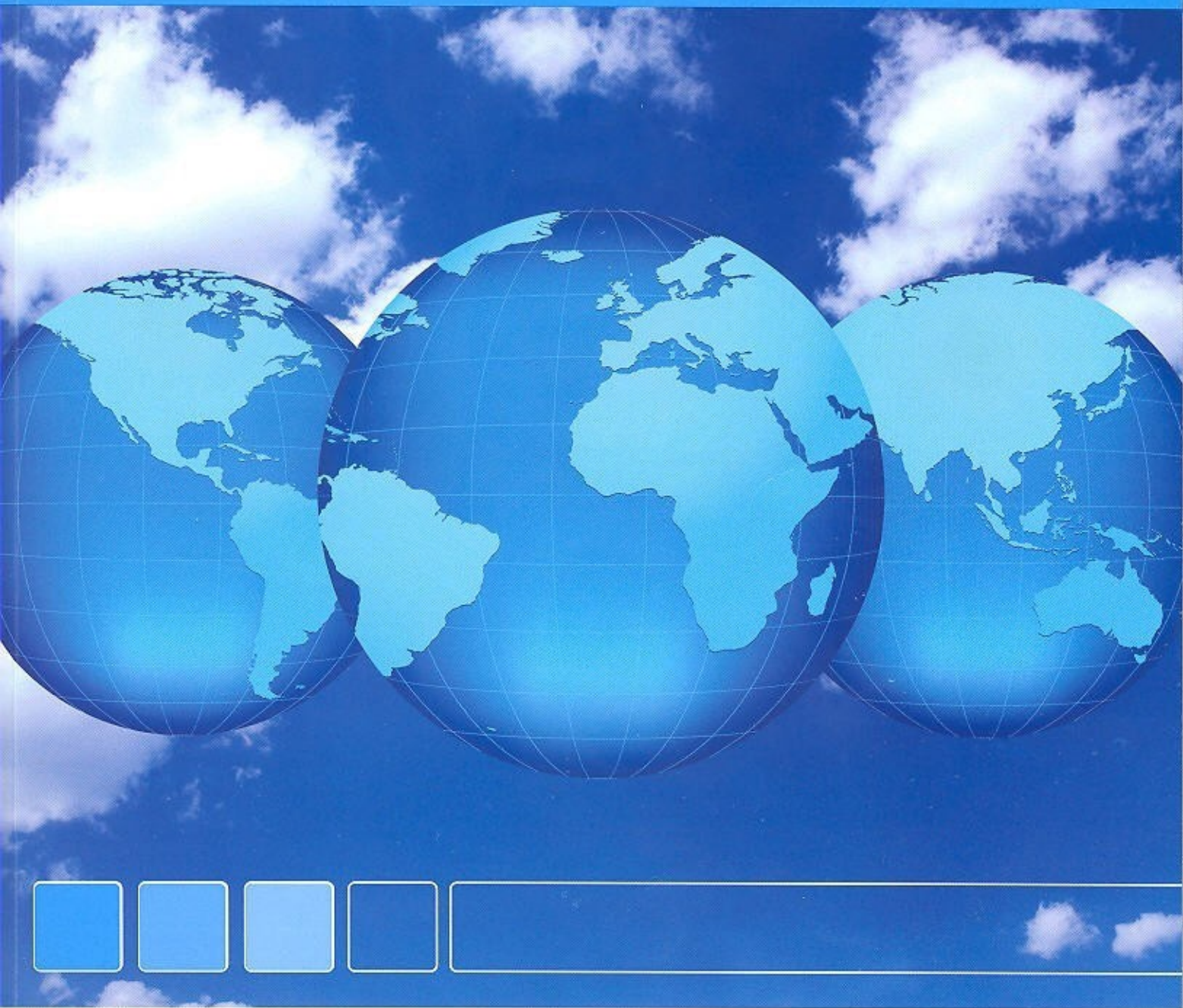
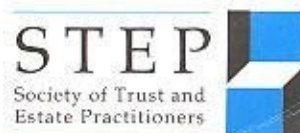


