

# CYPRUS

## Law and Practice

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## 1. Tax

### 1.1 Tax Regimes

#### Direct Taxes

Cyprus has an attractive direct personal tax regime. In terms of direct (personal) taxes, the tax regime comprises of the following:

- income tax (IT);
- special defence contribution (SDC); and
- capital gains tax (CGT) with limited scope – ie, in relation to gains made as a result of the disposal of real estate in Cyprus or shares in a company which directly or indirectly owns real estate in Cyprus (and with full exceptions for transfers between close family members).

In Cyprus there is no inheritance tax (or other death tax), gift tax, wealth tax or immovable property tax (ie, real estate tax).

#### Indirect Taxes

In terms of indirect taxes, an individual may be liable to register as a taxable person for value added tax (VAT) purposes if he or she is engaged in any activity that constitutes a supply of goods and services (for VAT purposes). In addition to normal business activities, the sale of real estate may, under certain circumstances, render an individual liable to register as a taxable person for VAT purposes.

#### Tax Residency

Individuals who are tax residents in Cyprus pay IT on their worldwide income (with a maximum rate of 35%).

Individuals who are not tax residents in Cyprus are taxed on Cyprus-sourced income (eg, rental income).

Tax residency in Cyprus is determined by either of the following tests:

- The 183-day test (ie, an individual must spend 183 or more days in any one calendar year in Cyprus).
- The 60-day test (ie, an individual must spend at least 60 days in any one calendar year in Cyprus), provided he or she:
  - (a) does not spend time in any other jurisdiction for 183 or more days in any one calendar year; and
  - (b) is not, and is not treated as, a tax resident in or by any other jurisdiction;
  - (c) has a business in Cyprus and/or is employed and/or a director in a company that is tax resident in Cyprus during the relevant tax year; and
  - (d) maintains, in the relevant tax year, a permanent residence in Cyprus (owned or rented).

#### Deductions

The main (personal) deductions for IT purposes are:

- contributions to social insurance, approved provident funds, the national health system and life policies premiums (all together up to one sixth of the total gross income).
- donations to approved charities.

Profits from sale of “titles” are not subject to IT. The term “titles” includes shares, bonds, debentures, founders’ securities other securities of legal entities incorporated in Cyprus or abroad and rights thereon. This exception, in combination with the limited scope of CGT, means that individuals who trade in such titles will not be subject to any IT or CGT in Cyprus.

#### SDC

An individual who is tax resident in Cyprus and has Cyprus domicile, will be liable to SDC in respect of the following types of income:

- dividends (17%);
- (passive) interest (ie, interest earned on investment) as opposed to (active) interest income (ie, interest earned as a result of a business activity) (30%); and
- rent (reduced by 25% at the rate of 3%).

For the purposes of the SDC Law, an individual is domiciled in Cyprus if he or she has a domicile of origin or domicile of choice in Cyprus or if he or she has been a tax resident in Cyprus for at least 17 out of the 20 tax years immediately prior to the tax year of assessment.

#### CGT

The scope of CGT in Cyprus is limited. It is imposed on gains made as a result of the disposal of:

- real estate in Cyprus (which is not otherwise subject to IT); or
- shares in a company, which directly or indirectly owns real estate in Cyprus, provided that the value of the shares is at least 50% attributed to the market value of the real estate.

The tax rate is 20% on the gain, which gain is calculated as: the selling price, minus the acquisition cost (or a set value for any real estate acquired prior to 1980), minus indexation cost, minus other allowable deductions (eg, general lifetime exemption, agricultural land exemption and dwelling house exemption).

The following transfers are exempted from CGT:

- shares listed on any recognised stock exchange; and
- real estate or shares transferred by way of gift:

- (a) from parent to child;
- (b) between spouses;
- (c) between relatives up to the third degree;
- (d) from an individual to a company, where all the company's shareholders are (at the time of the gift), and continue to be for five years thereafter, members of the donor's family (ie, spouse and/or relatives up to the third degree);
- (e) by a family company, the shareholders of which are all members of the donor's family (as above) provided that the property transferred was originally acquired by the company by way of a gift and is kept by the donee for at least three years;
- (f) to approved charities; and
- (g) to the State.

## VAT

The VAT legal framework in Cyprus is fully in line with the EU framework. In addition to normal business activities which usually constitute the supply of goods and services for VAT purposes, the sale of real estate may, under certain circumstances, render an individual liable to register as a taxable person for VAT purposes. Subject to certain conditions (eg, town planning zones, the disposal (by way of sale or otherwise) of real estate for the first time (ie, no previous disposals), may be subject to VAT.

## Trusts

The Tax Commissioner in Cyprus (i) treats trusts as tax transparent (ie, trusts are not treated as tax entities) and (ii) taxes the trustee(s) as agent(s) of the beneficiaries.

As a rule, and subject to otherwise being a taxable person in Cyprus, a beneficiary of a trust is liable for any direct taxes that may be payable on income (ie, IT and SCD). A beneficiary of a trust (irrespective of tax residence), will be liable for CGT for any gain made on the disposal of real estate in Cyprus or shares in a company that directly or indirectly owns real estate in Cyprus.

By way of exception to the general rule, the settlor of the trust may be liable to tax for any income or gain attributed to a minor beneficiary.

According to applicable practice, the Tax Commissioner requires the trustee(s) to file tax returns and pay any taxes that may be payable. In practice, this may not always be the case. Beneficiaries (and the settlor) often file tax returns themselves and pay the tax due.

Unless beneficiaries have fixed rights on any income that the trust may earn, the Tax Commissioner attributes the income equally to the beneficiaries (eg, in the case of a discretionally

trust). The rules apply even if the beneficiaries do not receive any income (ie, the trustee accumulates it).

Cyprus International Trusts are afforded favourable tax treatment as long as the beneficiaries remain, at all times, tax residents abroad (or, if they ever become tax residents in Cyprus, they enjoy a non-domiciled status).

## 1.2 Stability of the Estate and Transfer Tax Laws

In Cyprus there is no inheritance tax (or other death tax), gift tax, wealth tax or immovable property tax (ie, real estate tax). CGT was introduced in 1980 with limited scope and full exceptions for transfers between close family members (see **1.1 Tax Regimes**). It is not expected that there will be any changes to this regime.

