

TAX BRIEFING: Monthly Insight

Tax Treatment of Dividends, Interest and Royalties, Thin Capitalization Rules, Tax Treatment of Legal Entities

The Ministry of Finance issued Ministerial Circulars POL. 1039/26.01.2015 and POL. 1042/26.1.2015 with regard to the tax treatment of dividends, interest and royalties. Moreover, Thin Capitalization Rules and their application during the transitional provision until 2016 were clarified through the Ministerial Circular POL. 1037/2015. Finally, guidance for taxable income and certain exemptions of legal entities residing in Greece was provided by Ministerial Circular POL. 1044/2015.

IN THIS ISSUE

- A. Ministerial Circular POL. 1039/26.01.2015 provides clarification on the tax treatment of intra-group dividend, interest and royalty payments**
- B. Ministerial Circular POL. 1042/26.01.2015 deals with the tax treatment of dividends, interest and royalties**
- C. Ministerial Circular POL. 1037/2015 clarifies the Thin Cap Rules**
- D. Ministerial Circular POL. 1044/2015 provides guidance on the tax treatment of profit and non - profit legal entities**

- A. Clarification on the tax treatment of intra-group dividend, interest and royalty payments by way of Ministerial Circular POL. 1039/26.01.2015 (application of Articles 48 and 63 of the Greek Income Tax Code)**

Income Tax on Dividends

According to Article 48 of the Greek Income Tax Code, legal persons residing in Greece and receiving intra-group dividends from legal persons residing in either another EU member state or in Greece are exempted from income tax on dividends if the following conditions are met:

1. the recipient is a legal person with a tax residence in Greece and holds a minimum 10% participation interest in the distributor for at least 24 months; where the 24 month condition is not met, the recipient may instead provide a bank guarantee; and
2. the distributor is a legal person as per the terms of Annex I, Part A of Directive 2011/96EU, is a tax resident of an EU member state and is subject to one of the taxes referred to in Annex I, Part B of Directive 2011/96EU.

Dividends paid to cooperatives (*synetairismos*), societies (*koinonia*) and non-profit legal persons are not exempted from income tax. Dividends distributed to the permanent Greek establishment of EU companies residing in other EU member states by subsidiaries of these companies also residing in other EU member states are exempted from income tax, if the above conditions are met.

With regard to the Greek distributor, the legal person must be a *societe anonyme*, a limited liability company, a private capital company (*I.K.E.*) or a partnership (*prosopiki etaireia*). Dividends paid by joint ventures to their members are not exempted from income tax.

The dividends received are registered in a special reserve account, irrespective of the profit or loss position of the legal person. Upon distribution or capitalization, withholding tax at the rate of 10% applies, unless certain conditions are met.

If the above conditions for tax exemption are not met, a tax credit is provided against the income tax imposed on the dividends.

Withholding Tax on Dividends

According to Article 63 of the Greek Income Tax Code, dividends paid to legal persons residing in Greece or in another EU member state are exempted from withholding tax if the following conditions are met:

1. the recipient:
 - a. is included in Annex I, Part A of Directive 2011/96EU;
 - b. is a tax resident of an EU member state;
 - c. is subject to one of the taxes referred to in Annex I, Part B of Directive 2011/96EU; and
 - d. holds a minimum 10% participation interest in the paying entity;
2. the participation must have been held for at least 24 months; where the 24 month condition is not met, the person or entity liable to withholding tax may provide a bank guarantee instead; and
3. the distributor is any legal person or entity.

The Greek recipient may be a *societe anonyme*, a limited liability company, a private capital company (*I.K.E.*) or a partnership (*prosopiki etaireia*). Dividends paid by joint ventures to their members are subject to withholding tax, unless the members are legal persons. Dividends paid by a joint venture to a legal entity are not exempted from withholding tax. Therefore in the case where the Greek branch of a non-Greek company receives a dividend payment from a joint venture, withholding tax may be imposed, depending on whether the non-Greek company is a legal person or a legal entity.

Switzerland

Based on the agreement between the EU and the Swiss Confederation, legal persons residing in Greece and receiving dividends from legal persons residing in Switzerland are exempted from income tax on dividends, if the conditions set out in the agreement are met. The same rule applies in the case of legal persons residing or with a permanent establishment in Greece, paying dividends to legal persons residing in Switzerland.

