

Trends and Issues in Economic Relations of Cyprus and Russia

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Abstract

Relations between the USSR and the Republic of Cyprus have been maintained since 18 August 1960, and on 7 April 1992, Cyprus recognised Russia as the legal successor of the Soviet Union. Since then, the relations between the two countries in economic, political and cultural spheres have been actively developing. This study will analyse the economic relations between Russia and Cyprus at the present time, both in the macro, as well as in the company levels. On the one hand, Russia and Cyprus remain important partners for the mutual development of national economies, while on the other hand, there is a significant outflow of Russian capital from Cyprus, which can be described as a new negative trend in bilateral cooperation.

Keywords: double taxation, automatic exchange of information, tax resident, Multilateral Competent Authority Agreement (MCAA), economic cooperation, Russia and Cyprus relations, tax planning

Legal Basis of the Economic Relations between Russia and Cyprus

The fundamental basis of economic relations between Russia and Cyprus is the agreement between the Government of the Russian Federation and the Government of the Republic of Cyprus for the avoidance of double taxation with respect to taxes on income and capital, which was signed on 5 December 1998 (often referred

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to as the Double Tax Treaty or DTT). However, there were certain problems related to the fact that the tax authorities of the Russian Federation did not receive the required information in full. In this regard, negotiations were held on the DTT between Cyprus and Russia, which ended on 16 April 2009, and resulted in a protocol amending the agreement signed on 7 October 2010 in Nicosia, during the visit of the President of the Russian Federation to Cyprus. The State Duma sanctioned and promulgated the agreement on 15 February 2012, the Federation Council approved it on 22 February, and President Dmitry Medvedev ratified it on 29 February 2012. According to the statements of official representatives of State bodies of Russia and Cyprus, this protocol should promote the development of international business and contribute to the further development of economic relations between Russia and Cyprus.²

Nevertheless, the main result, in the authors' opinion, is that, due to the signing and ratification of the protocol, Cyprus was excluded from Russia's Ministry of Finance's 'black list', and therefore dividends distributed by Cypriot companies are exempt from Russian taxation under the rebate the Russian Federation provides in the tax code on the release of income from strategic participation. Such an amendment should make Cyprus a more attractive jurisdiction to be used in structuring Russian investments abroad.

Many of the amendments to the agreement specify the exemption and do not deprive the Cyprus resident companies of the benefits that the Double Tax Treaty provides to them. What are the main amendments?

1. The effect of the article on dividend taxation was extended to payments on shares of joint investment funds or similar forms of collective investment. As for other changes in the taxation of interest and dividends, insignificant changes have taken place, in particular, to reduce the taxation rate at source to 5% when taxing dividend payments, and the contribution to the charter capital should be EUR100,000 (previously USD100,000). Upon the Protocol entering into force, any interest that is a result of the 'thin capitalisation' rules is recognised as dividend for tax purposes under Russian law, and will be subject to taxation at the rates stipulated by the agreement for dividends (5-10% instead of 0%).

² See Demetris Ch. Demetriades LLC 'Cyprus-Russia Tax Treaty Protocol', Nicosia: Demetris Ch. Demetriades LLC (2017, November 24), available at: <https://www.ddlegal.co/2017/11/24/cyprus-russia-tax-treaty-protocol>, accessed 22 Feb. 2019; Russia-Cyprus talks. (2017). President of Russia official web page, available at <http://en.kremlin.ru/events/president/news/55910>, accessed 22 Feb. 2019.

2. The article on the taxation of income from alienation of property has been substantially amended. Thus, according to these changes, when disposing shares of a company, where 50% of the value of assets is real estate, income from such a sale may be taxed in the State where the property is located. This rule, however, will not be applied to cases when a company is reorganised or when shares are alienated on recognised stock exchanges, as well as by the pension fund and the governments of Cyprus and the Russian Federation. The changes were to come into force on 1 January 2014. However, the provisions of clause 4 are not applicable to income from the alienation of shares if the recipient is a pension fund, a provident fund, or the government of the contracting State.

