

## Chapter 15

### Cyprus

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## I. BANKING SYSTEM

### § 15:1 Banking legislation

There been profound changes in the banking sector in Cyprus and this in turn has been reflected in changes to its legislative framework. The key legislation underpinning the Cyprus banking system is:

1. The Central Bank Law;<sup>1</sup> and
2. The Banking Law.<sup>2</sup>

The principal drivers for legislative amendments since 1997 have been:

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#### [Section 15:1]

<sup>1</sup>Law Number 13 8(I) of 2002, as amended by Law Number 166(I) of 2003 and Law Number 34(I) of 2007.

<sup>2</sup>Law Number 66(1) of 1997, as amended by Law Number 74(I) of 1999, Law Number 94(I) of 2000, Law Number 119(I) of 2003, Law Number 4(I) of

1. Increased internationalization of banking activities;
2. New entrants to the banking market place;
3. Implementation of the *acquis communautaire* in preparation for and since the accession of Cyprus to the European Union (EU) on 1 May 2004;
4. Transposition of the recommendations of the Basel Committee on Banking Supervision;<sup>3</sup> and
5. Entry into the European Monetary Union (EMU) and adoption of the euro as the national currency on 1 January 2008.

Following the entry of Cyprus into the EMU, one of the most important functions of the Central Bank of Cyprus since its establishment, the determination and implementation of monetary policy, has been delegated to the European Central Bank. The Governor of the Central Bank of Cyprus participates in the General Council and the Governing Council of the European Central Bank as a permanent and *ex officio* member with the governors of all the other EU national central banks that are also part of the Eurosystem.<sup>4</sup>

The Central Bank of Cyprus is vested with the power and authority to regulate and supervise the banking sector in Cyprus in accordance with the provisions of the banking legislative framework, to assure the stability of the financial system, to regulate and oversee the payment, clearing, and settlement systems operating in Cyprus,<sup>5</sup> and to collect statistical data on domestic banking in fulfillment of the obligations of the Central Bank of Cyprus as a member of the European System of Central Banks.<sup>6</sup>

The Central Bank of Cyprus exercises its supervisory role with a view to maintaining the stability of the banking system, to minimize systemic risk and to protect the interests of depositors. The paramount and primary objective of the Central Bank of

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2004, Law Number 151(I) of 2004, Law Number 231(I) of 2004, Law Number 235(I) of 2004, Law Number 20(I) of 2005, Law Number 80(I) of 2008, Law Number 100(I) of 2009, Law Number 123(I) of 2009 and Law Number 27(I) of 2011.

<sup>3</sup>Core Principles for Effective Banking Supervision, Basel Committee on Banking Supervision (September 1997).

<sup>4</sup>Central Bank Law, section 20(3)(a).

<sup>5</sup>All references to Cyprus in this text refer to the legally recognized Republic of Cyprus and to its legitimate government and institutions.

<sup>6</sup>Central Bank Law, section 6.

Cyprus remains price stability<sup>7</sup> although, as mentioned above, the pursuit of this goal has been delegated to the European Central Bank.

In exercising its functions, the Central Bank of Cyprus is granted extensive powers to issue secondary legislation directives,<sup>8</sup> as well as to impose sanctions on participants in the domestic banking system for violations of the primary and secondary banking legislation. The sanctions range from reprimanding and imposing fines on the bank's management, initiating its winding up, or revoking its license.<sup>9</sup>

### § 15:2 Definition of “bank”

The Banking Law defines a “bank” as a legal person with a special license issued by the Central Bank of Cyprus to conduct banking activities.

A bank as a body corporate and as far as its corporate aspects are concerned is regulated by the provisions of the Companies Law if it is incorporated in Cyprus, or other relevant laws applicable at the place of its establishment, if established outside Cyprus. Branches of foreign banks do not have a distinct legal personality.

### § 15:3 Types of financial institutions

There are 47 banks and numerous local cooperative credit societies active in Cyprus. The principal categories are:

1. Public listed companies established in Cyprus;
2. Affiliates of foreign banks established in Cyprus as private companies;
3. Branches of foreign banks-companies;
4. Cooperative banks and special-purpose banks;
5. The Housing Finance Corporation; and
6. Representative offices of major international banks.

### § 15:4 Activities of banks

Banking activities are defined as activities carried out within Cyprus or abroad from within Cyprus and consist of the lending

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<sup>7</sup>Central Bank Law, section 5.

<sup>8</sup>Central Bank Law, section 16.

<sup>9</sup>Central Bank Law, section 16; Banking Law, Part XII, XIII, sections 30, 42, and 42A.

of funds acquired from the assumption of obligations to the public in the form of deposits, securities, or other evidence of debt.<sup>1</sup>

According to the Banking Law,<sup>2</sup> a deposit is a sum of money paid or received on terms under which it will be repaid with or without interest or a premium and either on demand or within a term, or under conditions agreed by or on behalf of the person making the payment and the person receiving it, but which are not related to the sale or supply of property, the provision of services, or the issue of debentures or shares.

The sole business of accepting deposits, although not a banking activity per se according to the definition in the Banking Law, nevertheless requires a license from the Central Bank of Cyprus and is subject to all applicable regulation. The Central Bank of Cyprus has the power<sup>3</sup> to exempt certain transactions from the definition of deposit by reference to any factors it deems appropriate and especially by reference to the amount of the deposit, the overall obligations of the person who accepts the deposit, the circumstances surrounding the deposit or the purpose for which the deposit was made, and the number or value of the transactions.

A bank is prohibited from engaging in activities other than those necessary in the ordinary course of banking operations for the satisfaction of debts due to the bank and the activities specified by the Banking Law as integral or closely related to banking business, e.g., financial leasing, factoring, money transmission services, issuing and administering means of payment including credit cards, travelers' checks, and banker's drafts, guarantees and commitments, investment services, data processing services, insurance brokerage services, safe custody services, and any other activity which may be specified as such by the Central Bank of Cyprus.<sup>4</sup>

Insofar as banks provide investment services, they are subject to the provisions of the legislation implementing the EU Markets in Financial Instruments Directive (MIFID),<sup>5</sup> but they remain

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**[Section 15:4]**

<sup>1</sup>Banking Law, section 2.

<sup>2</sup>Banking Law, section 2.

<sup>3</sup>Banking Law, section 3(3).

<sup>4</sup>Banking Law, sections 14 and 13(3).