No legislative provision on tax was introduced to deal with the impact of COVID-19 (other than a provision for a deduction, for IT purposes, by real estate owners who have agreed to reduce the rent their tenants pay).

The Tax Commissioner, in consultation with professional bodies, is considering adopting a practice guidance in relation to the impact COVID-19 may have had on residency. The current proposal is in line with OECD recommendations and revolves around the principle that no individual or company (with tax residency in Cyprus) should, because of travel or other restrictions that forced any individual to stay Cyprus or abroad, be penalised by:

- being attributed a tax residency (either in Cyprus or abroad); or
- losing its tax residency.

## 1.3 Transparency and Increased Global Reporting

Cyprus has adopted many international anti-avoidance initiatives to enhance transparency, exchange of information and fair taxation. In particular:

- it has entered into more than 60 double tax treaties;
- it has adopted the Common Reporting Standard (CRS) on automatic exchange of financial account information;
- it has signed an intergovernmental agreement (IGA) with the United States for the Financial Account Tax Compliance Act (FATCA);
- it has introduced a mandatory country-by-country reporting requirement for multinational enterprise groups (MNE groups) generating consolidated annual turnover exceeding EUR750 million;
- it has transposed into domestic law all EU Directives on Administrative Co-operation and Mutual Assistance (DACs 1-5) and the European Union Anti-Tax-Avoidance Directive

- (ATAD) and, more specifically, the interest limitation rule, controlled foreign company (CFC) rule, and the general anti-abuse rule (GAAR);
- it is currently in the process of implementing the DAC amendment known as DAC6, which provides for mandatory automatic exchange of information in relation to reportable cross-border arrangements, pursuant to Directive 2011/16/EU; and
  - it has voted on the second implementation law with respect to the remaining provisions of ATAD (ie, the exit taxation provisions and the hybrid mismatch rules, which become effective on 1 January 2020 except for the reverse-hybrid mismatch provisions, which will become effective on 1 January 2022).

## 2. Succession

### 2.1 Cultural Considerations in Succession Planning

In Cyprus family businesses and family wealth were traditionally owned and controlled by the founder and the older generation, usually passing to the next generation on death.

In some cases, wealthy families transferred assets (usually real estate) to the next generation or made arrangements in order to deal with extraordinary family circumstances. In such cases, the methods adopted evolved around the principle of not relinquishing control. These methods included:

- the division of the share capital of the family business into voting and non-voting shares;
- the transfer of real estate with reservation of rights (eg, life interests); and
- the use of more sophisticated arrangements such as trusts.

In the last 15 years or so, we have seen new trends. Wealthy families are more open to the idea of organising their succession planning. Both in terms of the family business and their private assets. More and more families wish to consider options for passing the family business and wealth onto the next generation. The most common concerns evolve around:

- safeguarding the smooth operation of the business and avoiding internal conflicts;
- maintaining control of the decision-making process, both at board of directors' level and through shareholders' meetings; and
- protecting family wealth from potential future disputes (divorce and others).

### 2.2 International Planning

For the last 40 years, Cyprus has attracted international families who have set up business or home (as a main or second residence, or for retirement).

People chose, and continue to choose, to make Cyprus their home for many reasons. These include:

- quality of life (eg, weather, hospitality, extensive use of the English language, friendly local population, low crime rates, safe conditions and the low cost of living);
- the flexible legal system, which is modelled on the English legal system; and
- the stable and attractive personal tax system (ie, in Cyprus there are no death, gift or wealth taxes and CGT has limited scope with full exceptions for transfers between close family members).

In recent years other reasons have played an important role in the choice to set up a business or home or invest in Cyprus. These include:

- Cyprus's EU membership (since 2004);
- the attractive personal IT regime (eg, an individual with non-dom status may enjoy his or her worldwide investment income tax free);
- the coming into force of the EU Succession Regulation, which effectively provides the opportunity to people living in an EU member state (other than Denmark and Ireland) to regulate the succession of their worldwide assets under one system of law (by default, the law of the country of their habitual residence or by choice, the law of the country of their citizenship);
- the Cyprus Investment Programme and the Permanent Residence Programme, which provide the opportunity to individual investors to invest in Cyprus and obtain Cypriot citizenship or residence; and
- the matrimonial property regime, which is fair and reasonable and does not expose wealthy spouses to high division of property claims.

Traditionally international families with a Cyprus connection have been able to choose ways (outside the normal succession system) to organise their succession (eg, by using trusts or foundations or other similar arrangements). The Cyprus legal system either caters for such arrangements or does not restrict their use in any way, whether in Cyprus or abroad (eg, as a rule, forced heirship rules in Cyprus would not invalidate any such arrangement made during the lifetime of an individual).

## 2.3 Forced Heirship Laws

Cyprus has a mixed succession system with limited testamentary freedom and forced heirship rules.

Depending on his or her personal status (ie, whether married, with children, or single with living parents or other close relatives), every person has the right to leave by will a portion of his or her property freely (ie, to whoever or for whatever purpose he or she may choose). The rest (of his or her estate) will be divided between his or her lawful heirs equally. For example, a married person with three children may leave up to 25% of his or her estate by will (to whoever he or she wishes). The rest will be divided equally between his or her spouse and three children.

Contrary to what applies in most European countries, in Cyprus, which has a common law legal system, the heirs get the net value of the estate of a deceased (ie, debts and other obligations of the deceased are paid first).

In dealing with this topic, it is important to highlight that in Cyprus:

- there is no community property regime (ie, the property each spouse owns is his or her own property irrespective of when it was acquired); and
- it is possible to organise one's succession outside the normal succession system (eg, by using trusts, foundations and other arrangements, such as lifetime gifts), the forced heirship rules would not, as a rule, invalidate any such arrangement.

## 2.4 Marital Property

Community property is not part of Cyprus law. The matrimonial property regime in Cyprus recognises that each spouse's property is his or hers. This means that property registered to, and owned by, any of the spouses before marriage does not become joint marital property following their marriage. The rules on division of property are triggered only on divorce and such rules do not apply to all property.

