Cyprus – international financial services is one of the main drivers of recovery

REPORT SUMMARY

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- Economic citizenship
- Corporate/fiduciary regulation
- Registration of trusts
- Tax treaties

BY PHILIPPOS ARISTOTELOUS

The early months of 2013 were dominated by the "bail-out" of Cyprus by the European Stability Mechanism and the IMF. For the first time, depositors in banks were compelled by the Eurogroup to contribute to the recapitalisation of the banks, and depositors in Cyprus's two largest banks lost all or a substantial proportion of any balance in excess of €100,000. Many people lost their life savings and a number of businesses closed – the death of Cyprus as an international financial centre was widely predicted, not least by some competitor jurisdictions.

However, although the banking sector was damaged, the other two pillars on which Cyprus's success as an international business centre is based – its transparent legal system and high-quality professional services – remained intact, and the predicted exodus of Russian and Eastern European investment did not happen.

Corporate tax rate

In April 2013, at the behest of Cyprus's international creditors, the corporate tax rate was increased from 10% to 12.5%. Even after the increase, Cyprus's corporate tax rate is one of the lowest in the EU and the increase has not materially affected most holding companies. Furthermore, the other benefits of the Cyprus holding company regime such as the tax free flow of dividends through Cyprus and the beneficial exit opportunities offered by Cyprus's favourable tax legislation and wide network of double tax agreements (DTAs) remains intact.

Economic citizenship

In April 2013 the government issued details of its "economic citizenship" programme, under which individuals with substantial economic interests in Cyprus and their dependents may obtain citizenship by naturalisation on an accelerated basis. In order to qualify, applicants must have a clean criminal record and own a residence in Cyprus, and must invest €2.5 million or more in Cyprus, or be the owner or substantial shareholder of a company doing business in Cyprus. Since Cyprus is an EU member, Cyprus citizenship is proving highly attractive to HNWIs, as it considerably simplifies international travel and visa requirements for certain countries.

Corporate/fiduciary regulation

The Law Regulating Companies Providing Administrative Services and Related Matters of 2012 (ASP Law), enacted

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in December 2012, transposed the EU Third Money Laundering Directive into national law. It regulates the provision of company and trust management services and establishes a framework for the licensing and supervision of service providers, offering security to clients and strengthening confidence in the sector. The ASP Law provides that relevant services may be offered only by persons or legal entities that hold a licence from the Cyprus Securities and Exchange Commission (CySEC) or who are specifically exempted from the licensing requirement (principally, registered lawyers and accountants, who are regulated by their respective professional bodies).

Registration of trusts

In September 2013 the ASP Law and the International Trusts Law of 1992 to 2012 were amended to create a register of trusts established in Cyprus. Each of the supervisory bodies for the purposes of the ASP Law – CySEC, the Cyprus Bar Association and the Institute of Certified Public Accountants of Cyprus – is required to maintain a register of trusts established by the service providers they regulate, which contains the following information:

- Name of the trust;
- Name and full address of every trustee at all relevant times;
- Date of establishment of the trust;
- Date of any change in the law governing the trust to or from Cyprus law; and
- Date of termination of the trust.

For new trusts the information must be provided to the supervisory body within 15 days of establishment of the trust; for existing trusts six months (to 9 March 2014) was allowed.

Service providers establishing trusts are now required to obtain documentary evidence of identity of the settlor, the trustees, the beneficiaries (or information on the class of beneficiaries including those to whom any distributions have been made under the trust) and others associated with the trust, as well as information on the activities of the trust. This information must be available for inspection by the relevant supervisory body on request.

These changes will enhance Cyprus's position as an attractive trust jurisdiction with a legal infrastructure that entrenches jurisdictional and asset protection for trusts whilst fully complying with all applicable EU and domestic AML laws and regulations. The registers of trusts are not open for public inspection, so confidentiality is not prejudiced.

Tax treaties

Despite the other distractions the government pressed ahead with its initiative to expand and modernise Cyprus's network of DTAs. On 1 January 2014, five new DTAs took effect between Cyprus and Estonia, Finland, Portugal, Spain and Ukraine. The first four are entirely new treaties, while the agreement with Ukraine replaces the old Cyprus-USSR treaty, which had been adopted after the dissolution of the USSR. All the new agreements follow the OECD Model.

The new DTAs with Estonia, Finland, Portugal and Spain are expected to lead to a substantial expansion of economic ties and reciprocal investment activities with Cyprus. The revised agreement with Ukraine retains the principal benefit of the DTA it replaced – the highly favourable provisions regarding capital gains on disposal of shares in property-rich companies. Movable property including shares is taxable only in the owner's country of residence. Since Cyprus imposes no tax on disposals of shares except where the gain is derived from real estate in Cyprus, Cyprus companies have become an ideal means of holding real estate in Ukraine, effectively allowing property to be disposed of tax-free.

Conclusion

A year after the bail-out, it is clear that reports of Cyprus's demise were premature. The targets for economic reform agreed with international lenders are being met or exceeded, and while there is serious unemployment in the economy as a whole, and particularly in the construction industry, the international services sector has held up well and is likely to be one of the drivers of recovery.

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It is also clear that a great deal of the bad press that Cyprus received in the early months of 2013 alleging laxity in application of its anti-money laundering legislation was unjustified. An audit carried out by Deloitte and Moneyval, the Council of Europe's anti-money laundering body, found that Cyprus has robust legislation that is applied consistently and systematically. Similarly, the decision of the OECD Global Forum to assess Cyprus, together with the British Virgin Islands, Luxembourg and Seychelles, as non-compliant with international information exchange standards appears to have been unduly harsh, given that Austria, Jamaica and Mauritius, which achieved full compliance in fewer areas than Cyprus, were not.

Certain of the reforms outlined above, made at the behest of Cyprus's international creditors, will improve regulation and keep out undesirable practices, and so help to enhance Cyprus's reputation for transparency and reliability – and its attractiveness to reputable investors. The government and the financial services sector are committed to offering a competitive tax and business environment with the highest standards of probity. While there are undoubtedly challenges ahead, progress to date is highly encouraging.