<sup>5</sup>Investment Services and Activities and Regulated Markets Law, Law Number 144(I) of 2007. MIFID came into force on 1 November 2007 when it replaced the Investment Services Directive. It provides a harmonized regulatory regime for investment services across the 30 member states of the European

subject to the exclusive supervision of the Central Bank of Cyprus in relation to these services as well.<sup>6</sup>

### § 15:5 Particular activities—Banks

The Banking Law imposes specific restrictions on certain business activities and transactions with the intent of ensuring that a bank always maintains an adequate capital base. These restrictions are summarized below:

A bank incorporated in Cyprus may not allow the total value of exposure granted to any one person to exceed at any time 25 per cent of its net assets, or such other lower percentage as the Central Bank of Cyprus may determine from time to time.<sup>1</sup>

A bank may not permit the aggregate of all large exposure<sup>2</sup> to exceed at any time 800 per cent of its net assets, or such other lower percentage as the Central Bank of Cyprus may determine from time to time.<sup>3</sup>

A bank may not grant any credit facility to any director unless the transaction has been approved by a resolution of the board of directors carried by a majority of two-thirds of the total number of directors of the bank at a meeting at which the director concerned was not present during the discussion of the subject by the board and did not vote on the resolution. The exposure in such a case should be granted on the same commercial terms as would apply to a customer for a similar exposure in the ordinary course of banking business.<sup>4</sup> In any case, the bank may not permit the total value of exposure in respect of all its directors to exceed

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Economic Area (EEA, the 27 member states of the EU plus Iceland, Norway, and Liechtenstein).

<sup>6</sup>Law Number 144(I) of 2007, section 120. See also in this respect the Directive for the Professional Conduct of Banks during the Provision of Investment or Ancillary Services and during the Performance of Investment Activities issued by the Central Bank in December 2007, available at [http://www.centralbank.gov.cy/media/pdf/BSDRE\\_Directive\\_for\\_the\\_professional\\_conduct\\_of\\_banks.pdf](http://www.centralbank.gov.cy/media/pdf/BSDRE_Directive_for_the_professional_conduct_of_banks.pdf).

#### [Section 15:5]

<sup>1</sup>Under the Banking Law, section 11(1)(a), the Central Bank may allow exposure in excess of 25 per cent provided that the excess relates to trading book exposures and is covered by additional capital requirements as prescribed by the Central Bank of Cyprus Directive.

<sup>2</sup>A large exposure is defined in the Banking Law, section 11(4), as an exposure to any one person equal to or greater than 10 per cent of the net assets of a bank.

<sup>3</sup>Banking Law, section 11(1)(b).

<sup>4</sup>Banking Law, section 11(1)(c).

at any time 40 per cent of its net assets, or such other lower percentage as the Central Bank of Cyprus may determine from time to time. Furthermore, the bank may not permit the total value of unsecured exposure in respect of all its directors to exceed at any time 5 per cent of its net assets, or such other lower percentage as the Central Bank of Cyprus may determine from time to time.<sup>5</sup>

A bank may not acquire, purchase, or hold any right in any immovable property, except where the property may be currently required for the purpose of conducting its business and other activities or where the property is acquired in the course of satisfaction or settlement of debts due to the bank, in which event the property must be disposed of as soon as possible and in any case within three years of its acquisition, except where the Central Bank of Cyprus extends the period of three years if it considers that such extension is fully justified on account of exceptional circumstances.<sup>6</sup>

A bank may not acquire or hold, directly or indirectly, more than 10 per cent of the share capital of any other company or have control over such a company and, in the case of a bank incorporated in Cyprus, the value of any share capital held in any other company may not exceed 10 per cent and for all companies in aggregate may not exceed 25 per cent of the bank's net assets, unless the Central Bank of Cyprus gives its prior written approval subject to any conditions which it may consider proper to impose.<sup>7</sup> This limitation does not apply:

1. Where a bank acquires or holds any part of the share capital of any company under an underwriting or sub-underwriting contract for a period not exceeding two years from the time of acquisition except where the Central Bank of Cyprus considers it proper to extend the period of two years on account of exceptional circumstances;
2. To any holding of share capital in a company incorporated in Cyprus which carries out banking business, nominee,

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<sup>5</sup>Banking Law, section 11(1)(e).

<sup>6</sup>Banking Law, section 12. According to a directive issued by the Central Bank on this issue, see [http://www.centralbank.gov.cy/media/pdf\\_gr/BCDRG\\_AKINITI\\_PERIOUSIA\\_TRAP.pdf](http://www.centralbank.gov.cy/media/pdf_gr/BCDRG_AKINITI_PERIOUSIA_TRAP.pdf), banks are required to report bi-annually acquisitions and disposals of real property.

<sup>7</sup>Banking Law, section 13. See the directive issued by the Central Bank on this issue at [http://www.centralbank.gov.cy/media/pdf\\_gr/BCDRG\\_EPEND\\_SE\\_TRITEW\\_ETER.pdf](http://www.centralbank.gov.cy/media/pdf_gr/BCDRG_EPEND_SE_TRITEW_ETER.pdf), whereby banks are required to report annually acquisitions and disposals of shares in other companies.

executor, or trustee functions, or predominantly other functions integral to or closely related to banking business;<sup>8</sup> or

3. To any share capital in another company which was acquired by the bank in the course of satisfaction of debts due to it, provided that such share capital is disposed of not later than three years from the time of its acquisition, except where the Central Bank considers it proper to extend the period of three years on account of exceptional circumstances.<sup>9</sup>

A bank is prohibited from engaging in any trading activity or enterprise, whether on its own account or on a commission basis, save in so far as may be necessary in the ordinary course of banking operations for the satisfaction of debts due to the bank.<sup>10</sup>

A bank may not acquire or deal for its own account in its own shares without permission from the Central Bank of Cyprus, or grant credit facilities to persons other than the employees of the bank in excess of €85,430 per person for the purpose of financing the purchase of its own shares, the shares of its holding company, or the shares of any subsidiary of the bank or of its holding company.<sup>11</sup>

### § 15:6 Particular activities—Cooperative societies

In Cyprus, the more than 100 Cooperative Credit Societies and the Central Cooperative Bank (the CCB) currently hold an aggregate market share of over 30 per cent of local deposits and loans. The main aim of the Societies is to make available credit facilities and other banking services to their members in accordance with their principles of mutual help and assistance. The Societies are not profit-oriented organizations and they have strong links with local communities, since each is governed by a committee of residents of the geographic area where it offers its services. They are registered cooperative societies and comply with the Cooperative Societies Laws and Rules.