Under the law applicable in Cyprus, marriage settlements or agreements for the distribution of the property of the spouses, which are concluded prior to the marriage or separation of the spouses, are not binding and the Cyprus Family Courts are bound to disregard them. In other words, in principle prenuptial or postnuptial agreements are not recognised and enforced in Cyprus. That said, a foreign judgment recognising a prenuptial or postnuptial agreement and regulating potential property claims between the spouses, subject to certain requirements being satisfied, may be recognised and enforced in Cyprus.

The division of property in divorce proceedings in Cyprus is based on a clear principle. Each spouse may claim against the other spouse only to the extent that:

- there has been an increase in the value of any property acquired after marriage (gifts are excluded); and
- that spouse has made a (monetary or non-monetary) contribution.

## EU Matrimonial Property Regulation

As of 29 January 2019, in case of divorce proceedings in Cyprus, the EU Matrimonial Property Regulation (2016/1103) forms part of the legal framework regulating the determination of the property rights of spouses with cross-border or international connections.

The Regulation aims to establish a unified legal framework in the EU for determining the jurisdiction and the law applicable to matrimonial property regimes. It applies to legal proceedings instituted on or after 29 January 2019 or to court settlements approved or concluded on or after 29 January 2019 (irrespective of when the proceedings were instituted). It provides for a universal application and establishes that the applicable law designated shall be applied whether or not it is the law of an EU member state. It also provides for unity of the applicable law and that the designated applicable law will apply to all assets regardless of where they are located. As a result of the Regulation coming into force in Cyprus, where applicable, prenuptial or postnuptial agreements may now be recognised and enforced by Cyprus Courts.

## 2.5 Transfer of Property

In the absence of wealth, death or gift taxes; the limited scope of CGT; the full exemption from CGT of gifts of real estate or shares in a company – that directly or indirectly owns real estate – between close family members, death or lifetime gifts and transfers between close family members, do not affect the cost basis and do not give rise to any tax issues or concerns.

In cases of gifts of real estate or shares in a company, which directly or indirectly owns real estate between close family members, the cost basis will remain the same (ie, the cost base of the donor). If the donee sells at a later point, the donor's base cost will be taken into consideration. For example, if a father acquires a plot of real estate in 1990 for EUR1,000 and transfers it by way of gift to his son in 2005, that transfer does not give rise to any CGT. If the son later sells the plot (say in 2010) for EUR€7,000, his base cost will be (the donor's original cost of) EUR1,000.

There is one exception to the above rule about the cost base, namely where an individual who is a sole trader transfers an

asset, which forms part of his or her stock, by way of gift to a family member. For example, if an individual who is trading in real estate in 2010 transfers a piece of real estate which he acquired in 1990 to his daughter he will be treated as disposing the same at its market value (in 2010) and not his cost base. The cost base for the daughter (in respect of any subsequent sale) will be the 2010 market value of the plot.

## 2.6 Transfer of Assets: Vehicle and Planning Mechanisms

Because tax considerations do not arise in such cases (see **1.1 Tax Regimes**), passing property on death and outright lifetime gifts are the main forms that the transfer of assets takes. Trusts, foundations and other similar arrangements in some cases, are also common methods of transferring property to the next generation.

## 2.7 Transfer of Assets: Digital Assets

There is no legal framework expressly regulating the succession of digital assets in Cyprus. To the extent that such assets constitute property (eg, cryptocurrency) and/or may be recognised as constituting property (eg, because they have value), they will form part of a deceased's estate. Accordingly, the normal succession rules will apply and such assets, when identified and collected by the administrator of the deceased's estate, will be divided between the lawful heirs.

Subject to the above, the contracts, if any, between the deceased and any third person in respect of any such digital asset or digital right, may also be relevant: Do such contracts provide that digital assets or rights are personal? Do they restrict transfer or transmission? Do they make any other special provisions?

## 3. Trusts, Foundations and Similar Entities

### 3.1 Types of Trusts, Foundations or Similar Entities

The Cyprus legal system recognises trusts, the relevant legal framework is comprised of:

- the principles of equity, which form, together with common law, part of the Cyprus legal system;
- the Trustees Law (Cap 193), which, is modelled on the English Trustee Act of 1925; and
- the International Trusts Law (the CIT Law).

The CIT Law was introduced in 1992 and was substantially amended in 2012. The CIT Law was introduced to offer international families the opportunity to create trusts with very attractive and advantageous features (eg, no perpetuity period,

recognised statutory right of the settlor to reserve powers, firewall provisions, and a limitation period on bringing legal action challenging the validity of a CIT).

### Trusts

Generally speaking, there are two types of private trusts; fixed trusts and discretionary trusts.

#### *Fixed trust*

Under a fixed trust the interests of the beneficiaries are fixed. The document creating the trust expressly defines the rights and interests of the beneficiaries (eg, when the trust property and/or the income thereof is to be distributed to them). This type of trust is more suitable when the settlor has a clear idea of what his or her wishes and intentions are, where flexibility to adjust depending on changing needs and circumstances is not required, where the settlor wishes to benefit a person during his or her life (eg, his or her spouse), or where there are no asset protection concerns.

#### *Discretionary trust*

Under a discretionary trust there is a class of persons (ie, the (potential) beneficiaries) who do not have any fixed or other ascertained rights and interests in the trust property. The trustees have the discretion to pay or use the trust property and the income thereof to or for the benefit of any (potential) beneficiary or beneficiaries. Under a discretionary trust, the trustees have the power to decide who (if any) gets what and when. No (potential) beneficiary can claim as of right to be paid the trust property or its income or any part of it. This type of trust is more suitable when the settlor wishes to have flexibility to adjust depending on changing and future needs and circumstances or when there are asset protection concerns.

#### *Protective trust*

A protective trust is a very attractive combination of fixed and discretionary trusts. A protective trust is created as a fixed trust, normally with one principal beneficiary enjoying the income of the trust. Such a trust is automatically converted into a discretionary trust upon the happening of predefined events (eg, a matrimonial dispute). Such events may be any of a list of such events that are defined in the law or any that the settlor may chose. A protective trust is more suitable when the settlor has a clear idea of what his or her wishes and intentions are but at the same time wishes to put in place an asset protection arrangement.

### Foundations

In Cyprus currently there is no legal framework for private foundations (the law currently provides for non-profit/charitable foundations). A bill to introduce private foundations is currently under review. That said, local and international

families with a Cyprus connection have traditionally used foundations governed by foreign law to regulate succession.

