Expected corporate tax developments 1/49/21

The Corporate Income Tax (CIT) Act has been amended only slightly during 2021, as we wrote in our Flash News edition of 20 April 2021. This article explores the latest changes to the CIT Act as well as amendments being proposed for the near future, including the long-awaited rules for bad debt provisions under IFRS 9 *Financial Instruments*.

Bad debt provisions

Provisions made under IFRS 9

When preparing the CIT return for December 2021, many companies were planning to add their bad debt provisions to the tax base for the first time because those would have exceeded the time limit of 36 months after they were made. That is why companies welcome amendments that will release provisions made under IFRS 9 from this requirement, as they are based on a different set of criteria and were not consistent with the substance of a bad debt provision when they were made.

There are also plans to pass amendments by the end of the year that will insert in section 9 of the CIT Act some exceptional conditions a company has to meet before it can take an exemption: the company holds an appropriate auditor's report; each trade receivable included in the provisions (credit losses) can be traced; and procedures for recognising, recovering and derecognising receivables (financial assets) are in place. The new conditions will apply to trade receivables covered by provisions (credit losses) made after 2017.

However, if a provision made in this way applies to a truly bad debt the company has expensed and which will not have been recovered within 60 months after it arose when the customer was supposed to pay the supplier, and the receivable is ineligible for an exemption under section 9(3) of the CIT Act, then provisions made under IFRS 9, too, will have to be added to the tax base.

Other bad debt provisions

There are plans to extend the period during which a company has the option of keeping its bad debt provisions out of the tax base in the following situations:

1. If the debtor goes into insolvency, the 36-month period is extended to 60 months.
2. For all provisions made before 2022, the period for increasing the tax base will be 60 (not 36) months after a particular provision was made.

Accordingly, bad debt provisions can stay out of the tax base on the CIT return for December 2021.

Thin capitalisation rules

The CIT treatment of interest expenses and the current thin cap restrictions are facing a number of important developments, as section 10 and transition rules of the CIT Act and the Covid-19 Act are being amended.

Covered bond entities

Covered bond entities organised and existing under the Covered Bonds Act are governed by amendments to the CIT Act already in force. Thus, covered bond entities will not be required to apply the thin cap restrictions, and for companies paying interest to covered bond entities, those interest payments will not create any additional CIT expense.

Special relief in 2021 and 2022

To cope with the adverse impact of Covid-19 on the financial position of companies, there are plans to waive the current cap on any loan interest that does not represent a CIT item in 2021 and 2022. The Covid-19 Act provides for these amendments.

Net interest cost

There are also plans to change the way of measuring interest costs so that companies can calculate net interest – the difference between interest payments and interest revenues (if any). However, this approach will be allowed for only one of the two methods, i.e. if the company’s interest costs exceed EUR 3 million a year. These amendments are to apply from the financial year beginning in 2021.

Estimated interest arising under IFRS 16

Interest estimated on an operating lease in companies applying IFRS 16 *Leases* can stay out of their thin cap calculation if that lease is essentially an operating lease. This new provision, too, applies to estimated interest from the financial year beginning in 2021.