At the same time, on 29 December 2016, Cyprus' Ministry of Finance published a message that an agreement was reached between the competent authorities of Russia and Cyprus to postpone the application of the new version of this article. It was also reported that the approval of the draft of an additional protocol is being completed, and it was announced that the new version will not be applied until similar provisions are included in other double tax treaties between Russia and European countries. Russia's Ministry of Finance has not commented on the message of its Cypriot counterpart. It should be noted that the international treaty concluded by the Russian Federation cannot be modified, and its effect cannot be postponed by an agreement between the competent authorities, a memorandum of understanding, a presidential decree, or other regulatory legal act. Such postponement is only possible after the sanction of the international instrument by means of the adoption of an appropriate federal law) its ratification, and entry into force. Usually such procedures in Russia take three to six months.

3. Income from real estate will be taxed in the State according to where it is located, as was the case before. However, the provisions of this article are also extended to mutual funds, which are created solely for the purpose of investing in real estate.

4. The agreement is amended by article 29, which aims to limit the benefits provided by it. According to this provision, if, as a result of consultations between the competent authorities of both contracting States, it is established that the main purpose or one of the main goals of establishing or operating a residency was to obtain benefits under the agreement that would otherwise not be available, and such a company is registered in third countries (not in the territory of the Republic of Cyprus or Russia), it will not be able to use the benefits. Article 29 will affect com-

panies that are registered in third countries but are managed and controlled from the territory of the Republic of Cyprus, which makes it possible to apply for resident status and, therefore, to use the advantages of the agreement.

5. The protocol provides for new rules on how to determine a company's residence. Namely, if it is impossible to determine the place of effective management of a legal entity, the State agencies of Russia and Cyprus will decide the issue of such residence in each specific case by conducting conciliation procedures.

6. In addition, the concept of permanent establishment has been expanded. According to the new regulations, if a company acts on the territory of another contracting State through an individual who stays in the territory of a foreign State for 183 or more days within 12 months, such a company may have a permanent establishment in that State. This can have serious consequences in relation to taxation. In this regard, so as not to allow the emergence of a permanent establishment, the use of general powers of attorney for making certain transactions in the territory of the Russian Federation should be avoided.

7. Another important change is the new revision of article 27 of the agreement, on mutual assistance in tax collection, which has become more specific. In particular, the issues of the imposition of interim measures were resolved, the definition of the concept of a tax order was given, etc.

8. Important changes in the protocol deal with the provisions on information exchange. It should be noted that the protocol does not specify what kind of information the competent authorities of the respective countries can exchange; it indicates only information 'that can be considered essential for applying the provisions of the agreement or for administering and applying domestic legislation in respect of taxes of any kind or name'. In fact, these changes are aimed at a certain specification of the already existing article of the agreement and will not entail any major changes in the sphere of confidentiality of information. At the same time, it should be borne in mind that this conclusion stems from a strictly formal assessment of the new and current revisions of this article. Time will show how relations in the field of information exchange between the Russian Federation and Cyprus will develop in practice. In any case, the meaning of this article has not changed simultaneously with the text.

However, despite the above-mentioned changes, the use of Cypriot companies retains huge preferences as a tool for tax planning. We would also like to note that

the main goal of the amendments to the existing agreement is to prevent tax evasion and abuse of the DTT conditions, and to demonstrate the willingness of the Russian authorities to focus on the existence of real commercial goals in international structures.

The main areas of economic cooperation between Russia and Cyprus

The most important area of economic cooperation between the two countries is tourism. Russian tourists traditionally rank second after the UK in the total number of arrivals in Cyprus. Since 2010, the tourist flow from the Russian Federation increased from 224,000 people in 2010 to 784,000 people in 2018 (Table 1). The share of Russian tourists increased during this period from 10% of the total number of tourists to 20%, while the share of tourists from UK declined from 46% to 34%.