Withholding Tax on Interest and Royalties

Article 63 also provides exemption from withholding tax on intra-group payments of interest and royalties if:

1. the recipient legal entity holds a minimum 25% participation interest in the paying taxpayer; or the paying taxpayer holds a minimum 25% participation interest in the legal entity receiving the payment; or a third legal entity holds a minimum 25% participation interest in both the legal entity receiving the payment and the paying taxpayer;
2. at the time of payment or credit, the above participation interest has been held for at least 24 months; where the 24 month condition is not met, the paying entity may provide a bank guarantee instead;
3. the legal person receiving the payment falls within the Annex to Directive 2003/49EC, is a tax resident of an EU member state and is subject to one of the taxes referred to in Article 3 of Directive 2011/96EC; and
4. the paying entity is any legal person or entity.

The Circular clarifies that Greek recipients must be a *societe anonyme*, which is the only type of Greek company included in the Directive's Annex.

Procedure and Documentation for Exemption from Withholding Tax on Dividends, Interest and Royalties (Ministerial Circular POL. 1036/26.01.2015)

Ministerial Circular POL. 1036/26.01.2015 sets out the procedure, as well as the form and content of the documentation to be submitted to the tax authorities, when applying for an exemption from withholding tax on dividends, interest and royalties. For payments effected between 1st January, 2014 and the issuance of Circular POL. 1036/26.01.2015, the documentation for the exemption from withholding tax can be submitted up until 30th April, 2015.

B. The Tax Treatment of Dividends, Interest and Royalties (Ministerial Circular POL. 1042/26.01.2015)

The payment of withholding tax at a tax rate of 10% for dividends, 15% for interest or 20% for royalties, exhausts the tax

obligations of non-resident legal persons or entities without a permanent establishment in Greece, including non-profit legal persons or entities acting through an office or branch, or individuals receiving income from dividends, interest or royalties. In the case of resident legal persons or entities, or of legal persons or entities with a permanent establishment in Greece, any income from the distribution of profit, interest or royalties is added to the annual income of the legal person or entity or the income of the permanent establishment, and is further taxed as income from a business activity. The same applies for individuals that engage in the business activity of receiving royalties from rights held by them, for example the providers of downloading services.

Greek resident legal persons or legal entities or individuals engaging in business activity, Greek Government bodies, or any taxpayer acting through a permanent establishment in Greece, are liable to withhold tax on the above types of income. It is noted that in case of interest remitted to Greece, withholding tax is imposed on the gross amount of interest by the financial institution or fiduciary in Greece which intercedes and acts as paying agent.

Dividends

The term *dividends* includes any income from: shares, founding titles, other rights for participation in profits that do not constitute debt claims, other corporate rights such as parts (*meridia*) and participation units (*merides*), dividends paid in advance (*promerisma*), mathematical reserves, participation in the profit of partnerships (*prosopikes etaireies*), profit distributions by any legal person or entity and any other similar distributed amount. The following are also deemed dividends: any profit distribution from a Greek or non-Greek source and related to listed or non-listed shares, founding titles, corporate parts of limited liability companies or to the participation in partnerships, joint ventures and other legal entities, interim dividends, temporary receipt of profits by shareholders or partners, interest from preferred shares, investment yields of the mathematical reserves of insurance companies, distribution of profits from trusts and off-shore companies, any form of remuneration paid to the members of the Board of Directors, administrators and personnel from the profits of the legal entity, profit distribution by units or shares in UCITS established in the EU, EAA or EFTA in the form of dividends or other proceeds and distributions of mutual funds established in third countries.

Profit distribution subject to withholding tax also includes any distribution or capitalization of the previous year's profits and reserves, with the exception of the distribution or capitalization of:

1. reserves created up until 31st December, 2013 which had been exempted from taxation; and
2. the reserves of limited liability reserves created up until 31st December 2010.

Profits distributed in the form of dividend or other proceeds from shares and units in UCITS established in the EU, EAA or EFTA are exempted from income tax. Profits remitted by a company with a permanent establishment in Greece to its headquarters abroad are not subject to withholding tax.

Legal persons or entities which keep revenue and expense books and distribute profits, are not under an obligation to withhold tax on payments. Accordingly, when these legal persons or legal entities receive profits, they are not subject to withholding tax and profits are taxed only in the name of the legal person or entity.

Temporary receipt of profits in the case of partnerships and legal entities which practice double entry bookkeeping are subject to withholding tax upon receipt of such profits.