### **Companies Limited by Guarantee**

Companies limited by guarantee (CLG) may provide a very attractive alternative to trusts and foundations and may provide increased asset protection comfort where required because of their nature. The main features of CLGs, which are regulated by the Companies Law, are:

- limited liability for members up to the amount they undertake to pay in the event of winding up (it may be nominal);
- members not having a property right (ie, membership is not transferable or transmissible and cannot be charged or attacked by third parties);
- easy entry and exit in the company;
- no capital being required;
- double tax treaty (DTT) protection; and
- that they may be used as an alternative to trusts or foundations, and similar mechanisms may be put in place restricting or extending rights (eg, as to management and distributions).

### **3.2 Recognition of Trusts**

The Cyprus legal system is modelled on the English legal system. English law (in terms of common law and equity) is an important part of the legal system. English (and other commonwealth) judicial precedent is of persuasive authority and Cyprus courts follow and apply such judgments when there is no Cyprus judicial authority on the point. Cyprus is a signatory to, and has ratified, the Hague Convention on the Law Applicable to Trusts.

### **3.3 Tax Considerations: Fiduciary or Beneficiary Designation**

As explained in 1.1 **Tax Regimes**, trusts are transparent for tax purposes in Cyprus. In terms of IT, the crucial test for the tax treatment of any income is the tax residency of the beneficiaries. In terms of CGT, the crucial test for the tax treatment of any capital gain is the location of the real estate; it must be in Cyprus.

Accordingly:

- a beneficiary of a foreign trust who is tax resident in Cyprus will be taxed in Cyprus on any trust income he or she receives or that is attributed to him or her (the same way he or she would have been taxed had the trust been a Cyprus trust);
- a beneficiary of a (Cyprus or foreign) trust, irrespective of his or her tax residence, will be liable for CGT for any gain made on the disposal of real estate situated in Cyprus or

shares in a company that directly or indirectly owns real estate situated in Cyprus; and

- subject to the above, the residency of the trustee of a foreign trust will not give rise to any tax considerations in Cyprus.

In principle, the dual capacity of a settlor or donor or of any beneficiary as a trustee or other fiduciary of a foreign trust or foundation or similar arrangement, will not in itself, give rise to any tax considerations in Cyprus.

In the case of a foreign foundation or similar arrangement, where the structure has a separate legal personality and the fiduciary (whether the donor and/or beneficiary or a third person) is tax resident in Cyprus and effectively manages and controls the structure, tax implications may arise in Cyprus.

### **3.4 Exercising Control over Irrevocable Planning Vehicles**

In 2012, the CIT Law was materially amended. One major change introduced was the codification into a statutory right, of the right of a settlor of a trust to reserve certain powers. The changes introduced went far beyond the powers to revoke the trust, or require the trustees to obtain the settlor's consent in special circumstances, or to appoint and remove trustees and protectors, which were traditionally reserved by settlors. The changes include far-reaching powers such as:

- to revoke or amend the terms of the trust;
- to instruct the trustees to make payments and distributions of trust property;
- to give binding directions to the trustees in connection with the purchase, retention, sale, management, lending, pledging or charging of the trust property or the exercise of any powers or rights arising from such property;
- to appoint or remove any trustee, enforcer, protector or beneficiary, or any investment manager or investment adviser; and
- to change the applicable law or the forum of administration of the trust.

The CIT Law expressly provides that the reservation by, or granting to, the settlor of any right or interest to the trust property or any of the above powers shall not in any way affect the validity of the trust nor delay the execution of the trust. That said, it is strongly advisable that these powers should seldom be used in order to avoid claims and/or challenges as regards the validity of the trust.



## 4. Family Business Planning

### 4.1 Asset Protection

#### Trusts

Trusts have traditionally been used to plan for asset protection, not only against the risk of third-party claims, especially to protect venerable people such as the elderly, those with special needs or circumstances, or minors or spendthrift persons.

In particular, discretionary trusts and the (statutory) form of protective trusts provide excellent asset protection opportunities. Discretionary trusts by reason of the beneficiaries not having ascertained (fixed) rights over the trust property; protective trusts by reason of being converted into discretionary trusts upon the happening of certain events. Such events are expressly defined by statute (eg, the event of bankruptcy of the beneficiary) or may be expressly provided in the trust deed (eg, a third-party claim against the beneficiary. There is no limitation as to the events that may trigger the conversion of a protective trust into a discretionary trust (as long as such events are lawful and do not violate public policy principles). The other important qualification to make is that a person cannot create a protective trust for him or herself.

The CIT Law expressly limits the grounds to challenge the validity of a CIT or the transfer of property to the trustee(s) to just one single ground: the defrauding of the creditor. A person who wishes to challenge a CIT in Cyprus must bring a legal action within two years from the transfer of the property to the trustee(s) and prove that the trust was set up to defraud him or her.

#### CLGs

The Cyprus legal system provides another excellent succession planning option, which may very well cater for asset protection concerns. Both in terms of the assets and the interests of the intended beneficiaries. Companies limited by guarantee (CLGs) cater for both in that:

- any assets that the donor will transfer to the CLG will become the property of the company; and
- the membership in a CLG does not constitute property, it is therefore in principle not transferable, transmissible or chargeable and cannot be the subject matter of attack by a third party.

### 4.2 Succession Planning

As already stated, the transfer of a family business or private wealth to the next generation does not, in principle, give rise to any tax implications or considerations in Cyprus. In such cases the main considerations include:

- safeguarding the smooth operation of the business and avoiding internal conflicts;
- maintaining control of the decision-making process at board of directors' level and shareholders' meetings; and
- protecting family wealth from potential future disputes (eg, divorce).

The following are some (but not all) of the main mechanisms used in family business succession planning:

- life directorships;
- veto rights;
- division of share capital into voting and not voting shares;
- use of increased or weighted voting rights and majorities;
- use of draconian share(s), those with a predetermined evolution (eg, from founder to a first designated member of the next generation and subject to a second designated person of the next generation and so on, until all family members reach a certain age or upon the occurrence of a specific event);
- admission as shareholder(s) and/or appointment as director(s) of non-family trusted person(s) who provide wisdom and useful insights to the decision-making processes and, where required, may tip the balance to avoid or solve deadlocks;
- decision-making on major issues following consultation with wise/trusted advisors whose advice may be binding if no decision can otherwise be made; and
- arrangements whereby all or some members of the next generation may serve by rotation as CEOs.