Table 1: Arrivals of Tourists to Cyprus by Country of Usual Residence and Residents of Cyprus Travelling Abroad in 2010-2018, *thousands*

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Arrivals of Tourists to Cyprus by Country of Usual Residence									
All Countries	2173	2392	2465	2405	2441	2659	3187	3652	3939
United Kingdom	996	1021	959	891	872	1041	1158	1254	1328
Share of UK in total	46%	43%	39%	37%	36%	39%	36%	34%	34%
Russia	224	334	474	609	637	525	782	824	784
Share of Russia in total	10%	14%	19%	25%	26%	20%	25%	23%	20%
Residents of Cyprus Travelling Abroad									
All Countries	1246	1209	1194	1115	1209	1119	1268	1407	1446
Greece	429	395	411	360	452	466	539	538	540
Share of Greece in total	34%	33%	34%	32%	37%	42%	43%	38%	37%
United Kingdom	298	304	311	310	286	187	218	261	215
Share of UK in total	24%	25%	26%	28%	24%	17%	17%	19%	15%
Russia	55	56	51	56	56	48	59	67	74
Share of Russia in total	4%	5%	4%	5%	5%	4%	5%	5%	5%

Source: Compiled by the authors from data provided from the Statistical Service of Cyprus (CYSTAT) (2019a) Arrivals of Tourists by Country of Usual Residence and the Statistical Service of Cyprus (CYSTAT) (2019b) Residents of Cyprus Travelling Abroad.

As for Cypriot citizens, it turned out that, after travelling to the traditional destinations of Greece and the UK, Russia was the third most popular destination (Table 1). First of all, intensive business and investment cooperation led the country to third place i.e., the majority of large Cypriot companies in Russia have partners, and medium and small-sized businesses regard the Russian Federation as a source of clients and tourists, and therefore these companies regularly take part in conferences, exhibitions, working meetings, and they maintain close relationships with existing and potential customers.

The volume of bilateral trade, unfortunately, is insignificant and, in recent years, it has tended to decline. According to the Rosstat of the Russian Federation, in 2000, the trade turnover between the two countries amounted to USD1,8 billion, in 2010 reflected USD1,7 billion, and in 2017 only USD314 million. In the total volume of Russia's trade with non-CIS countries, the share of Cyprus decreased from 2% in 2000 to 0.1% in 2017. (See Table 2) The reasons for this situation are the 2013 financial crisis in Cyprus, the EU's anti-Russian sanctions related to the situation in Ukraine and the countermeasures of the Russian Federation in 2014.

Table 2: Foreign Trade of The Russian Federation
with Non-CIS Countries* at current prices, million US dollars

	2000	2010	2015	2016	2017
	Exports from Russia				
Total	89269	337467	298420	247687	309688
Cyprus	1722	1641	244	289	306
Share of Cyprus **, %	1.929	0.486	0.082	0.117	0.099
	Imports to Russia				
Total	22276	197184	161693	162658	202608
Cyprus	36	27	59	52	8
Share of Cyprus **, %	0.159	0.014	0.037	0.032	0.004
	Total Turnover				
Total	111545	534651	460113	410345	512296
Cyprus	1758	1668	303	341	314
Share of Cyprus **, %	2.088	0.5	0.119	0.149	0.103

*CIS – Commonwealth of Independent States ** Share of Cyprus in total volume of exports, imports and turnover of the Russian Federation

Source: Compiled by the authors on the basis of Rosstat, *Russian Statistical Yearbook 2018*.

During the meeting of the presidents of Russia and Cyprus, organised on 24 October 2017, agreements were signed in the Kremlin concerning sea and road transport, communications, information technology and legal cooperation. Following the visit, Russia and Cyprus also signed a declaration on cooperation in the field of economic modernisation and a joint action programme between the Russian Federation and Cyprus for 2018-2020. And on 23 October 2017, the President of Cyprus met with the Prime Minister of the Russian Federation, Dmitry Medvedev. They discussed issues of energy and shipping, as well as economic cooperation between the countries as a whole. They said that Cyprus has become a very important channel for attracting direct investment from Russia. The official representative of the Government of Cyprus, Nikos Christodoulides, spoke about the total amount of accumulated direct investment figure – more than EUR140 billion, which came into the Russian economy through Cyprus.³

There are also projects for the creation and development of infrastructure facilities. Such projects include the construction of a hospital for cancer patients in Paphos, which will use modern proton technologies supplied by Russia, as well as carrying out joint work to develop innovations, including the ones in cooperation with the main Russian technological project Skolkovo.