# STEP Directory and Yearbook 2007



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Cyprus

# Cyprus

## EDITORIAL BOARD

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## 1. INTRODUCTION

### a. History and background

An independent and sovereign Republic of Cyprus came into being in 1960 following several decades as a British colony. Early and persistent tension between the Greek Cypriot majority and Turkish Cypriot minority culminated in violence, leading to deployment of UN troops in 1963 and the establishment of enclaves of Turkish Cypriots. In 1974, a coup attempt, sponsored by the Greek government, led to Turkish military action. Turkey's intervention gave rise to occupation and control of a third of the island in the north. A prolonged and extant stalemate between the two sides continues, even though the UN have repeatedly tried to bring about *rapprochement*.

The Republic, comprising of the entire island, entered the European Union (EU) on 1 May 2004. However, the application of EU law does not apply to the areas that are not controlled by the Cypriot government.

Cyprus is the third largest island in the Mediterranean, and is located in the Levant, about 40 miles south of Turkey's southern coastline. Its population is estimated to be just fewer than 800,000 people and its total

area comprises of approximately 900,000 square kilometers. Its security is complimented by the presence of the British Sovereign Bases on the island possessing 99 square miles of British territory.

Tourism and financial services dominate Cyprus' economy, representing three quarters of GDP. Recent rates of growth of GDP have been above the EU average. Cyprus has already joined the European Exchange Rate Mechanism with a view to adopting the euro at the beginning of 2008. A successful outcome is not yet guaranteed and the government has organised an austerity program of economic measures to increase the chances of success.

The government is promoting Cyprus as an international financial centre through the negotiation of bilateral tax agreements and membership of the EU.

The currency is the Cyprus pound (CYP)

### b. Legal system

Cyprus has a written constitution incorporating separation of powers as well as fundamental and embedded articles that neither the president nor the unicameral legislature nor any other office of the Republic may

change. One such embedded article deals with fundamental rights and liberties (and obligations) which are afforded to all persons and not just Cypriots.

The constitution is the highest legal authority and no other law may contradict it. The next level below the constitution is comprised of international agreements, conventions and treaties, including the EU's *Treaty of Accession* and numerous double tax treaties. These override national statute law in the event of discrepancy.

The flavour of statutory law is a combination of the legislature's laws, British colonial regulations and EU directives. In addition, statute law directs the courts to follow English civil and criminal jurisprudence, including the rules of equity, wherever practicable.

Cyprus has an independent judiciary comprising of a supreme court and several kinds of subordinate courts.

Owing largely to the withdrawal of the Turkish Cypriots from the political process there are some

exceptional constitutional cases where the doctrine of necessity has been applied.

## 2. SOURCES OF LAW

### a. Trust creation and administration

The primary source of trust law is English common law and the colonial regulation *CAP193 Trustees*, which is based upon the English *Trustees Act 1925*. In 1992 the *International Trusts Law 1992 (ITL)* was introduced. The *ITL* builds on existing law, modifying it in certain instances. A trust formed in accordance with the *ITL* is known as a Cyprus International Trust (CIT). However, its provisions are not available for permanent residents of the Republic.

### b. Property, estate and probate

The majority of property, estate and probate law is English in origin. The rules governing intestacy are based upon the *Italian Civil Code*.

Property rights and their enjoyment are protected in the Constitution.

## NEW DEVELOPMENTS

- Euro anticipated for January 2008.
- Professional trustees and corporate service providers to be regulated before the end of 2007.
- Should be possible to form a European company by the end of 2006.
- Total number of treaties in force is now 33, covering 43 countries.



### 3. TRUSTS

#### a. Introduction

Cyprus law expressly adopts common law and equitable principles of English law. The civil and criminal courts follow these principles unless otherwise mandated by statute law or the Constitution. The *ITL* was designed with the intention of bringing international trusts into line with global developments at the time. The *ITL* does not apply, however, in cases where a settlor is a permanent resident of Cyprus.

#### b. Most frequently used trusts

Trusts being administered by trustees in Cyprus for domestic purposes are categorised as private or public. The CIT is the most common arrangement for international structures.

CITs are useful for inheritance and tax planning, and include special features such as protection from inheritance rules of other jurisdictions.

