Minimum Tax Rate of 15% Now a Reality in the European Union

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On Thursday, 15 December 2022, the European Commission announced the official adoption of the minimum tax rate across its territory, effective as of 1 January 2024, i.e. in just one year from now.

The relevant European Directive must be transposed into law by all Member States without exception, including of course Cyprus.

At international level, an agreement had already been reached by around 140 OECD member countries back in October 2021. It was therefore only a matter of time before the Member States of the EU would unanimously agree to adopt the Directive, despite the reservations expressed initially by Poland and later on by Hungary.

This new reality affects only multinational and domestic groups with a total annual turnover of at least €750 million, based on their consolidated financial statements. Groups of such size will pay this additional tax in case the effective tax rate on their accounting profit in each separate jurisdiction they have presence is below 15%.

The impact of imposing this additional tax of up to 15% on the accounting instead of the taxable profit is huge, as in many jurisdictions accounting profit is much higher than taxable profit due to the many and varied tax exemptions and deductions that they offer.

Cyprus is, of course, one such jurisdiction and therefore companies based in our country and belonging to such groups, whether their ultimate parent company is here or abroad (in the EU or in other third countries) are inevitably subject to this increased tax on their accounting profits.

According to the general rule, the additional tax is imposed on the ultimate parent company, which pays it to its own tax authority for all its subsidiaries wherever they are located worldwide.

However, under the European Directive that has just been adopted and in order to safeguard the sovereignty of EU Member States, each Member State may choose to apply the Directive at domestic level for companies established in its own jurisdiction and therefore collect this additional tax itself instead of leaving it to the jurisdiction of the parent entity.

The question that naturally arises is how Cyprus may be affected by this new reality and whether we actually have here in Cyprus such companies that ultimately belong to global giant conglomerates.

We, at PwC Cyprus, conducted a few months ago our own internal study. Our findings have revealed that the number of such companies based in Cyprus is indeed significant. Moreover, the amount of annual taxes that these companies pay to the Republic of Cyprus is quite substantial in relation to the total corporate income taxes that our Government collects.

The impact of the application of these new rules must therefore be assessed in a responsible, thorough and prompt manner.

The challenge for us as an international business centre is to fully comply with the European Directive, while somehow managing to remain competitive. Our goal should not be limited to finding ways to retain the foreign corporate investors who have trusted Cyprus so far, but also to turn this new challenge into an opportunity to attract an even greater number of such global foreign investors. These substantial taxes currently collected by our Government could more than double but at the same time could very well be lost altogether if we are unable to strike the right balance.

It is therefore critical, in our view, to react as soon as possible and certainly earlier than the other Member States and third countries with a profile similar to ours.