Cooperation between Russia and Cyprus in the Financial Sector

For a long time, Cyprus has played a leading role in the inflow of direct foreign investment into Russia and in direct investment from Russia abroad. According to the data from the Central Bank of the Russian Federation, the share of Cyprus in the total accumulated volume of direct foreign investment in the Russian Federation ranged from 28% to 37% from 2010 to 2018. The total amount of accumulated Cyprus investments in the Russian Federation, at the beginning of 2018, amounted UDSD173 billion (See Table 3). Cyprus investments are mainly channelled in manufacturing, mining industry, real estate, construction, wholesale and retail, transportation and communications.

The share of Cyprus in the total accumulated volume of overseas direct foreign investment from the Russian Federation between 2010 and 2018 ranged from 31% to 41%. The total amount of accumulated investment from the Russian Federation in Cyprus amounted to USD187 billion in 2018 (see table 3). As a comparison, at

³ Russia-Cyprus talks. (2017). President of Russia official web page [online], available at: <http://en.kremlin.ru/events/president/news/55910>, accessed 22 February 2019.

Table 3: Accumulated volume of direct foreign investment from the Russian Federation abroad and in Cyprus in 2010-2018, as at the beginning of year

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Direct foreign investment in the Russian Federation									
Total amount of investment in the Russian Federation from abroad, billion US dollars	377	489	455	515	566	371	348	478	530
The amount of investment from Cyprus, billion US dollars.	130	179	136	179	194	115	99	149	173
The share of investment from Cyprus in the total amount of investment from abroad, %	34	37	30	35	34	31	28	31	33
Direct overseas investment from the Russian Federation									
Total amount of overseas investment from the Russian Federation, billion US dollars.	298	361	362	410	480	411	368	418	469
The amount of investment in Cyprus, billion US dollars.	116	150	125	151	163	126	112	150	187
The share of investment in Cyprus in the total amount of overseas investment (%)	39	41	35	37	34	31	31	36	40
The Russian Federation portfolio investment overseas									
Total amount of overseas investment from the Russian Federation, billion US dollars	36	33	38	43	51	52	65	69	69
The amount of investment in Cyprus, billion US dollars.	2	4	3	2	2	6	2	5	2
The share of investment in Cyprus in the total amount of overseas investment (%)	7	12	8	5	5	11	3	7	2

Source: Compiled by the authors according to figures from Central Bank of Russia (2019), *Statistics on International Economic Relations*.

the beginning of 2018, the amount of accumulated direct investments from Germany into the Russian economy was USD18,9 billion, and the amount of accumulated Russian investments into the German economy was USD9,3 billion.⁴

Unfortunately, in recent years the situation in the financial sector, which undoubtedly is pivotal in relations between the two countries, has begun to get worse. The new Cyprus measures to combat money laundering, as well as European and US sanctions against Russia, contribute to the outflow of Russian capital from the island.⁵

The same information is confirmed by the statistics. According to the figures of the Central Bank of Cyprus, the value of accounts owned by non-EU citizens at the end of November 2018 decreased to EUR 7,1 billion. This is a dramatic change, if we take into account that, at the end of 2012, it was EUR 21,5 billion.

There are good reasons for this. Now a world trend requires companies and individuals to show their source of income, taxes paid from them and their tax residency.⁶ In Cyprus, which is not an exception to the world trend, this situation has developed in relation to the Russians. As a result, the Central Bank puts pressure on commercial banks to close the accounts of individuals not living in Cyprus and companies that belong to such persons and / or do not have an office and employees in Cyprus. However, the main reason lies in the fact that the Russians who keep their savings in Cypriot banks may soon lose their 'hard earned' capital.