Interest

The term *interest* refers to income from a Greek or non-Greek source arising from claims of any kind and in particular income from deposits, government securities, titles, bonds and any lending relationship, including agreements regarding premiums, repos or reverse repos, and consideration arising from titles, bonds or securities. It also includes loan interest, default interest on the basis of a contractual obligation and adjudicated interest resulting from a Court decision, irrespective of whether it is related to the company's business activity.

Banks and Credit Institutions

In the case of loans granted by credit institutions residing in Greece or abroad in the context of their business activity, interest, including default interest, interest on inter-bank deposits and interest from the use of credit, is exempted from withholding tax. However, interest acquired by credit institutions and arising from bond loans is subject to withholding tax, even if the credit institutions are not tax resident and do not have a permanent establishment in Greece. Circular POL. 1042/26.01.2015 does not clarify whether bond loans assumed 100% by credit institutions are exempt from withholding tax, due to the fact that in reality they constitute loans granted by credit institutions.

Governmental Bonds and Treasury Bills

Interest arising from Greek government bonds and treasury bills is not subject to income tax if acquired by an individual. If acquired by non-Greek tax resident legal persons or entities which do not have a permanent establishment in Greece, no withholding tax is imposed. Interest arising from EFSF bonds issued for the restructuring of Greek debt is not subject to income tax, if acquired by an individual or a legal person.

Royalties

The term *royalties* refers to income from a Greek or non-Greek source which relates to the use or the right to use the rights,

irrespective of whether they have been officially registered. Payments for the re-licence or sub-licence of the intangible asset to which the royalty relates, as well as payments relating to the lease of containers and industrial, commercial or scientific equipment, such as equipment for the transmission of power, telecommunication, gas or oil, are also considered as royalties. Should the transfer of ownership of intangible assets result in the alienation of the owner from these assets, the relevant payment is not considered as constituting a royalty payment. On this basis, payments to exclusive agents, resellers, mediators and so on, as well as the sale of standard software, are not treated as royalty payments. No withholding tax is imposed on royalty payments between legal persons or entities residing in Greece or with a permanent establishment in Greece.

C. Thin Capitalization Rules and Transitional Period for Application

Ministerial Circular POL. I037/2015 provides clarifications with regard to the application of thin capitalization rules by legal entities. In particular:

1. interest from loans granted by third parties, with the exception of interest on bank, interbank and bond loans granted by societies anonymes, is not deducted from the gross income of the company to the extent that it exceeds certain limits or other requirements set by the law on tax;

2. subject to 1. above, if the interest expenses paid annually by the company are lower than the threshold of €5m for each of the 2014 and 2015 tax years, and €3m for the tax years beginning on 1st January, 2016 onwards, any surplus interest expenses (i.e. the amount of interest expenses exceeding the amount of interest income) are fully deductible from the company's gross income, even if they exceed 60%, 50%, 40%, or 30 % of EBITDA for the tax years beginning on 1st January, 2014, 2015, 2016 or 2017 respectively; where the interest expenses exceed the threshold of €5m or €3m respectively, the deductible interest expenses cannot exceed the ceiling as above of the surplus interest expenses as a percentage of EBITDA; and
3. the amount of interest expenses that can be carried forward in each tax year cannot exceed the amount resulting from the percentage of EBITDA reduced by the surplus interest expenses of the same year.

D. Taxable Income of Legal Entities in Greece - Tax Exemptions

Ministerial Circular POL. I044/2015 provides further guidance on Law 4172/2013 with regard to the subjects and object of income tax. In particular:

1. the forms of legal entities which are subject to corporate tax in Greece are defined by the law;
2. all the revenues of a legal entity constitute profits earned from a business activity on which tax is imposed; under certain conditions an exemption applies for income deriving from dividends in the case of intra-group transactions;
3. non-profit legal entities are subject to income tax, with the exception of income earned exclusively during the fulfillment of their scope, which is not taxable; whether or not the income was generated in the course of the fulfillment of the non-profit's scope is determined by the tax authorities with reference to the scope set out in their constitutional documents, the nature of which gave rise to the income and its use; and
4. certain legal entities are fully tax exempt, such as the Bank of Greece, Portfolio Investment Entities and Organizations of Collective Investments (OSEKA) established in Greece or within the EU or EEA, international organizations under the condition of mutuality and the Hellenic Republic Asset Development Fund (TAIPED); a partial tax exemption is provided for some governmental entities.

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