Both CITs and private trusts can be used to structure pension schemes, employee incentive schemes and family trusts, whereas CITs and public trusts can be used for charitable purposes.

CITs must appoint and retain at least one trustee who is resident in Cyprus at all times. That person may be either natural or juristic. There is provision within the *ITL* for the transfer of a CIT from Cyprus to another suitable jurisdiction.

#### c. Proper law of a trust

Cyprus is a member state of the *Hague Convention on Private International Law*. Although a signatory of the *Hague Convention on the Law Applicable to Trusts and on their Recognition*, 1 July 1985, Cyprus has not yet ratified the treaty. Cypriot courts take the *Convention* into account when considering trust matters of private international law.

In reaching a decision about jurisdiction, the court takes into account the place of administration, *situs* of the trust's property and objects of the trust.

#### d. Creation of a trust

*i. Validly constituted trusts*  
Cypriot trusts must be properly constituted in accordance with English legal principles or the *ITL*. Furthermore, a settlor's intentions to settle a trust must be demonstrably certain. Finally, the property of a trust and its beneficiaries must be verifiable.

Trusts can be created orally. However, those involving land must be in writing.

#### *ii. Duration and termination of a trust*

Private trusts ordinarily endure for a 'life in being' plus 21 years. However, the *ITL* offers duration of either up to 100 years or perpetuity in the case of a 'purpose' trust. Public trusts may also endure without limitation.

#### *iii. Beneficiaries*

Private trusts must have beneficiaries who can enforce the trusts vested in the trustees; otherwise, the trust will fail and its property will revert to its settlor. However, CITs may have objects rather than beneficiaries, as long as there is an appointed enforcer of the trusts, and the distribution of trust property upon cessation is clearly defined.

The rights attaching to a beneficial interest give beneficiaries access to the court as regards the proper execution of a trust. If appropriate, the court will compel trustees to discharge their obligations and make restitution for any breach of trust that has resulted in loss. Where all beneficiaries of a trust are known, *sui juris*, absolutely entitled and in agreement with one another, they can bring a trust to an immediate dissolution.

The beneficiary who is entitled to a fixed interest may sue to enforce an entitlement. In the case of a discretionary trust, a beneficiary may bring an action against the trustee if that trustee has not exercised the discretions required under the trust instrument.

#### *iv. Trustees*

The powers granted to a trustee are primarily found in the trust instrument, although other powers may be granted by statute or court order. Trustees have a duty to administer a trust's property diligently and prudently and to observe the highest standards of integrity. If they fail, they may be held personally liable. Usually one trustee is appointed, however, where the trust property includes land, there must be at least two trustees. Trustees must always act unanimously, unless the trust instrument provides otherwise. The number of trustees shall not exceed four in number.

#### *v. Protectors*

Although the law is silent in this regard, protectors of a trust may theoretically be appointed. Protectors have a fiduciary duty to act in the best interests of a trust.

#### *vi. Role of courts*

The court may enforce trusts on behalf of beneficiaries. Furthermore, the court may appoint and replace trustees, as well as provide authorisation, indemnification and directions in certain circumstances.

#### e. Trust administration

##### *i. Investment*

There are special provisions for CITs that allow trustees to make any investments subject to the terms of the trust and the satisfaction of the 'prudent person' test. Other private and public trusts must invest in statutorily authorised investments.

##### *ii. Maintenance and advancement*

Trustees are authorised under *CAP193 Trustees* to advance up to half of a presumptive share of capital to a beneficiary, subject to any beneficiary's prior interest. In addition, trustees may accumulate income during a beneficiary's minority or apply it for the minor's maintenance, advancement or general benefit.

##### *iii. Variation of a trust*

The British *Variation of Trusts Act 1958 (VTA)* was not enacted in Cyprus before independence and, as a result, the Cypriot courts have less power to vary or influence private and public trusts than they would otherwise have had. However, the provisions of the *VTA* were built into the *ITL*. As a consequence, the court can now vary a CIT on behalf of beneficiaries such as mentally handicapped persons or unborn children, provided that no material adversity accrues to other interested persons.