According to the new tax requirements, Russian citizens will have to report

⁴ Central Bank of Russia, *Statistics on International Economic Relations*. Central Bank of Russia (2019) [in Russian], available at: <http://www.cbr.ru/statistics/?PrId=svs>, accessed 22 Feb. 2019; A. Zhabin, E. Volkodavova and E. Nesterenko, 'The Problem of Formation of Long-Term Investment Resources Formation in the Modern Russian Economy', *International Journal of Economics and Financial Issues*, Vol 6, S. 5 (2016), pp. 166-171.

⁵ P. Tugwell and G. Georgiou, 'Cyprus No Longer Mediterranean Haven for Russian Businesses', Bloomberg.com (2019, January 10), available at: <https://www.bloomberg.com/news/articles/2019-01-10/cyprus-loses-luster-as-mediterranean-haven-for-russian-business> [Accessed 22 Feb. 2019]; N. Stamouli and D. Hinshaw, 'U.S. Takes on Russia's Favorite Money Haven: Cyprus', *The Wall Street Journal* [online], available at <https://www.wsj.com/articles/u-s-takes-on-russias-favorite-money-haven-cyprus-1538316001>, accessed 22 February 2019; J. Caytas, 'Sanctions, Real and Imaginary: Experiences with Russia in the Ukraine Crisis'. *Amsterdam Law Forum*, Vol. 9, No. 2 (2017), 26

⁶ See T. Beck C. Lin, and Y. Ma, 'Why Do Firms Evade Taxes? The Role of Information Sharing and Financial Sector Outreach', *The Journal of Finance*, Vol. 69, No. 2 (2014); N. Johannesen, and G. Zucman, 'The End of Bank Secrecy? An Evaluation of the G20 Tax Haven Crackdown', *American Economic Journal: Economic Policy*, Vol. 6, No. 1 (2014); G. Korolev and A. Levashenko, 'Modern Trends in Minimisation of Offshore Jurisdiction: OECD, G20 and Russia', *Russian Economic Developments*. No.1 (2014); S. Phua, 'Convergence in Global Tax Compliance', *Singapore Journal of Legal Studies* (2015), 77-104.

transactions, and in case they refuse, they will have to close the accounts. The bank inspectors of the island state they began checking transactions for compliance with legal requirements, and began to request individual account holders to explain the reasons for transactions over the past 15 years. In addition, they demanded Russian citizens to explain transfer of funds between their own accounts. In the near future, owners of about 150,000 qualified accounts may face similar problems.⁷

Such requirements were introduced by local banks after the representatives of the US Treasury Department visited Cyprus in 2018. They expressed the need to strengthen control over the origin of customers' funds and their transactions. The US Treasury seeks to cut off channels for criminal money transactions around the world, as well as to ensure the implementation of US sanctions.

Without exception, all Cyprus banks, which are Russians' preferred choice to store their savings, are obliged to implement the new requirements. This may lead to the citizens of the Russian Federation begin a large-scale capital withdrawal from the island. Previously, something similar happened to Latvia, where the Russians also keep huge amounts of money. After the emissaries of the US Treasury Department visited that country, its local banks ceased their relations with the Russians and the country's organisations that came under sanctions. Moreover, some banks blocked Russian assets until the history of their origin was clarified.⁸

For the US, putting pressure on offshore banking territories is a key strategy, since their existence in fact makes their sanctions policy ineffective. After all, even with the conditions of the automatic system for exchanging tax information, which started to work this spring, tracking the movement of capital and finding the ultimate beneficiaries of the activities of offshore organisations remain extremely difficult.⁹

⁷ EY, *Russia Doing Business in Cyprus 2017. Measuring Quality and Efficiency Survey Report* (Nicosia: EY, 2017), available at <https://www.ciba-cy.org/wp-content/uploads/2018/11/ey-russian-report.pdf>.