The Central Cooperative Bank is the core of the system of cooperative credit societies since it fulfils both the role of lender of last resort and the banker of the system and the role of the

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<sup>8</sup>Banking Law, section 13(3).

<sup>9</sup>Banking Law, section 13(4).

<sup>10</sup>Banking Law, section 14.

<sup>11</sup>Banking Law, section 15.



central body, as defined in Directive 2000/12/EC.<sup>1</sup> This dual role renders it subject to the supervision of both the Cooperative Societies' Supervision and Development Authority and the Central Bank of Cyprus<sup>2</sup> on all issues related to the conduct of banking activities, e.g., capital adequacy, liquidity, risk management policies, governance, internal control, and anti-money laundering regulations.

### § 15:7 Housing Finance Corporation

The Housing Finance Corporation is a state-owned banking institution whose main aim is the provision of housing loans to individuals of middle and low income.<sup>1</sup> The board of directors of the Corporation, consisting of seven members, is appointed by the Council of Ministers. The Board may:

1. Proceed with loans on mortgages and promote saving plans;
2. Grant loans using deposits as security; and
3. Act as a trustee of the government, international or local organizations, foundations, or other legal entities.

The Corporation is a banking institution and by express provision of the Housing Finance Corporation Law<sup>2</sup> is subject to the supervision of the Central Bank of Cyprus and the provisions of the Banking Law.<sup>3</sup> Owing to its nature as a state-owned and controlled entity, its activities are also monitored by the central government.

### § 15:8 Housing Finance Corporation—Representative offices of international banks

The Banking Law defines a representative office as an office (and not a distinct legal entity) of a foreign bank from which the interests of that bank are in any way promoted or assisted. Importantly, neither banking business nor the business of accept-

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#### [Section 15:6]

<sup>1</sup>Article 2(5) and (6) of Directive 2000/12/EC relating to the taking up and pursuit of the business of credit institutions.

<sup>2</sup>Banking Law, section 35(2).

#### [Section 15:7]

<sup>1</sup>Housing Finance Corporation Law, Law Number 43 of 1980, section 5(1).

<sup>2</sup>Housing Finance Corporation Law, section 5(3).

<sup>3</sup>Banking Law, section 36.

ing deposits may be carried on at such an office.<sup>1</sup> The establishment of a representative office is subject to the prior approval of the Central Bank of Cyprus that may grant its approval subject to any conditions it considers proper to impose.<sup>2</sup>

A representative office may use the word bank or any grammatical variation of that word as part of its name, provided that it is the name under which the banking institution to which it belongs carries on business in its country of origin and provided further that the name is used in Cyprus in conjunction with the description “Cyprus representative office”. The Central Bank of Cyprus has wide discretion in the exercise of its supervisory functions over representative offices operating in Cyprus. At any time it may impose conditions or cancel any conditions already imposed or even revoke any approval granted.<sup>3</sup>

#### **§ 15:9 Ownership requirements—Restrictions imposed under the Banking Law**

Under the Banking Law, the Central Bank of Cyprus is afforded significant approval and monitoring powers in respect of bank ownership.

Section 4c of the Banking Law stipulates that the Central Bank of Cyprus may not grant authorization for the taking-up of the business of a bank unless it has been informed of the identities of the shareholders or members, natural or legal persons, who have direct or indirect control of the company and the percentage of that control.

“Control” is deemed to exist where a shareholder owns alone or together with connected entities or persons 20 per cent or more of the share capital of the company. Section 4d imposes an obligation on the Central Bank of Cyprus to refuse such authorization if, taking into account the need to ensure the sound and prudent management of the bank, it is not satisfied as to the suitability of the shareholders or members.

The owners and the controlling shareholders of banks are also subject to monitoring and prior approval by the Central Bank of

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**[Section 15:8]**

<sup>1</sup>Banking Law, section 2.

<sup>2</sup>Banking Law, section 8(1).

<sup>3</sup>Banking Law, section 8(3) and (4).

Cyprus not just at the stage of the bank's licensing,<sup>1</sup> but throughout the bank's life.<sup>2</sup> Additionally, shareholdings equal to or more than 10 per cent of the bank's share capital also must be reported on a continuous basis to the Central Bank of Cyprus.

For the purposes of the Banking Law, persons deemed to be acting in concert with any proposed share purchaser are:

1. The spouse or relatives of the first degree of kindred of that person;
2. Any company of which that person is a director or has control over it;
3. Any person who is a partner of that person, and in the case where that person is a company (a) any director or any person who has control over that company, (b) any subsidiary of that company, and (c) any director of any such subsidiary;
4. Any other person or persons whose interests, in the opinion of the Central Bank of Cyprus, are interdependent with those of that person or of any other person who holds shares.

As stated previously, section 15 of the Banking Law provides that a bank may not acquire or deal for its own account in its own shares without permission from the Central Bank of Cyprus, or grant credit facilities to persons other than the employees of the bank in excess of €85,430 per person for the purpose of financing the purchase of its own shares, the shares of its holding company, or the shares of any subsidiary of the bank or of its holding company.

Section 16 requires any "bank" as defined by the Banking Law to obtain the prior written approval of the Central Bank of Cyprus before it can sell or dispose of the whole or part of its business by amalgamation or any other means. The Central Bank of Cyprus may grant such approval on a conditional or an unconditional basis.

### **§ 15:10 Ownership requirements—Restrictions on participation in share capital of a bank**

In the banking sector, no person of any nationality, whether resident or non-resident, may own directly or indirectly 10 per

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#### **[Section 15:9]**

<sup>1</sup>Banking Law, section 4(c) and (d).

<sup>2</sup>Banking Law, section 17. Prior reporting and approval obligations are triggered when a shareholder intends to acquire or relinquish control over 20 per cent, 33 per cent, and 50 per cent of the bank's capital.

cent or more of a banking company's share capital or voting stock without the approval of the Central Bank of Cyprus.

**§ 15:11 Other financial institutions—Cooperative societies**

In general, the Banking Law<sup>1</sup> does not apply to cooperative societies, except for those established principally for the purpose of carrying on banking business for the benefit of their members who are themselves cooperative societies. The majority is, however, subject to the Cooperative Societies Law.<sup>2</sup>

The Cooperative Societies Law was amended to implement the *acquis communautaire* in relation to credit institutions. It regulates the establishment and operation of cooperative societies, including cooperative credit societies. Cooperative credit societies are supervised by a special authority, the Cooperative Societies' Supervision and Development Authority.

