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Cyprus – VAT – Cash flow management – COVID-19 - Bad debt relief – reminder

One of the main areas businesses across the world are urgently addressing in these unprecedented circumstances is their cash flow management. Businesses in Cyprus are no exception.

In this respect, a reminder of the applicable in Cyprus VAT provisions on bad debt relief could be very useful.

Even though the conditions under which the bad debt relief applies have **not** been eased in response to the current crisis, which would be a welcome measure, some businesses might find that VAT previously paid by them on goods or services they have supplied could be claimed back subject to the applicable conditions and timeframes.

To check if they are eligible for bad debt relief, VAT registered businesses in Cyprus should review all their outstanding receivables in order to confirm if the conditions of the bad debt relief are met.

The guide below aims to assist VAT registered businesses in Cyprus in evaluating the relevant conditions.

Short legal background

Legal provisions	VAT Circulars/Information Leaflets issued by the Tax Department
Article 27 of the VAT Law N 95(I)/2000 (as amended)	VAT Circular 234 of 13 June 2019 (replaced the previously applicable VAT Circular 204 of 12 June 2016) This Circular was issued in response to CJEU case A-PACK CZ of 8 May 2019 – interpretation of Article 90 of the EU VAT Directive
Regulations 89 to 103 of the General VAT Regulations ΚΔΠ 314/2001 (as amended)	Information Leaflet 14 of January 2002 (should be read together with the latest VAT Circular 234 of 13 June 2019)

Summary of the conditions and the steps to be taken

The summary is mainly based on the issued by the Tax Department on 13 June 2019 VAT Circular 234.

(1)

On making a claim to the Commissioner of Taxation, the bad debt relief shall be allowed where the person making the claim

- a has supplied good or services **and** has accounted for and paid the VAT on the supply,
- b has **written off** the whole or part of the consideration in his accounts as bad debt,
- c has taken all '**necessary measures**' under the respective circumstances to collect the bad debt, and
- d a **period of 12 months has elapsed**, starting with the date of the supply.

Indicative list of 'necessary measures' under the circumstances

- sending a letter to the debtor demanding payment of the debt,
- sending a letter through a lawyer,
- unsuccessful debt collection,
- taking legal actions, etc.

(2)

The claim must be made within 4 years from the **later of**

- a the date on which the outstanding amount came due and payable, or
- b the date of the supply,

by including the amount in Box 4 of the relevant VAT return (effectively as an increase in the input VAT claimed for the period even though the amounts actually concern output VAT being adjusted for total or partial non-payments from relevant customers).

(3)

The bad relief claim is subject to the claimant giving the debtor **a written notification** within **7 days** from the date the claim was made, including in the notification the information provided for in Regulation 92 of the General VAT Regulations (see table below).

In addition, and within the same time limit of 7 days from making the claim, the Commissioner of Taxation must be notified of the claim, including in the notification the VAT numbers of the debtors under the claim. This is a new condition introduced with Circular 234.

Reg 92 - written notice to debtor (where he is a taxable persons) needs to contain

- a) the date of issue of the notification;
- b) the date of the claim;
- c) the date and number of any VAT invoice issued in relation to each relevant supply;
- d) the amount of the consideration for each relevant supply which the claimant has written off as a bad debt;
- e) the amount of the claim.

(4)

The claimant must keep the necessary evidence in support of the claim as provided for in Regulation 93 and keep records as per Regulation 94 of the General VAT Regulations (see tables below).

Any record kept shall be kept in a single account known as 'Refund for bad debts account'.

Reg 93 - evidence for each supply must be held before making a claim and shall include for each relevant supply

- a) either –
 - i. a copy of any VAT invoice provided to the customer, or
 - ii. where there was no obligation to provide a VAT invoice, a document which shows the time, nature and purchaser of the relevant goods or services, and the consideration therefor;
- b) records or any other documents showing that the claimant has accounted for and paid the VAT thereon; and
- c) records or any other documents showing that the consideration was written off in his accounts as bad debt.