⁸ A. Antoniou, 'Cyprus Is the Real Loser in the US-Russian Economic War', *Forbes.com* [online] (2018, October 26), available at <https://www.forbes.com/sites/antonisantoniou/2018/10/26/cyprus-is-the-real-loser-in-the-us-russian-economic-war/#684dd2dc2bbc>, accessed 22 Feb. 2019; A. Antoniou, 'Has Cyprus Sided With The West, Leaving Russia Out In The Cold?' *Forbes.com* [online] (2018, November 22), available at <https://www.forbes.com/sites/antonisantoniou/2018/11/22/has-cyprus-sided-with-the-west-leaving-russia-out-in-the-cold/#5edfbb684424>, accessed 22 February 2019; E. Neocleous, 'The potential impact of Russian de-offshorization legislation on Cyprus holding and finance structures', *Trusts & Trustees*, Vol. 21, No. 6, (2015), 610–613.

⁹ J. Caytas, 'Weaponizing Finance: U.S. and European Options, Tools, and Policies', *Columbia Journal of European Law*, Vol. 23, No. 2 (2017).

Features of Taxation and the Impact on the Russian-Cypriot Relations

On 12 May 2016, Russia signed the Multilateral Competent Authority Agreement or MCAA. In accordance with the Communiqué of the 10th Meeting of the OECD Forum on Tax Administration, when signing the MCAA, Russia committed to make the first exchange of information in 2018 for the year 2017. On 6 September 2016, a draft bill entitled 'On Amendments to Part One of the Tax Code of the Russian Federation (due to the implementation of international automatic exchange of information on financial accounts and documentation for international groups of companies)' was published. In March 2017, following a public discussion, a revised version of the bill was published, which, among other things, clarified the provisions regarding the possibility to terminate the contract between a financial institution and its customers.

After developed countries endured budget deficits that were brought on by the global financial crisis, they decided to replenish their treasury by any means. One of the main ways they resort to is to fight tax evasion and, as a result, aggressive tax planning. The US was the first to succeed in this issue due to the Foreign Account Tax Compliance Act (FATCA), which came into operation in 2014. The main emphasis was placed on banks, which, under the threat of being disconnected from payments in US dollars, agreed to report all offenders. The Organization for Economic Cooperation and Development (OECD), following the same strategy, created a Common Reporting Standard (CRS) system as part of the implementation of the BEPS plan, which establishes the general rules for international automatic exchange of tax data. Some of the countries which signed the automatic exchange agreement already made their first exchange in 2017.¹⁰

It is worth noting that FATCA and CRS have a lot in common. Thus, the CRS developers borrowed the basic terminology from FATCA, for example, the definition of financial organisations that have to collect and submit the information. The definitions of passive and active financial institutions, controlling entities and much more, also coincide. In FATCA, the definition of passive income is taken from US Internal Revenue Code, and the definition of passive income, which is given in the commentary on CRS, essentially duplicates it. In addition, the mechanisms for collecting and exchanging data are similar.

¹⁰ D. Sao and A. Gupta, 'Threats to the International Trade Regime: Economic and Legal Challenges Arising from Anti-Offshoring Measures Across the Globe', *The International Lawyer*, Vol. 47, No. 3 (2013).

Although, what is fundamentally different is the essence of the regulation and the consequences of its application. FATCA is only aimed at collecting data on US taxpayers; tax residents of other countries are not affected by this law. The CRS emphasised the global exchange of tax information. Financial organisations in all the countries that agreed on the exchange (including Russia and all European countries) must collect information about their clients, such as their tax residence, and submit it to the appropriate tax authorities. It is worth noting that today the majority of the countries have already joined the automatic exchange of tax information, and the rest of them are planning to do it in the near future. After all, if the State does not join the global project, it risks to be cut off from the global financial system.

Now, there are two options for the exchange of information on taxpayers between States:

- two-way exchange (two States negotiate among themselves all the details of the exchange);
- multilateral exchange (now, over 100 States have joined this type of exchange).