The Cooperative Societies' Supervision and Development Authority exercises its supervisory role through regular inspection visits, attendance at meetings, and the audit reports of the Audit Service of Cooperative Societies, which is responsible for auditing the financial statements, and for the financial management, of Cooperative Societies.

Cooperative societies may give loans to their members, subject to their special regulations. According to section 37(1) of the Cooperative Societies Law, a cooperative society may not give a loan to a person who is not one of its members. However, with the consent of the Registrar of the Cooperative Societies, a society may grant loans to other societies or to any group of persons not a member of the lending society. Notwithstanding the provisions of section 37(1) of the Cooperative Societies Law, a society may grant a loan to one of its depositors and use his deposit as security.

A society may accept deposits and receive loans from its members and from non-members only under the relevant regulations. A society may deposit or invest its capital in government bonds or in the Central Cooperative Bank or, with the approval of the Registrar of the Cooperative Societies, in any other bank.

The Central Cooperative Bank is the core of the system of Co-

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**[Section 15:11]**

<sup>1</sup>Banking Law, section 35(1).

<sup>2</sup>Law Number 22(1) of 1985, as amended.

operative Credit Societies since it fulfils both the role of lender of last resort and the banker of the system, as well as the role of the central body as defined in Directive 2000/12/EC.<sup>3</sup> A Cooperative Credit Society, if it fulfils certain minimum criteria set by the law and regulations on cooperative societies (e.g., minimum share capital, capital adequacy, internal control, and organizational structure), may choose to be recognized either through its affiliation with the Central Cooperative Bank's Central Body or as a free standing cooperative credit society with autonomous and continuing compliance obligations.

A cooperative credit society not fulfilling these criteria should always be affiliated to the Central Cooperative Credit Society. For an affiliated cooperative credit society to qualify for exemption from the obligation to fulfill, on an individual basis, the requirements imposed on credit institutions, the Central Cooperative Bank Central Body should guarantee its obligations and provide it with continuous technical assistance and instructions.<sup>4</sup>

The guarantee of the Central Cooperative Bank's Central Body, provided for the benefit of the depositors of the affiliated cooperative credit societies, is triggered when an affiliated cooperative credit society is unable to meet its current obligations towards its depositors. The Central Cooperative Bank's Central Body also is vested with authority to monitor the application of its instructions by the affiliated credit societies while coordinating with the Cooperative Societies' Supervision and Development Authority for the avoidance of duplication and overlap of their respective supervisory functions.

#### **§ 15:12 Other financial institutions—Housing Finance Corporation**

Section 36 of the Banking Law stipulates that provisions of the Banking Law also apply to the Housing Finance Corporation to the extent that these are not in conflict with the provisions of the Housing Finance Corporation Law. The Companies Law does not apply to the Housing Finance Corporation. Under sections 6 and 7 of the Housing Finance Corporation Law, the Council of Ministers appoints the Board of Directors of the Housing Finance Corporation, consisting of seven members who exercise control over the Housing Finance Corporation and determines its policies. Despite this close government involvement, the Central Bank of

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<sup>3</sup>Article 2(5) and (6) of Directive 2000/12/EC relating to the taking up and pursuit of the business of credit institutions.

<sup>4</sup>Regulatory Administrative Decree Number 393/2006.

Cyprus maintains a significant monitoring role in respect of the Housing Finance Corporation.

Under section 5 of the Housing Finance Corporation Law, the Housing Finance Corporation, after being so requested by the Central Bank of Cyprus, must appoint a duly authorized official of the Central Bank of Cyprus to examine books, records, and any other documents, including those relating to loans and other credit facilities, as well as any other information given to the Housing Finance Corporation in relation to the employment and the financial status of its debtors.

**§ 15:13 Cyprus-incorporated banks operating abroad—In general**

The Banking Law differentiates between opening a branch or representative office in an EU member state and a third-party state.

**§ 15:14 Cyprus-incorporated banks operating abroad—Opening a branch in a European Union Member State**

Section 10C(1) requires a bank incorporated in Cyprus to notify the Central Bank of Cyprus of the following:

1. The program of operations setting out the types of business envisaged and the structural organization of the branch;
2. The address of the branch in the member state from which documents may be obtained;
3. The names of the prospective persons to be responsible for the management of the branch; and
4. The capital base and the capital adequacy ratio of the bank.

Unless the Central Bank of Cyprus has reasons to doubt the adequacy of the administrative structure or the financial situation of the bank, it should, within three months of receipt of a correct notification, communicate the information contained in it to the competent supervisory authorities of the proposed host member state. This communication should also be notified to the bank within three months.

Where the Central Bank of Cyprus declines to communicate the information referred to in section 10C(1) to the competent supervisory authority of the host member state, it must give reasons for its refusal to the bank concerned within three months of receipt of all the information in accordance with section 10C(1). The Central Bank of Cyprus must inform the European Commission of the number and type of cases where it has refused to com-

municate the information to the competent supervisory authority of the host member state.

**§ 15:15 Cyprus-incorporated banks operating abroad—  
Crossborder services within a European Union  
Member State**

Under section 10C(5) of the Banking Law, where a bank intends to carry on its activities for the first time by providing crossborder services within an EU member state without establishing a branch in that state, it must notify this intention to the Central Bank of Cyprus, specifying the member state and the activities which it intends to carry on.

The Central Bank of Cyprus must, within one month of receipt of the notification, send that notification to the competent supervisory authorities of the host member state.

**§ 15:16 Cyprus-incorporated banks operating abroad—  
Opening a branch or representative office in a  
Non-European Union State**

Under section 7(1) of the Banking Law, a bank incorporated in Cyprus may not establish or maintain a branch or a representative office outside of the EU without prior approval of the Central Bank of Cyprus. Such approval may be granted subject to any conditions that the Central Bank of Cyprus may consider appropriate. Additionally, the Central Bank of Cyprus may at any time, by notice in writing, attach to an approval already granted any new conditions, or amend or cancel any conditions so attached, as it may think proper.

The Central Bank of Cyprus may, at any time, by notice in writing, revoke an approval granted under section 7(1). In such an instance, the operation of the branch or representative office, as the case may be, must be terminated within such time limit as may be specified in the notice.

In exercising its discretionary power, the Central Bank of Cyprus is obliged to take into consideration, by way of guidance, international practice, and the Directives and Regulations of the EU, the protection of depositors, and the interests of the customers of the bank in general, and the orderly functioning of the banking system, and it must issue adequately reasoned decisions or directives.