The following methods are usually adopted when transferring family wealth:

- outright (lifetime) gifts; and
- the use of trusts, foundations and other similar structures and arrangements.

### 4.3 Transfer of Partial Interest

In view of the fact that the transfer of shares in the family business is neutral for tax purposes, no such consideration arises. That said, if a valuation is required for any reason, the methods used take into consideration the marketability or the control of the sale shares (or lack thereof).

## 5. Wealth Disputes

### 5.1 Trends Driving Disputes

Disputes between family members in Cyprus arising out of or in relation to succession arrangements are rare. The absence of such disputes may be explained on a number of reasons. These



include the mixed succession rule system we have in Cyprus (limited testamentary freedom and force heirships rules) the right of individuals to deal with their property while alive and to act as they wish (eg, by making lifetime gifts or setting up trusts or other similar arrangements), and the absence of any community property regime.

In many cases there may be disappointed heirs and hard feelings (of course). The undue influence and duress grounds, which may be invoked to challenge the transfer or transmission of family wealth to the next generation, are seldom invoked and relied on and/or accepted in court given the difficulties of proving such claims.

The most common disputes between family members in Cyprus usually revolve around the management and control of the family business. These disputes are hotly challenged and fought, and they usually end with one side exiting the business; most often following a settlement after long and costly (uncompleted) litigation and seldom following a court order.

In recent years Cyprus has seen some high-profile court cases between members of international families, usually following hotly fought divorce proceedings elsewhere. In such cases, the claimant usually commences litigation to freeze assets constituting trust property of a CIT or other assets in Cyprus structures. The firewall and other special provisions of the CIT Law in Cyprus (eg, foreign succession and matrimonial laws are ignored) make it difficult for a claimant to successfully bring a legal action in Cyprus.

## 5.2 Mechanism for Compensation

The award of damages or other compensation by the courts in Cyprus depends on the type of claim and the grounds for claiming damages/compensation.

In a successful claim where, for example, a family member claiming that another family member received lifetime gifts from the deceased which should have been taken into account in calculating the share of the deceased's estate to which each heir is entitled, the court will award remedies to bring the heirs into the position intended by law (eg, in principle all heirs take equally (including lifetime gifts)).

In a successful matrimonial property claim, the court will award an amount equal to the contribution that the claiming spouse proves that he or she has made in the increase of the value of any property acquired after marriage (gifts and legacies excluded).

In a dispute between family members in relation to a family business, where the court orders that one side buys the other

out, the amount will usually be estimated on the basis of experts' valuation(s).

## 6. Roles and Responsibilities of Fiduciaries

### 6.1 Prevalence of Corporate Fiduciaries

Cyprus law allows the use of corporate fiduciaries to act as trustees or officers of companies or other business entities. In this section we will consider the use of corporate trustees.

In Cyprus, the provision of trustee services is regulated by statute. Trustee services may be provided:

- by regulated professionals (ie, lawyers or accountants or companies or firms owned by them), in such cases the competent authorities (ie, the regulators) are:
  - (a) the Cyprus Bar Association; and
  - (b) the Institute of Certified Public Accounts of Cyprus; and
- by persons (individuals or companies) that are licensed by the Cyprus Securities and Exchange Commission.

### Family Trusts

By way of an exemption to the above, individuals and Cyprus companies may act as trustees in what we will call family situations (ie, such individuals or companies act as trustees of family trusts and not in a professional capacity).

An individual may act as the trustee of a family trust subject to the following conditions:

- he or she is the settlor of the trust;
- where all the beneficiaries of the trust are the settlor and/or his or her spouse and/or his or her family members and/or his or her spouse's family members up to the fourth degree; or
- if appointed as such under a will.

A Cyprus company may act as the trustee of a family trust subject to all of the following conditions being satisfied:

- the company is owned exclusively by the settlor and/or his or her spouse and/or his or her family members and/or his or her spouse's family members up to the fourth degree;
- all of the beneficiaries of the trust fall within the class of the individuals referred to in the point above; and
- the company secretary is a regulated service provider or an individual resident of Cyprus.

The duties and obligations of trustees in Cyprus are not codified in a statute. As a rule, the duty of the trustee is that of the reasonable person managing their own affairs. A higher duty is expected from professionals. A professional must employ the care, skill and diligence reasonably expected of a prudent businessperson in the management of the affairs of others.

Trustees, professional and not, have compliance duties and obligations (eg, AML reporting and filings).

## 6.2 Fiduciary Liabilities

Under Cyprus Law, where trustees enter into a transaction with a third party in their capacity as trustees and disclose their trustee capacity, they will not attract any personal liability.

When loss or other damage is caused to the trust property as a result of breach of trust or any unlawful act or omission (that may give rise to liability), the trustees are liable to compensate the beneficiaries and make the loss or damage good.

Trustees in Cyprus usually require standard exoneration and exculpatory clauses in the trust deed and provisions to limit their liability. Such clauses do not cover trustees in cases of their own fraud (and in some cases, but not always, in cases of negligence).

## 6.3 Fiduciary Regulation

Under Cyprus Law, trustee powers are regulated by:

- the document creating the trust;
- the Trustee Law; and
- where applicable, the CIT Law.

Subject always to the document creating the trust and any express provisions and/or limitations:

- the Trustee Law provides a list of authorised investments which the trustee may make; and
- the CIT Law provides that the trustees of a CIT have wide powers of investment and may invest trust property as if they were absolutely entitled to it.

In practice, and in the light of the overriding duty of the trustees to always act in the best interests of the beneficiaries and act prudently to protect the trust property that the settlor has entrusted to them, when it comes to investing trust funds in securities (of any nature) in the open market, the trustees make sure that they diversify and that they engage expert investment advisers and fund managers with whom they consult or to whom they delegate their investment power.

## 6.4 Fiduciary Investment

The trustees of a Cyprus trust may hold shares in private companies or other assets which do not produce income (eg, a family home).