Financial institutions (banks, investment and insurance companies, etc.) are obliged to collect information on taxpayers. Information is exchanged only between those States, which signed the agreements on automatic exchange of tax data.

What consequences can Automatic Exchange have for the Russians?

The automatic exchange can have negative consequences for those who have been hiding their assets, for example, in offshore banks. So far, Russia's tax authorities cannot cope with such a huge amount of data, especially since the information in most cases is provided in foreign languages, primarily in English. It should be noted that, although the beginning of the automatic exchange does not mean that tax audits, automatic fines or additional charges will now start with respect to taxpayers whose information will be revealed, the automatic exchange still enables controlling authorities to carry out their routine procedures without making any additional requests to receive information on foreign accounts which Russian tax residents have opened in foreign banks, as well as on foreign companies they own. Due to this, the Federal Tax Service will be able to increase the tax collection rate for personal income in the form of undistributed profit of controlled foreign companies and other incomes accumulated on foreign accounts.¹¹

¹¹ A. Gusev, 'Russia is ready for Automatic Exchange of financial account Information in tax matters', St. Petersburg: Borenium Attorneys (2018, July 20), available at <https://www.borenium.ru/en/2018/07/20/>

Thus, those tax residents of Russia who actually own controlled foreign companies or have accounts in foreign banks, but did not report this, fall into the main risk group, since it is now easy to set up an indication of such discrepancies with respect to taxpayers' data. It is on such discrepancies that the tax authorities will focus.

So, what should be done? Those who want to insure themselves against unpleasant surprises from the tax service should think about disclosing all financial information before the Federal Tax Service of Russia receives all the data on their tax residency from foreign sources. In addition, this is fraught with considerable fines.

Perhaps, moving to a State that does not participate in the automatic exchange may at first glance seem to be the best way out in such a situation. However, there are very few such countries left. If these countries do not join the exchange, they run the risk of being blacklisted, which means that their residents will most likely not be able to open accounts in foreign banks.

The best solution in this situation is to change the tax residency. Each State has its own criteria for tax residency. To obtain such a status, most States require home ownership or residence in their territory for more than six months, as is the case in the Russian Federation. To minimise the risks associated with the automatic exchange of information on taxpayers, one can consider the States that offer preferential taxation for their residents. One of the best options in this regard for a long time for Russians was Cyprus – which used to be a popular low-tax haven. First, let us consider the concepts of tax residency within the framework of the OECD concept.

The majority of the States adhere to the OECD concept in this matter, according to which an individual automatically becomes a resident of the State when spending more than 183 days a year there. Nowadays, businesspersons very often have to visit other countries; however, not everyone can stay for more than six months in the territory of one State. In this case, the rule of the centre of vital interests is applied. For example, it can be a place where the entrepreneur's family lives, where his children go to school or get higher education, and other factors.

Also, the Russians who keep their assets in foreign currencies should take into consideration such a moment as currency residency. In Russia, the management of foreign income is regulated not only by the Law on Controlled Foreign Companies

[russia-is-ready-for-automatic-exchange-of-financial-account-information-in-tax-matters/](#), accessed 22 February 2019.

(CFC), but also by the legislation on currency residence. According to this, every citizen of Russia is obliged to report on the foreign accounts that he/she owns, and attach statements of accounts translated into Russian. Failure to comply with this requirement is subject to fines, no matter where the taxpayer is actually located.