## **II. LICENSING OF BANKS**

**§ 15:17 Licensing process—In general**

The policy with respect to the granting of licenses to carry on



banking business is determined by the Central Bank of Cyprus. The licensing process for obtaining a banking business license involves four stages, namely:

1. Pre-application meetings;
2. Application stage;
3. Licensing of the bank; and
4. Authorization for the commencement of banking business by the bank.

Before a bank can be licensed, it also must have obtained the approval of the Central Bank of Cyprus of all direct and indirect controllers and of all persons appointed as board members and chief executives or managers.

#### **§ 15:18 Licensing process—Pre-application meetings**

Prospective applicants should seek to consult with the Central Bank of Cyprus as early as possible and, in any event, prior to their final decision to submit an application.

The purpose of such consultation is to discuss the nature of the prospective application and to receive the Central Bank of Cyprus's preliminary views on the manner in which the application should be prepared as well as on the prospects of the application.

#### **§ 15:19 Licensing process—Application stage**

Applications for a banking business license must be submitted to the Central Bank of Cyprus in writing by or on behalf of the applicant, accompanied by the Memorandum and Articles of Association, or any equivalent constitutional document.

During the application process, applicants must disclose all matters that may be relevant to the Central Bank of Cyprus in assessing the applicant's ability to satisfy and continue satisfying the Central Bank of Cyprus's requirements. For an application to be regarded by the Central Bank of Cyprus as complete, it must provide the Central Bank of Cyprus with information on:

1. The identity and suitability of all direct or indirect controllers, directors, and managers of the applicant;
2. The source of funding of the proposed bank, as well as the transparency and legitimacy of this source;
3. The financial standing of the applicant, its controllers, and any group to which it belongs;
4. The adequacy of the proposed bank's business plan, which must provide details of the proposed banking activities to be conducted, as well as on the proposed bank's projected



financial condition, its management, and organizational structures, including the proposed internal governance and compliance procedures and systems to be used; and

5. The existence of any close links between the applicant and other natural or legal persons, which may impede the effective exercise of the Central Bank of Cyprus's supervisory function.

At any time after receiving an application and before determining it, the Central Bank of Cyprus may require the applicant to provide it with such further information as it reasonably considers necessary to enable it to determine the application.

#### **§ 15:20 Licensing process—Licensing of the bank**

The Central Bank of Cyprus may, under section 4(3) of the Banking Law, with an adequately reasoned decision:

1. Grant a license without any condition or subject to such conditions it may consider proper to impose; or
2. Refuse to grant a license.

A refusal must be notified to the applicant within six months from the date of receipt of the application for a license. Should an application be incomplete, a refusal must be notified to the applicant within six months from the date of receiving the additional information or clarifications requested. Notwithstanding the above, the Central Bank of Cyprus is bound to take a decision within a year of the receipt of an application.

#### **§ 15:21 Licensing process—Authorization**

In the event that a license is issued by the Central Bank of Cyprus, the licensed bank must, within a maximum period of 12 months, prepare for its setting up and operation.

Prior to the Central Bank of Cyprus giving its final authorization to the licensed bank to commence operations, a letter must be addressed by the licensed bank to the Central Bank of Cyprus, declaring that:

1. It has observed all conditions attached to its banking license;
2. Its initial capital has been fully paid-up (for locally incorporated banks);
3. Its initial contributions to the Deposit Protection Fund and the Investor Compensation Fund for Clients of Banks have been paid, unless it is exempted from such an obligation under the relevant regulations governing the establishment and operation of these funds;
4. The premises where banking activities will be conducted

comply with security and protection requirements according to best practices and industry standards; and

5. The information and accounting systems implemented by the bank are adequate to disclose its true financial position, to provide the necessary information for decision making, and to ensure the compilation of annual or periodic financial statements, as well as of any regulatory, prudential, or statistical returns, in an accurate and timely manner.

The above letter should be accompanied by a confirmation from the bank's approved external auditors that the above requirements have been met by the bank.

#### **§ 15:22 Central Bank of Cyprus control after issue of license**

Section 30(1) of the Banking Law gives the Central Bank of Cyprus extensive powers to intervene in the event that a bank fails to comply with any of the provisions of the Banking Law, or of any Regulation issued under the Banking Law, or with the conditions of its license, or if, in the opinion of the Central Bank of Cyprus, the liquidity and character of its assets have been impaired or there is a risk that the ability of the bank to meet its obligations promptly may be impaired, or where this is considered necessary for the safeguarding of the interests of depositors or creditors. In these circumstances, the Central Bank of Cyprus may take all or any of the following measures:

1. The Central Bank of Cyprus may require the bank forthwith to take such action it considers necessary to rectify the matter or to restrict the operations of a bank by imposing conditions on its license as it thinks desirable; and
2. Without prejudice to the generality of the previous paragraph, the Central Bank of Cyprus may impose conditions in particular which (a) require the bank to take certain steps or to refrain from adopting or pursuing a particular course of action or to restrict the scope of its business in a particular way, (b) impose limitations on the bank in the acceptance of deposits, the granting of credit, or the making of investments, (c) prohibit the bank from soliciting deposits, either generally or from specified persons or classes of persons, (d) prohibit the bank from entering into any other transaction, or class of transactions, (e) require the removal of any director, chief executive, or manager of a bank, (f) oblige the bank to hold own funds in excess of the minimum level laid down pursuant to the provisions of section 21 of the Banking Law, (g) require the reinforcement of the ar-

rangements, processes, mechanisms, and strategies of the bank, (h) require the bank to apply a specific provisioning policy or treatment of assets in terms of capital requirements, (i) restrict or limit the business, operations, or network of banks, and (j) require the reduction of the risk inherent in the activities, products, and systems of banks.

Any condition imposed by the Central Bank of Cyprus may be varied or withdrawn by it.