Under applicable law and practice:

- the trustees are not required to have an active role in managing or controlling the affairs of a (private or public) company in which they hold shares; and
- it is possible to expressly provide in the document creating the trust that the trustees have no duty, obligation or responsibility to interfere in the affairs of the company.

In properly discharging their duties, trustees in Cyprus often put in place a trust governance; follow up and monitor the affairs of the underlying company or companies; and, where necessary, take remedial action (eg, replacing a director who breaches his or her duties).

## 7. Citizenship

### 7.1 Requirements for Domicile, Residency and Citizenship

In this section we will consider the legal requirements (not the taxes) that relate to domicile, residency and citizenship under Cyprus law.

#### Domicile

Under Cyprus law, domicile is regulated in accordance with the rules applicable in England. Accordingly, Cyprus law recognises:

- the domicile of origin (ie, the domicile acquired by every person at birth), as a rule, this is the domicile of their father; and
- the domicile of choice (ie, the domicile that a person has clearly chosen (by word and/or contact) to be their domicile).

#### Residency

The question of where a person is resident may arise in a number of circumstances (eg, to determine any tax obligations or to determine the applicable law for succession purposes). In this respect different set of rules apply. For non- Cypriots who may wish to reside in Cyprus the following rules apply:

- Citizens of EU members states may freely reside in Cyprus subject to some procedural requirements being satisfied (eg, registration).
- Non-Cypriots may make Cyprus their country of residence by investing in Cyprus under the Investor Permanent

Residence Programme, this programme grants the investor and his or her family a residence permit to reside in Cyprus permanently and allows visa free travel to or from Cyprus; the required investment is in the form of a new residential property of at least EUR300,000 (other requirements include a clean criminal record and the keeping of a deposit of EUR30,000 with a local bank).

- Non-Cypriots may make Cyprus their country of temporary residence by obtaining:
  - (a) a Temporary Residence Permit (visitor's status) – such permits are issued subject to minimum requirements, which include a clean criminal record and the keeping of a deposit of EUR30,000 with a local bank; or
  - (b) a Temporary Residence Permit (employee status) – such permits are issued to persons who are directors in or are employed by a Cyprus company or to foreign employees of a Cyprus company (subject to criteria).

## Citizenship

### *Cyprus Investment Programme*

In its efforts and initiatives to encourage foreign direct investment in Cyprus, the government has introduced the Cyprus Investment Programme. Investors may acquire Cyprus citizenship under this programme subject to the following conditions:

- investing EUR2 million or EUR2.5 million in Cyprus, depending on the type of investment;
- having a clean criminal record;
- having a permanent residence permit in Cyprus and a Schengen visa;
- holding their investment(s) for at least five years from the date of their naturalisation; and
- having a permanent residence (house) worth at least EUR500,000.

Investors applying to acquire Cyprus citizenship under this programme (and their family) are subjected to very strict due diligence checks by approved service providers and by the government.

### *Citizenship through residence*

In addition to the above route, EU and non-EU citizens who legally reside in Cyprus for a required period and fulfil certain conditions and criteria are eligible to apply for Cyprus citizenship.

### **COVID-19**

The COVID pandemic has inevitably slowed down processes. The authorities in Cyprus have shown understanding and flexibility in cases where travel and other restrictions cause problems and difficulties. For example, they accept the filing

of applications without all supporting documentation. They also accept that applicants will travel to Cyprus to complete any required steps as soon as they can. No legislative or others measures (eg, formal practice directions) have been introduced or issued to deal with matters arising as a result of the pandemic and/or which affect investors who filed an application under the programmes described above.

## 7.2 Expeditious Citizenship

A person may acquire Cyprus citizenship in any of the following manners:

- by virtue of any his or her parents having Cyprus citizenship; or
- if non-Cypriot:
  - (a) by virtue of marrying a Cypriot citizen;
  - (b) by virtue of residing in Cyprus for a number of years and meeting certain other criteria;
  - (c) by exception in very exceptional cases for public interest reasons; or
  - (d) through the Cyprus Investment Programme described in **7.1 Requirements for Domicile, Residency and Citizenship**.

## 8. Planning for Minors, Adults with Disabilities and Elders

### 8.1 Special Planning Mechanisms

Trusts offer an effective way to plan for minors or adults with disabilities. There are no specific legal or other requirements and in such cases the settlor may determine the purposes and terms of the trust based on his or her own specific and personal circumstances. Check and balances may be also put in place in the form of appointing a protector (or a committee of protectors) with an oversight role and with certain powers (eg, to approve certain decisions or to provide their consent before the exercise of certain trustee powers, such as the power to sell or charge trust property).

Other planning mechanisms include the issue of a power of attorney or the making of a provision for the appointment of a guardian in a will. Both of these mechanisms are considered in

### 8.2 Appointment of Guardian.

### 8.2 Appointment of Guardian

Under Cyprus Law the parents or the living parent are/is the lawful guardian(s) of a minor. In exceptional cases where the wellbeing and safety of the minor so warrants (eg, sexual or other physical or mental abuse) the parent(s) may, by court order, be deprived of the parental guardianship.

In the case of an orphan minor (by reason of both or any of his or her parents dying), the living parent or the guardian to be appointed must administer the property of the minor subject to the supervision of the court.

Cyprus Law expressly provides that the living parent of a minor may, by will, designate who the guardian of his or her minor child or children may be. In the absence of such an arrangement, the court will appoint a guardian, usually a close family member who is fit and willing to undertake such a role.

### 8.3 Elder Law

Cyprus has long offered a significant social insurance protection net to eligible older individuals (in terms of pensions, support and other benefits). In the last couple of years, it has also introduced a National Health System, which is open to effectively all people. It has also encouraged people (by tax and other allowances) to take out life insurance policies and participate in approved private pension schemes (eg, provident funds).

The relevant applicable legal framework, which regulates situations where people are unable or incapable to act, is summarised below.

A person who is adult and capable of acting and managing his or her affairs (ie, is mentally fit), may appoint an attorney, with wide or limited authority to manage those affairs. In the event that he or she becomes incapable of acting because of unsound mind, such power of attorney is revoked.