In this situation, Cyprus looks the most attractive. As mentioned above, after the banking crisis that occurred in 2013, Cyprus lost its former attractiveness, and since then its government has been developing strategies to attract business to the country, including Russian business. After the law on the CFC was adopted in Russia, small businesses became more active in Cyprus and the rental cost for housing and offices in Limassol increased significantly. Also, in 2016, the local authorities introduced a new, quite revolutionary legislation for the island State, according to which, in order to receive Cyprus' tax resident certificate, it is enough to spend only 60 days in the country. To get the certificate, in addition to having a physical presence in the country for 60 days, it is necessary to register a company in Cyprus, provide local citizens with jobs and contribute to the local economy. Another important condition is the purchase or rental of real estate on the island.¹²

In addition, the notion of domicile for Cypriot tax residents was introduced, according to which passive income in the form of interest on loans and dividends is not subject to a special defence tax if an individual has been in Cyprus for less than 17 years from the required 20, starting with the moment when a citizen of a third state became a Cyprus resident. That is, in fact, all passive income in Cyprus is no longer subject to the special defence tax. So, in order to attract talented specialists to the island, whose monthly salary would be significantly higher than the 'standard' for Cyprus, the authorities decided to cut the income tax in half in cases where the resident's salary is EUR100,000 or more.

For anyone who is thinking about getting Cyprus tax residency, it will be beneficial to know what advantages it provides. Let us consider the advantages in favour of becoming a Cyprus resident:

There is no capital gains tax in Cyprus, except for income tax on real estate transactions. Although the income received from operations with foreign real estate is exempt from taxation. Passive income (dividends and interest) of an indi-

¹² M. Brown, I. Evangelou, and H. Stix, 'Banking Crises, Bail-ins and Money Holdings', Working Paper Series (Nicosia: Central Bank of Cyprus, 2018); D. Christofi, 'The Cypriot Banking Sector During the Financial Crisis and Its Reforms: An Examination in Light of the Case of the UK', *The Cyprus Review*, Vol. 29, No.1 (2017); Association of Cyprus Banks, 'Cyprus Banking Insight' (2018, May).

vidual who is not domiciled in Cyprus is exempt from the defence tax. Income from securities transactions is also not taxable.

It should be taken into consideration that the status of Cyprus tax residency imposes certain obligations, where these residents are obliged to prepare and submit an annual Wage and Tax Statement.

Incomes of individuals who are Cyprus residents are taxed regardless of the place where they are received. Therefore, the profit received both in Cyprus and abroad must be declared, after which it is necessary to pay all Cyprus taxes. The tax rate is directly related to the amount of income.

Conclusion

Russia and Cyprus are important partners. Changes in both national and international legislation have led to more than significant results: 67 different agreements are in force between Russia and Cyprus, 19 of which have been prepared and signed in the last six years.

By joining the European Union and implementing disclosure standards, Cyprus has become one of the most transparent jurisdictions from the point of view of European countries. After signing the Protocol on the Double Tax Treaty, Cyprus has become more transparent for the Russian tax authorities. As a result, not all of the 'solutions' used now, within the framework of informational closeness, will work in the future. Russian companies with Cypriot structures will have to analyse the impact of the agreement changes on existing structures, and, if necessary, take steps to modernise them.

As for the authorities of Cyprus, they also found themselves between the hammer and the anvil. On one hand, the massive exodus of Russian capital and withdrawal of assets could lead to a full-scale crisis in the local economy. Approximately 60% of the country's GDP is formed by the banking and financial sectors. Of this 60%, approximately between 15% and 20% are provided by organisations that are, in one way or another, connected with Russian capital. On the other hand, they are under pressure from US demands, the country that no one wants to quarrel with now.

In order to balance the situation, Cyprus authorities have taken a number of measures to facilitate obtaining tax residency status in Cyprus. Now it can be done in two ways: to stay in Cyprus for more than 183 days a year or live in Cyprus for at least 60 days a year and fulfil some other conditions.

OECD has recently been paying more attention to citizenship and residency for investment programmes, suspecting that they can be used for tax evasion. Perhaps, this is because the results of the first automatic exchange, held in 2017, were not lived up to hope and the fees were significantly less than expected. The OECD will continue to fight tax evasion through citizenship and residency for investment. Despite some deterioration in the business climate, Cyprus' jurisdiction is still very attractive for companies leading a real business. In the context of a fairly large-scale business, a personal presence on the island and the correct pricing policy, business efficiency increases significantly compared with traditional forms.

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