#### f. Confidentiality and disclosure

Trustees have a duty in equity to provide, when requested by a beneficiary, trust documentation such as the terms of the trust, particulars of trust property and accounts. Trustees also have a duty in equity to keep the trust's details confidential. This duty can be lifted by consent in the trust instrument.

#### g. Rights of creditors

##### *i. Transfers into trust*

Under bankruptcy law, a settlement into trust made two years before bankruptcy is void. Similarly, a settlement made up to ten years before bankruptcy, if the bankrupt cannot show that there was solvency on the bankrupt's part at the time of settlement, is void. With the establishment of CITs, it has become possible to settle property more effectively, since creditors must bring an action within two years of a settlement's commencement in order to make a qualifying claim. Also, creditors must show that a settlor was insolvent at the time of making the settlement and that a settlor intended to defraud the creditor.

##### *ii. Limitation period*

Actions to be brought against trustees must be commenced within six years of the cause of action. Where the cause of action has been concealed by fraud, the period of limitation begins to run from the time of discovery. For minors, incapacitated persons, the unborn, and beneficiaries with a future interest, the limitation period does not begin until discovery of the cause of action.

##### *iii. Rights of trustees and beneficiaries*

Trustees may be indemnified from and have lien over trust property.

### 4. COMMONLY USED LEGAL ENTITIES

Public limited companies can be incorporated, but the private limited company is the pre-eminent legal entity in Cyprus. In addition, branches of foreign companies and international partnerships are in regular use. Companies may be limited by shares or by guarantee or a combination of both.

The law governing companies is contained in *CAP113 – Companies Law* (as amended). Amendments since independence have tended to be as a result of bringing Cypriot law into harmony with EU law.

Public or private collective investment schemes taking the form of companies, unit trusts or international partnerships have grown in popularity since the introduction of legislation in 1999. Such schemes are known for their tax-efficient qualities. The Central Bank of Cyprus regulates the probity of this sector.



### a. Incorporation

Private companies take about five days to incorporate after receiving the approval of the company name, which takes another three days. Practitioners often incorporate 'shelf' companies and obtain name clearance in advance for their inventories. The checking of names is now possible online.

Incorporation occurs upon filing of the company's Memorandum and Articles of Association, confirmed by a Cypriot lawyer, but never earlier than the date given on the Company's certificate of incorporation. The documents to be filed must be written in Greek (or Turkish); however, copies in any European language may also be filed as long as they are accompanied by an affidavit confirming that they are a true translation of the Greek script.

### b. Capitalisation

The minimum share capital of private companies is CYP1,000. If a company intends to open an office in Cyprus, the current minimum is CYP10,000. At present, the maximum capital duty payable is CYP125. There are no exchange controls for foreign shareholders.

Shares in a company may be either ordinary, preference or redeemable. The rights of a particular class are set out in a company's Articles of Association.

### c. Director requirements

Before acting as director of a Cypriot company, the applicant must provide proof of identity, together with that person's name, address, nationality and occupation. A company having two or more members may have a single director that is a corporate body, provided the company's secretary is a different person. There is no such restriction for a single member company.

### d. Disclosure and other requirements

Cypriot law requires filing of financial statements and other documents with the Commissioner of Income Tax and the Registrar of Companies. The cost of an audit is comparatively low by European standards.

## 5. TAXATION

### a. Introduction and developments

Direct taxation is principally based

upon residency and charged on a resident's worldwide income. Individuals are resident in Cyprus if they spend more than 183 days in the country in a calendar year. Companies are resident if they are managed and controlled in Cyprus. A Cypriot company is not subject to Cypriot income tax on its worldwide income if it is managed and controlled outside Cyprus. Trustees must account for tax if a beneficiary of a trust is resident in Cyprus. All legal persons are liable for tax on income arising in Cyprus, subject to relief provided through tax treaties or law.

Since 1 January 2000, the estate of a deceased person is not subjected to tax; however, within six months of death, the executor must file a statement of assets and liabilities with the Commissioner of Income Taxes.

As a full member of the EU, Cyprus has implemented laws relaxing bank confidentiality in order to facilitate the automatic exchange of information about bank interest paid to individuals who are resident in other member states of the EU.

