that they exceed 3% of deemed value (*antikeimeniki axia*) of the real property. Non-profit legal persons may deduct the total amount of deemed lease payments without taking into consideration the above percentage.
9. *Expenses made when organizing and conducting informative conferences and meetings*, for example conferences regarding business strategy, future goals, import of new products to the market, product promotion, new techniques etc., for the accommodation (meals and stay) of clients or employees of a business as well as for the imposed municipal duties, to the extent that such expenses exceed €300 per participant and that the total annual expense exceeds 0.5% of a business' annual gross income. The Circular further clarifies that expenses incurred in relation to the conference venue, the

transportation of visitors and any speakers' remuneration are not included in the above non-deductible expenses.

10. *Expenses made for celebratory events and related accommodation* (meals and stay) of guests including municipal duties, to the extent that such expenses exceed €300 per participant and that the total annual expense exceeds 0.5% of a business' annual gross income.
11. *Entertainment expenses* (unless the main activity of the business is the provision of entertainment services).
12. *Private consumer expenses*. It is clarified that benefits in kind provided to employees and taxed as income from employment are considered to be effected for the benefit of a business and therefore are deducted as payroll expenses, if the rest of the conditions of Article 22 of the Income Tax Code are met. Other expenses that are not considered as taxable benefits in kind, for example, vouchers up to €6, the use of mobile phones, 70% of the cost of the company cars etc., are deductible according to the provisions of Article 22 of the Income Tax Code. The same rule applies to amounts paid by employees for their stay, meals and transportation when providing their services. In the case of benefits in kind in the form of loans granted to employees, partners or shareholders by a legal person or entity through an agreement in writing, the interest (deemed income from employment) taxed in the name of the individual is non-deductible for the legal person or entity.
13. *Further remarks:*
 - a. Advertising duties are non-deductible if they are not duly paid, i.e. paid after the expiration of the deadline for the filing of the respective income tax return.
 - b. Technical reserves that insurance businesses are obliged to create are tax deductible.
 - c. Expenses from the business activity of non-profit legal persons are deductible, in accordance with the provisions of Articles 22 and 23 of the Income Tax Code.
 - d. Articles 22 and 23 of the Income Tax Code are applicable to legal persons or entities acquiring income exclusively from real property. Such income is considered to constitute income from business activities.
 - e. Articles 22 and 23 of the Income Tax Code are also applicable to foreign legal persons or entities with no tax residence in Greece, irrespective of whether they acquire a permanent establishment in Greece, who are taxed for income from business activities in accordance with Articles 47 and 58 of the Income Tax Code.
 - f. Any bad debt provisions that are not booked in the P&L, for example, payments in advance, may be deducted in the

tax year during which the debtor is considered to be insolvent, in accordance with the provisions of Article 26 of the Income Tax Code and Ministerial Circular POL.1056/2015. Outstanding VAT on bad debts, which was not taken into consideration for the formation of the bad debt provision of Article 26 of the Income Tax Code, is

deductible in the tax year during which the debtor is considered to be insolvent according to the provisions of Article 26 of the Income Tax Code and Ministerial Circular POL.1056/2015, on condition that there is an obligation to pay VAT to the State and VAT was included in the VAT tax return (initial or amending) of the relevant tax period.