### § 15:23 Refusal to grant license

The Central Bank of Cyprus may, at its own discretion, refuse to grant a license if:

1. It has not been satisfied as to the suitability of the applicant, its controllers, or the group to which it belongs;
2. It has reasonable grounds to suspect money laundering or terrorist financing by the applicant or any of its controllers;
3. The information provided by any of the applicant's controllers does not disclose clearly their identity and their business activities and, in the case of controllers that are legal entities, the identity and business activities of persons having direct or indirect control over them have not been stated clearly;
4. The business plan submitted has not satisfied the Central Bank of Cyprus that the applicant has clearly defined and adequately researched objectives, nor that the proposed operations are consistent with the Banking Law and the Central Bank of Cyprus's licensing and prudential supervisory requirements;
5. The information made available to the Central Bank of Cyprus indicates that the activities and transactions carried out by the applicant or by any of its controllers are such that the proposed bank may not be able to carry out its activities in accordance with the law and with the requirements of prudent and sound banking practices;
6. Close links exist between the applicant and other natural or legal persons that may prevent the effective exercise of the Central Bank of Cyprus's supervisory function;
7. The corporate structure of the group of which the applicant is part, or its relationship with other undertakings under common control, is not clear and transparent and is such that it may result in the Central Bank of Cyprus being unable to exercise its supervisory responsibilities effectively;
8. The source of funds to be used for acquiring the participation in the share capital of the proposed bank cannot be clearly established;

9. The applicant or any of its controllers have not been transparent, open, and cooperative in their dealings with the Central Bank of Cyprus or other regulatory authorities;
10. Some or all of the controllers of the applicant or the applicant itself are established in a jurisdiction which does not impose the maintenance of shareholders' registers and proper accounting records and publication of financial statements, or which allows the preservation of anonymity regarding the identity of shareholders and persons charged with the management of the bank;
11. It has not been satisfied as to the fitness and propriety of the applicant's directors and managers;
12. It has reasonable grounds to believe that there is a lack of willingness and capacity on the part of the applicant to comply with its licensing and supervision requirements on a continuous basis;
13. The home supervisor of the parent bank seeking to establish a subsidiary or branch in Cyprus does not, in the opinion of the Central Bank of Cyprus, exercise adequate supervision in accordance with internationally accepted minimum standards, including supervision on a consolidated basis;
14. There is no legal basis, or possibility of cooperation, for exchange of information with the parent bank's home supervisor;
15. The parent bank or the group of which it forms part are incorporated in a country or territory considered by the Financial Action Task Force to be of "high risk" or "non-cooperative" or more broadly in a country or territory that has not taken sufficient measures to comply with robust anti-money laundering and anti-terrorist financing procedures complying with internationally accepted standards;
16. The consent of the parent bank's home supervisor has not been provided; or
17. The applicant does not have sufficient technical means or financial and human resources for the type or volume of transactions which it intends to carry out in Cyprus or its activities are such that the stability or control of the proposed bank in Cyprus may be affected by the high risk of such activities.

#### § 15:24 Insolvency

According to section 33 of the Banking Law, notwithstanding any provision contained in the Companies Law in connection

with the winding up of a company, the revocation of the license of a bank under section 30(1) of the Banking Law constitutes a ground for its winding up by the court on the application of the Central Bank of Cyprus. The appointment, in any case, of a liquidator of a bank other than the official receiver may not be made without the court having previously heard the views of the Central Bank of Cyprus.

According to the Companies Law, on the making of a winding-up order, a copy of the order must be forwarded to the Registrar of Companies for registration. When a winding-up order has been made, no action or proceeding may be continued or commenced against the company, except by leave of the court and subject to such terms as the court may impose. An order for winding up a company will operate in favor of all creditors of and all contributories to the company, as if made on the joint petition of a creditor and a contributory.

### III. REGULATORY ISSUES

#### § 15:25 Money laundering

The Prevention and Suppression of Money Laundering Activities,<sup>1</sup> that consolidates, revises, and repeals all former laws on this subject, came into force on 1 January 2008. It transposes into Cyprus legislation the provisions of the relevant EU Directives, including those of the Third Directive on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing (Directive 2005/60/EC).

The Central Bank of Cyprus is appointed as the money laundering supervision authority in relation to entities which have been granted a license under the relevant laws of Cyprus to carry on banking in or from Cyprus.<sup>2</sup>

For these purposes, the Prevention and Suppression of Money Laundering Activities Law<sup>3</sup> requires banks, as entities engaged in financial activities, to establish appropriate systems and procedures for the following:

1. Customer identification and due diligence;
2. Record keeping;

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#### [Section 15:25]

<sup>1</sup>Law Number 188(1) of 2007.

<sup>2</sup>Prevention and Suppression of Money Laundering Activities Law, section 59(1)(a).

<sup>3</sup>Prevention and Suppression of Money Laundering Activities Law, section 58.

3. Internal reporting and reporting to the Unit for Combating Money Laundering (MOKAS);<sup>4</sup>
4. Internal control, assessment, and management of risk with the purpose of preventing money laundering and terrorist financing;
5. Detailed examination of any transaction which by its nature may be considered to be particularly vulnerable or to be associated with money laundering or the financing of terrorism, particularly sophisticated, complex, and unusually large transactions, and all unusual types of transactions that are realized without obvious economic or explicit legal reason; and
6. Employee awareness with regard to the anti-money laundering regulatory framework and regular training to equip them to recognize and deal with suspicious transactions and activities which may be related to money laundering or terrorist financing offences.

The Central Bank of Cyprus, in exercise of the powers conferred on it by the Prevention and Suppression of Money Laundering Activities Law,<sup>5</sup> has issued a comprehensive directive laying down the specific policy, procedures, and internal controls that all banks should implement for the effective prevention of money laundering and terrorist financing and for achieving full compliance with the requirements of the Prevention and Suppression of Money Laundering Activities Law (the Prevention and Suppression of Money Laundering Activities Directive).<sup>6</sup> The Prevention and Suppression of Money Laundering Activities Directive also establishes a comprehensive system of regular reporting aiming at the early recognition of suspicious activities.

In particular, all banks in Cyprus are under an obligation to submit to the Central Bank of Cyprus monthly statements of large cash deposits and funds transfers, monthly statements of one-off deposits in foreign currency in excess of the equivalent of €100,000 which have been imported into Cyprus from abroad, and an annual statement of aggregate deposits in foreign currency notes in excess of the equivalent of €100,000 in a calendar year.

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<sup>4</sup>Prevention and Suppression of Money Laundering Activities Law, section 54.

<sup>5</sup>Prevention and Suppression of Money Laundering Activities Law, section 59(4).

<sup>6</sup>See [http://www.centralbank.gov.cy/media/pdf/BCMLDRE\\_MONEY\\_LAUNDERING\\_3RD\\_EDITION.pdf](http://www.centralbank.gov.cy/media/pdf/BCMLDRE_MONEY_LAUNDERING_3RD_EDITION.pdf).