### b. Tax System

#### i. General concepts of tax liability

There are no estate, inheritance or gift taxes in Cyprus. Capital gains tax applies only to immovable property which is situated in Cyprus. Stamp duty on transactions is generally applicable. There is an annual Immovable Property Tax based on property values of 1980, along with a similar tax, in certain circumstances, upon any conveyance. Cyprus law provides for a value added tax (VAT). Also, a 'defence tax', similar to a second income tax, is payable by residents.

#### ii. Rates and exemptions

Income tax, chargeable at different rates for individuals and companies, is calculated after the deduction of expenses incurred wholly and exclusively for the purposes of a trade, occupation or profession.

Capital gains tax, at a rate of 20 per cent, is assessed only on crystallised gains on transactions of immovable properties which are situated in Cyprus. The property is taxable irrespective of whether it is owned directly or indirectly. Exemptions apply to transfers on death and

transactions between relatives up to the third degree.

VAT has cash flow implications for commercial enterprises, and is levied at 15 per cent of an invoice's value. With some exceptions, this tax is usually fully offset or reclaimed by registered enterprises so as to have no effect on profits.

Income tax on companies is levied at ten per cent of taxable profits. If foreign income tax has already been paid, it may be offset against Cypriot income tax. In many cases, there will be no further income tax to pay.

For individuals who are resident in Cyprus, taxable income is taxed at incremental rates that reach 30 per cent when taxable income moves above CYP20,000. Although dividends and interest are exempt from income tax, Cypriot residents must pay defence tax on this income at a rate of 15 per cent (see (d) below).

Companies managing ships may opt for a special tonnage tax if it is more beneficial than income tax.

#### iii. Taxable period and filing requirements

The fiscal year is the calendar year. Individuals must file tax returns by the following 30 April. Companies are required to pay in the year of assessment itself (1 August, 30 September and 31 December) based on estimates. When liability is finalised, penalties and interest may be payable.

### c. International

#### i. Non-residents shareholders and trusts for non-residents

Shareholders (including persons owning shares through nominees) and beneficiaries of trusts who are not resident in Cyprus do not pay Cypriot taxes.

#### ii. Non-resident withholding taxes

Withholding taxes of between five per cent and ten per cent are payable by non-residents on Cypriot income derived from intellectual property rights, film royalties, or entertainment and sporting activities.

#### iii. Tax treaties

Cyprus continues to implement double tax treaties and currently has over 40 in force.

### d. Other taxes

The defence tax applies only

to residents on certain kinds of passive income. Cypriot companies that are resident in Cyprus are liable at rates of 15 per cent and ten per cent on dividends and interest respectively. Where a Cypriot company qualifies for an 'international participation exemption', the defence tax on dividends is eliminated. Moreover, if the taxpayer can show that foreign income taxes have already been paid on the foreign income, a foreign tax credit would apply.

### e. Other relevant matters

Reorganisation of corporate structures may be structured to utilise exemptions from capital gains tax and stamp duty. Unutilised losses may be transferred advantageously into the surviving company.

Pensions that are pursuant to contracts of service performed abroad and are payable to individuals who are residents of Cyprus are taxed at five per cent for amounts exceeding CYP2,000.

The EU's Parent/Subsidiary Directive has reduced the number of cases of EU withholding taxes being charged on dividends when paid to Cypriot companies.

Cyprus has enacted EU directives that provide for mutual assistance in matters of criminal and civil law.

## 6. OTHER RELEVANT MATTERS

### a. Anti-money laundering rules

Cyprus' law to prevent and suppress money laundering is in compliance with the latest EU Directive 2007/97/EC and the Financial Action Task Force's revised 40 Recommendations. The third Money Laundering Directive must be on the statute book and implemented by December 2007. The new law will require:

- registration or licensing of corporate and trust service providers
- identification and verification of trust beneficiaries who are or could be entitled to 25 per cent or more of capital, and
- regular training of persons working in this area.

## 7. RESOURCES

### Websites

STEP's resources

[www.step.org](http://www.step.org)

The Central Bank of Cyprus

[www.centralbank.gov.cy](http://www.centralbank.gov.cy)