In the case of a person who is incapable of acting and managing his or her affairs, because of mental disorder, drug addiction, alcoholism, or brain or other physical damage or disease or illness, an administrator may be appointed. This administrator is accountable and must report to the court at regular intervals. An administrator in such cases is appointed at the application of any parent, child or other relative or person who has a legitimate interest. The administrator has the following powers and duties:

- To administer and manage the incapacitated person's estate and affairs.
- To use the property and income of the incapacitated person to financially provide for him or her, his or her family and any other person or purpose for whom or which it was expected that the incapacitated person would provide is he or she were not incapacitated.

Cyprus has ratified the Hague Convention on the International Protection of Adults which provides a unified mechanism of protecting adults who are unable to protect their interests by reason of an impairment or insufficiency of their personal

faculties. Accordingly, Cypriots who have an international connection with countries that have also ratified this Convention and foreigners who have a Cyprus connection, may issue lasting powers of attorney to their attorneys to deal with their affairs following their incapacity. Such powers of attorney will be recognised and be given full effect in Cyprus where applicable.

## 9. Planning for Non-traditional Families

### 9.1 Children

Cyprus has adopted an extensive legal framework regulating the rights and wellbeing of children and has signed and ratified various relevant international treaties related to the subject. In short, it can be said that the law does not discriminate against any category of children.

The paternity of a child born out of wedlock can be established either by voluntary acknowledgement or by a court order. The mother and the child have the right to apply to court for acknowledgement of paternity (within five years after the birth). Once voluntarily or formally (by court) recognised, the child has, from birth, the same rights as if he or she were born in marriage.

An adopted child will be considered for all purposes as the legal and the natural child of the adoptive parents and in no case will be deemed to be the child of any other person. Adoption is effected by a court order and following strict legal procedures.

Surrogacy arrangements are legal and regulated in Cyprus. Couples and single persons are allowed to use a surrogate mother to carry their child if they are unable to have children of their own provided that they obtain a court order and the prior approval of the Council of Medical Assistance Reproduction in Cyprus (the Council). A child born as a result of surrogacy arrangements will be considered for all purposes as the legal and the natural child of the couple or person who used this process and in no case will be deemed to be the child of any other person.

The use of cryopreserved embryos is allowed. Such embryos may be used after six, and within 18, months after the death of the person having an interest provided, he or she gave written consent prior to death and the Council has granted the required approval. In such cases, Cyprus Law does not make an express provision as to whether the child will be recognised or considered as the legitimate child of the deceased parent or whether he or she will be entitled to benefit from his or her deceased parent's estate. Presumably, a person in the position of a guardian of such child, will apply in court for recognition.

Cyprus Law has long recognised the succession rights of children born after the death of their father (they have full succession rights).

## 9.2 Same-Sex Marriage

Same-sex marriages are not recognised in Cyprus.

Domestic partnerships (between same sex persons or not) are not recognised in Cyprus. If two partners live together and would like to provide for each other after their death or during their life or to enjoy increased rights they have two options:

- they may enter into a formal (registered) civil partnership/union; or
- they may consider setting up a trust (to avoid the forced heirship rules which would otherwise apply in case of death).

Civil partnership/unions between persons (including civil unions between people of the same sex) are recognised in Cyprus. Civil partnership/union partners are able to enjoy the same rights as a married couple except the right to adopt. Unless other arrangements are made, such persons have the same rights of succession or to the division of property in case of separation.

## 10. Charitable Planning

### 10.1 Charitable Giving

The Cyprus tax regime encourages charitable giving, by making the whole amount of a donation to an approved charity deductible from the gross income of an individual for IT purposes.

Furthermore, any gifts to approved charities are also exempted from CGT, where applicable (ie, gifts of real estate in Cyprus or of shares in a company that owns, directly or indirectly, real estate in Cyprus).

### 10.2 Common Charitable Structures

Under the applicable law and practice in Cyprus, a charity may take the form of a foundation, an association, a company limited by guarantee (CLG) or a trust. A foundation is, generally speaking, more commonly used for charity purposes in Cyprus than any other form.

A foundation is an orphan entity in terms of ownership. It has a separate legal personality. It may be set up by a founder and must be approved by the competent authority. It is regulated by Law and its constituent documents (ie, its memorandum and articles of association). It has reporting, filing and other compliance obligations and must prepare audited financial statements.

An association must have at least 20 members. It has a separate legal personality. It may be used for philanthropy although it is usually used for recreational set ups (eg, a club or the pursuit of common interests of a group) rather than for charitable purposes. It has reporting, filing and other compliance obligations.

A CLG must have at least one member (and being a company regulated by the Companies Law of Cyprus has a separate legal personality by default). It may be used for philanthropy although it is usually used for professional bodies or associations. It has the same reporting, filing and other compliance obligations as all companies in Cyprus.

Charitable trusts may also be used in Cyprus. By their nature they do not have, but may obtain legal personality status. They have reporting, filing and other compliance obligations.

In terms of compliance and administration, a foundation or a trust would be easier to operate and administer compared to an association or a CLG.

# CYPRUS TRENDS AND DEVELOPMENTS

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## Trends and Developments

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### Introduction

For the last 40 years, Cyprus has been an attractive jurisdiction for both businesses and individuals to set up presence or home. People chose and continue to choose Cyprus for many reasons, some of which are set out below.

Quality of life (eg, weather, hospitality, extensive use of the English language, friendly local population, low crime rates, safe conditions, and the low cost of living).

The excellent professional services sector (eg, well-educated, highly trained, solution-oriented professionals who have local knowledge and global reach and who have either gained international working experience before returning to Cyprus or work for international network firms).

The flexible legal system which is modelled on the English legal system. Traditionally, local and international families with a Cyprus connection have been able to choose ways outside the normal succession system to organise their succession (eg, by using trusts or foundations or other similar arrangements). The Cyprus legal system caters for such arrangements and does not restrict in any way the use of them (whether in Cyprus or abroad). As a rule, forced heirship rules in Cyprus would not invalidate any such arrangement made during the lifetime of an individual.

The stable and attractive personal tax system. In Cyprus there are no death, gift or wealth taxes and capital gain tax has limited scope with full exemptions for transfers between close family members. The income tax regime offers international families the opportunity to enjoy their worldwide investment income tax free.

Cyprus is also an EU member state.

### Developments

Cyprus follows global trends and developments and is continually, amending or introducing legislation (as may be required) to align with international best standards and practices; in particular, as regards transparency, AML and abusive tax practices. At the same time, Cyprus amends existing, and introduces and adopts new, legislation to attract international families (and businesses) to Cyprus.