**§ 15:26 Banking secrecy**

The Prevention and Suppression of Money Laundering Activities Law imposes a wide-ranging duty of confidentiality on directors, chief executives, managers, officers, employees, and agents of a bank and on all persons having access by any means to the records of a bank with regard to the account of any customer of the bank during their employment by or professional relationship with the bank during or after its termination.<sup>1</sup> The duty of confidentiality ceases to apply if:

1. The customer or his personal representatives give written permission;
2. The customer, if a natural person, is declared bankrupt or, if a company, is wound up;
3. Civil proceedings are instituted between the bank and the customer or his guarantor relating to the customer's account;
4. The information is given to the police under the provisions of any law or to a court in the investigation or prosecution of a criminal offence under any law<sup>2</sup> or to a public officer who is duly authorized under the law to obtain that information;<sup>3</sup>
5. The bank has been served with a garnishee order attaching money in the account of the customer;
6. The information is required in the course of his duties by a colleague employed by the same bank, its holding company, a subsidiary of the bank, or its holding company or an auditor;
7. The information is required to assess the creditworthiness of the customer in relation to a *bona fide* commercial transaction or prospective commercial transaction, so long as the

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**[Section 15:26]**

<sup>1</sup>Prevention and Suppression of Money Laundering Activities Law, section 29(1).

<sup>2</sup>Prevention and Suppression of Money Laundering Activities Law, section 45.

<sup>3</sup>Assessment and Collection of Taxes (Amendment) Law, Law Number 72(I) of 2008. Irrespective of any confidentiality law, the Tax Commissioner, in the context of procedures for the exchange of information established by a double tax treaty and after the relevant request of a competent national authority, may demand and collect from any person and in any form records, books, or other documents or information to the extent necessary, bearing in mind all the circumstances. The relevant request of the foreign authority should be adequately corroborated and the powers of the Commissioner may only be exercised with the consent of the Attorney General. Prevention and Suppression of Money Laundering Activities Law, section 27.



information required is of a general nature and in no way related to the details of the customer's account; and

8. The provision of the information is necessary for reasons of public interest or for the protection of the interests of the bank.<sup>4</sup>

### § 15:27 Bank deposit and investment protection schemes

Under the Prevention and Suppression of Money Laundering Activities Law<sup>1</sup> and the regulations for the establishment and operation of the Deposit Protection Scheme (the Deposit Protection Scheme Regulations),<sup>2</sup> a Deposit Protection Fund (the "Fund") has been in operation in Cyprus since September 2000.

The purpose of the Fund is to provide protection for and pay compensation to depositors in case a member bank is unable to repay the deposits of its customers.<sup>3</sup> The Fund constitutes a separate legal entity and is administered by a management committee according to the relevant provisions of the Deposit Protection Scheme Regulations.<sup>4</sup>

Participation in the Fund is compulsory for all banks incorporated in Cyprus, although a bank with its head office in another EU member state is considered to be adequately covered by a corresponding deposit protection scheme in its home state and thus may be exempt from participation in the Fund.<sup>5</sup> All participating banks must make contributions to the Fund that cannot exceed 0.3 per cent of their deposit base.<sup>6</sup>

The Deposit Protection Scheme covers deposits denominated in euros or any other currency of a member state of the EU. Several categories of deposits, such as deposits by provident and pension funds and deposits denominated in currencies other than euros or other member state currencies, are not protected by the Fund.<sup>7</sup>

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<sup>4</sup>Prevention and Suppression of Money Laundering Activities Law, section 29(2).

#### [Section 15:27]

<sup>1</sup>Prevention and Suppression of Money Laundering Activities Law, section 34.

<sup>2</sup>See [http://www.centralbank.gov.cy/media/pdf/BCSTE\\_DPSREGULATION0805.pdf](http://www.centralbank.gov.cy/media/pdf/BCSTE_DPSREGULATION0805.pdf).

<sup>3</sup>Deposit Protection Scheme Regulations, paragraph 3.

<sup>4</sup>Deposit Protection Scheme Regulations, paragraph 4 and Part IX.

<sup>5</sup>Deposit Protection Scheme Regulations, paragraph 5.

<sup>6</sup>Deposit Protection Scheme Regulations, paragraph 12.

<sup>7</sup>Deposit Protection Scheme Regulations, paragraph 18.



The level of compensation per depositor under the Scheme is 90 per cent of the amount of each protected deposit, subject to a limit of €100,000 or its equivalent in the currency of the member state of the EU in which the deposit is denominated. The limit applies to the aggregate of each depositor's deposits with the bank.

The Deposit Protection Scheme is activated when a deposit is rendered unavailable, i.e., if the Central Bank of Cyprus or another competent supervisory authority in relation to banks established outside Cyprus has determined that the member bank is unable to repay its deposits for reasons directly related to its financial circumstances and foresees that there are no prospects of it being able to do so in the near future, or if a competent court has issued an order for the liquidation of the bank.<sup>8</sup>

During liquidation proceedings, the Fund is subrogated to the rights and remedies of depositors from the moment the latter submit their claim for compensation to the Fund's Management Committee. Where the Fund recovers from the liquidator, in respect of any deposit, an amount greater than the amount paid as compensation, the Fund is required to refund to the beneficial owner of the deposit any amount in excess of the compensation paid.<sup>9</sup>

For the protection of the recipients of banks' investment services and in line with the provisions of Directive 97/9/EC on investor compensation schemes, an Investor Compensation Fund for customers of banks has been established and a set of relevant regulations has been issued by the Central Bank.<sup>10</sup> Participation in the Fund is compulsory for all banks incorporated in Cyprus that offer investment services.

A bank having its registered offices in a third country which maintains a branch in Cyprus or provides investment services in Cyprus on a crossborder basis is not required to join the Investor Compensation Fund in so far as an equivalent fund operating in the third country is extended to customer recipients of the bank's investment services in Cyprus.<sup>11</sup> The total compensation payable to each investment services customer of a bank that is a member

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<sup>8</sup>Deposit Protection Scheme Regulations, paragraph 23.

<sup>9</sup>Deposit Protection Scheme Regulations, paragraph 26.

<sup>10</sup>See [http://www.centralbank.gov.cy/media/pdf/IBRG\\_26Nov04.pdf](http://www.centralbank.gov.cy/media/pdf/IBRG_26Nov04.pdf).