Reg 94 - record of each claim must be kept in single account to be known as the "refund for bad debt account"

- a) in respect of each relevant supply for that claim –
 - i. the amount of VAT chargeable,
 - ii. the prescribed tax period in which the VAT chargeable was accounted for and paid to the Commissioner,
 - iii. the date and number of any invoice issued in relation thereto or, where there is no such invoice, such information as is necessary to identify the time, nature and purchaser thereof, and
 - iv. any payment received thereof;
- b) the outstanding amount to which the claim relates;
- c) the outstanding amount to which the claim relates;
- d) the amount of the claim;
- e) the prescribed tax period in which the claim was made; and
- f) a copy of the notice required to be given in accordance with Reg 92

(5)

The claimant must keep the documents, invoices and records which he holds in accordance with Regulations 93 and 94 for a period of 4 years from the date of making the claim, unless the Commissioner or Taxation allows otherwise.

(6)

The bad debt shall be *written off* from the accounting records of the claimant through the income statement (Profit & Loss Account) for the claim to be allowed.

(7)

The bad debt cannot be written off in a provisional account (Provision for Bad Debts). The write off shall be made in the income statement with a corresponding entry in the relevant debtor's account or in a separate account 'Debtors written off in income statement'. The separate account must make a reference to the name of the debtor who has been written off.

(8)

Where the claimant is a natural person, who is not required to prepare income statement and submit financial statements, the write off shall be made in the 'Refund for bad debts account'.

(9)

In case any amount from the written off amounts is *recovered after the claim for bad debt was made*, the claimant must proceed with a correction in respect of the VAT refunded. The correction is done by accounting for output VAT for the corresponding amount at the time of collection and *at the rate applicable to the original transaction*.

(10)

The correctness of the claim made by the claimant in his books and tax returns can be verified by the Tax Department only after such a claim have been made by the submission of the relevant tax return.

(11)

As per Article 27(5) of the VAT Law, where a claimant is entitled to make a bad debt relief claim and the VAT claimed has at any time been included in the customer's input VAT, the customer – from the time the claimant made the claim for bad debt relief, is no longer entitled to the input VAT deduction.

(12)

Special cases of bad debt relief

VAT status of a debtor in respect of which a bad debt relief is made

Previously, as a matter of policy detailed in the VAT Circular 204, a bad debt relief could not be claimed if the relevant debtor was no longer VAT registered at the time of the claim.

However, taking into account the CJEU decision in the A-PACK CZ case (C-127/18), the policy was amended and as explained in the latest VAT Circular on the matter (Circular 234), a bad debt relief claim could be made even if the respective debtor is no longer VAT registered at the time of the claim.

VAT de-registration of a debtor in respect of which a bad debt relief is made

It is noted that a debtor/customer cannot apply for VAT de-registration (or back dated de-registration) from a date which falls before the date on which the supplier has made a bad debt relief claim.

Customers not entitled to input VAT deduction

The right to refund of VAT under the bad debt relief procedure is not withdrawn if the debtor is not entitled to input VAT deduction in full or partially.

Legal rights of the creditor for collection of due amounts

The claimant is still entitled to proceed with legal actions against the debtor if he has claimed bad debt relief. Provided the conditions for claiming bad debt relief are met, where the supplier has already proceeded with legal actions against the debtor, this does not affect his right to claim bad debt relief.

Insolvency of the debtor, enforceable 'security' and bounced cheques

If the debtor is insolvent or his cheques have bounced, the procedure for claiming bad debt relief remains the same.

Where a receiver or administrator has been appointed to manage the tax affairs of the debtor, that person is responsible to make the necessary adjustments in the debtor's books.

In accordance with Regulation 98(5) of the General VAT Regulations, where the claimant holds an enforceable 'security' against the customer, the consideration written off in the accounts of the claimant shall be reduced by the value of that security. 'Security' means any mortgage, right to a lien or other security.

Where the claimant holds bounced cheques, these are not considered to be an enforceable security covered by Reg 98(5) of the General VAT Regulations

Claim/refund by a claimant who is no longer VAT registered

In accordance with Regulation 91(2) of the General VAT Regulations, if at the time the claimant becomes entitled to a refund, he is no longer required to make returns to the Commissioner, that is - he is no longer VAT registered, he shall make a claim to the Commissioner in such a form and manner as the Commissioner may direct.

In accordance with Regulation 97(4) of the General VAT Regulations, if at the time the claimant is required to repay any amount, he is no longer required to make returns to the Commissioner, that is - he is no longer VAT registered, he shall make a repay the amount to the Commissioner at such time and in such a form and manner as the Commissioner may direct.

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