In recent years Cyprus has introduced or adopted, and/or is in the process of implementing, the following new legislation and/or legal frameworks:

- The new tax residency regime (ie, the 60-day test).
- The new non-dom regime, a regime for people with a foreign domicile who may enjoy their worldwide investment income tax free.
- The Cyprus Investment Programme and the Cyprus Residency Programme, which provide foreign investors with the opportunity to obtain Cyprus citizenship or residency subject to satisfying very strict investment and personal criteria.
- The EU Succession Regulation, which effectively provides the opportunity to people living in any EU member state (other than Denmark and Ireland) to regulate the succession of their worldwide assets under one system of law; by default, the law of the country of their habitual residence or, by choice, the law of the country of their citizenship.
- The EU Matrimonial Property Regulation, which effectively provides the opportunity to people living in an EU member state to regulate what happens to their worldwide assets in case of divorce or separation under one system of law or by virtue of a contract (ie, a prenuptial or postnuptial agreement).
- The Hague Convention on the Law Applicable to Trusts.
- The EU General Data Protection Regulation.
- The Hague Convention on the International Protection of Adults, which provides a unified mechanism of protecting adults that are unable to protect their interests by reason of an impairment or insufficiency of their personal faculties and under which lasting powers of attorney are recognised and be given full effect in Cyprus where applicable.
- The recognition by statute of the settlor's right to reserve powers when creating a trust and the introduction of new extensive reserved powers.
- The consolidation into one piece of legislation of legal structures or arrangements that may be used for philanthropy.
- The publication of a bill to introduce private foundations in Cyprus.
- The adoption of the Common Reporting Standard (CRS) on automatic exchange of financial account information.



# CYPRUS TRENDS AND DEVELOPMENTS

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- The signing and ratification of an intergovernmental agreement (IGA) with the United States for the Financial Account Tax Compliance Act (FATCA).
- The introduction of mandatory country-by-country reporting requirement for multinational enterprise groups generating consolidated annual turnover exceeding EUR750 million.
- The introduction into domestic law of all EU Directives on Administrative Co-operation and Mutual Assistance (DACs 1-5) and the European Union Anti-Tax-Avoidance Directive (ATAD) and, more specifically, the interest limitation rule, the controlled foreign company (CFC) rule, and the general anti-abuse rule (GAAR); currently, Cyprus is in the process of implementing:

- (a) the DAC amendment known as DAC6, which provides for mandatory automatic exchange of information in relation to reportable cross-border arrangements; and
- (b) the remaining provisions of ATAD.

## • Trends

Creating, increasing and preserving wealth in a tax efficient manner was, for many years, the primary focus of entrepreneurs and wealthy families. During the last 20-25 years there has been a shift of focus. Not only preserving, but also passing wealth onto the next generation and using that wealth in a socially responsible manner have become the primary focuses.

Families in Cyprus (local and international) are considering early, and in consultation with their professional advisers, their succession and estate planning. In this process tax is always on the agenda but is not the only consideration. In Cyprus there are no wealth, death or gift taxes and capital gains tax has a limited scope with full exemptions for transfers between close family members. The interests, concerns, objectives, wishes and ideas of families when considering their succession and estate planning – both at family business level and for the private assets – revolve around other considerations. These are considered in the following paragraphs.

### *Estate-planning concerns*

For example, when people consider death or incapacity (or other extraordinary set of circumstances that cause concern), the legal and other complications that may arise in such an eventuality need to be contemplated. Questions around these issues include:

- What happens to the ownership and management of assets pending completion, of during or after the administration process?
- Who holds and manages the assets?

- Will such person(s) be recognised in all countries where assets are situated?
- What happens with any underlying assets (eg, the business)?
- Who will exercise the voting or management powers and how will this be done?
- Are the assets protected from heirs/third party claims?
- What about the rights/powers of minors?
- Are the minors' assets subject to court supervision?

### *Estate-planning alternatives*

In Cyprus, trusts and other set ups (eg, companies limited by guarantee), may provide a very attractive alternative option to succession and estate planning and may be used to plan for undesirable events such as death and incapacity (as well as many other sets of circumstances) and may accommodate the special and different needs and requirements of every family. It should be added that an individual with a Cyprus and an international connection may freely use foreign foundations or other similar arrangements commonly used in Europe to organise his or her affairs.

### *New estate-planning considerations*

In Cyprus in recent years we have seen that when clients consider their succession and estate planning they wish to consider and cater for a wider range of issues: These include:

- How to safeguard against substance abuse.
- Best investment practices and policies and how to encourage investment in environmentally friendly, technology-driven and socially responsible firms and in start-ups or other innovative outward and future-looking firms.
- How to educate, involve and make the next generation accountable in the management of the family wealth.
- What mechanisms may be put in place to know where the assets are situated and who has access and information to or in relation to them.
- How to cater for the risks involved in potential divorce proceedings.
- How to cater for economic, geopolitical and other risks and exit a jurisdiction if required.
- How to finance litigation or major needs in case of assets being subject to freezing orders.
- How to bring together or keep apart (if this is in the best interest of all) children from second or third marriages.
- How to cater for the old age in the light of the demographic changes.
- How to cater for extraordinary events such as going missing while travelling, diving or climbing, or in case of kidnapping.
- How to keep, in a world of almost full transparency, the family affairs private and confidential.

- What to provide for in a family constitution, which have become very popular in recent times, and how to deal with soft or hot issues like family mission and vision, family values, family governance, use of family assets (in particular luxury assets such as art, classic cars, yachts, planes and holiday homes), employment in the family business and compensating family members who exit.

## **Conclusion**

International and wealthy families live in a modern world full of challenges. These include volatility, uncertainty, complexity and ambiguity in both the global economy and geopolitics; an increased focus on transparency, which in many cases infringes on legitimate rights and desired levels of privacy; the shifting of public opinion to extremes; populist politicians; and social media. In the light of these challenges, clients want solutions tailored to their needs and concerns. For the last 40 years, Cyprus has established a proven record as a jurisdiction that attracts businesses and individuals who wish to set up a presence or home here and has provided and continues to provide excellent structure and succession planning opportunities and solutions.

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