<sup>11</sup>Regulations on Investor Compensation Fund for Clients of Banks, paragraph 5.

of the Investor Compensation Fund may not, in any case, exceed €20,000.<sup>12</sup>

In 2011 Cyprus imposed a levy on credit institutions, which will be used to create a financial stability fund. For each year from 2011 onwards credit institutions operating in Cyprus will be required to pay a levy of 0.095% on their customer deposits as at the preceding 31 December. No levy is payable on inter-bank deposits. The levy will be payable by:

- Cyprus banks in respect of their banking activities in Cyprus (overseas branches and subsidiaries will not be subject to the levy);
- the Cyprus operations of overseas (EU and third-country) banks and credit institutions; and
- co-operative credit institutions.

The levy, which will not be deductible for the purpose of calculating taxable profits, will be limited to 20% of the taxable profit for the year in which it is paid. The declaration of taxable deposits on the preceding 31 December must be made by 31 March each year, and the levy will be collected in four equal instalments at the end of each quarter, starting 31 March. The cost of the levy is intended to fall on banks, not their customers, and the law introducing the levy includes provision for a fine of up to €100,000 to be imposed on credit institutions which are found to have passed the cost onto their customers.

#### IV. SUPERVISORY ISSUES

##### § 15:28 Supervision and inspection

Under the Banking Law,<sup>1</sup> the Central Bank of Cyprus is responsible for the supervision of banks to ensure the orderly functioning of the banking system. The supervisory role of the Central Bank of Cyprus is further enhanced and elaborated in the context of the implementation in Cyprus of the Supervisory Review Process, i.e., Pillar II of Basel II and the Capital Requirements Directive framework.

The aim of the Supervisory Review Process is to ensure not only that banks have adequate capital to support all the risks in their business, but also that they develop and use robust risk

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<sup>12</sup>Regulations on Investor Compensation Fund for Clients of Banks, paragraph 30(5).

[Section 15:28]

<sup>1</sup>Banking Law, section 26(1).

management techniques in monitoring and managing their risks.<sup>2</sup> The Supervisory Review Process comprises two main elements, the Internal Capital Adequacy Assessment Process and the Supervisory Review and Evaluation Process.

In accordance with the Central Bank of Cyprus Directive,<sup>3</sup> banks are under a continuous obligation to implement an Internal Capital Adequacy Assessment Process, i.e., a complex of sound and comprehensive strategies and processes to assess and maintain on an ongoing basis the internal capital that they consider adequate at any time to cover the nature and level of the risks to which they are exposed.<sup>4</sup>

The Internal Capital Adequacy Process entails regular evaluations by each bank of such strategies and processes, to ensure that they remain comprehensive, proportionate, and adequate to the risks the bank is exposed to in view of the nature, scale, and complexity of its activities,<sup>5</sup> in line with the criteria set by the Banking Law.<sup>6</sup>

The Internal Capital Adequacy Assessment Process is complemented by the Supervisory Review and Evaluation Process which is exercised by the Central Bank of Cyprus in relation to all licensed banks in Cyprus on an individual, sub-consolidated, or consolidated basis.<sup>7</sup> In the course of the Supervisory Review and Evaluation Process, the Central Bank of Cyprus evaluates the banks' risk profiles, their capital adequacy, and the reliability of the Internal Capital Adequacy Assessment Process.<sup>8</sup> In addition, it assesses qualitative factors such as the competence of management and corporate governance.

In exercising the Supervisory Review and Evaluation Process, the Central Bank of Cyprus takes into account the principle of proportionality so that "the frequency and the intensity of the review and assessment of each supervised credit institution are

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<sup>2</sup>Banking Law, sections 19A and 26(6) and (8).

<sup>3</sup>Central Bank of Cyprus Directive, Unit A, paragraph 67.

<sup>4</sup>The Central Bank of Cyprus has issued detailed guidelines to banks for the design of their Internal Capital Adequacy Assessment Process; see [http://www.centralbank.gov.cy/media/BCCRDG\\_SupervisoryReviewProcess\\_ICAAP.doc](http://www.centralbank.gov.cy/media/BCCRDG_SupervisoryReviewProcess_ICAAP.doc).

<sup>5</sup>Framework for the Supervisory Review and Evaluation Process, Central Bank of Cyprus, March 2007.

<sup>6</sup>Banking Law, Annex III.

<sup>7</sup>Framework for the Supervisory Review and Evaluation Process, Central Bank of Cyprus, March 2007, at pp. 8–11.

<sup>8</sup>Central Bank of Cyprus Directive, Unit A, paragraph 67.

proportionate to the nature, scale and complexity of its operations, its risk profile and its systemic importance”.<sup>9</sup>

The Central Bank of Cyprus has designed a proprietary Risk Assessment System (RAS)<sup>10</sup> for better assessment of the risk profile of the banks under its supervision and identification of areas on which the supervision should focus through their classification according to a proprietary ratings system.

The Central Bank of Cyprus undertakes on-site supervision as well as off-site supervision. In such examinations, the Central Bank of Cyprus is entitled to request any document, record, or information that it may deem necessary for the assessment of the supervised institution,<sup>11</sup> subject to strict confidentiality obligations<sup>12</sup> on the Central Bank of Cyprus, its employees, and any person commissioned to assist in such inspections.

The planning of individual examinations conducted at each credit institution by the Central Bank of Cyprus is based on the results of a risk assessment for the particular bank under review (risk-based supervision). The activities that are associated with higher net risk levels are given priority in terms of timing and detail.

The methods of supervision available to the Central Bank of Cyprus include trilateral meetings with a bank and its auditors<sup>13</sup> or even bilateral meetings solely with the auditors.<sup>14</sup> Another important element of the Central Bank of Cyprus supervision is its authority to engage in exchange of information both with supervisory authorities of adjacent industries such as capital markets and insurance within Cyprus and with the supervisory authorities of other states.<sup>15</sup>

The Central Bank of Cyprus exercises consolidated supervision covering a bank and its subsidiaries and the associate companies of the bank or of its holding company which are engaged in bank-

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<sup>9</sup>Banking Law, section 26(9); Framework for the Supervisory Review and Evaluation Process, Central Bank of Cyprus, March 2007, at p. 18.

<sup>10</sup>See [http://www.centralbank.gov.cy/media/pdf/BCCRDE\\_SupervisoryReview\\_RAS.pdf](http://www.centralbank.gov.cy/media/pdf/BCCRDE_SupervisoryReview_RAS.pdf).

<sup>11</sup>Banking Law, section 26(2).

<sup>12</sup>Banking Law, sections 28A and 28B.

<sup>13</sup>Banking Law, section 28.

<sup>14</sup>Banking Law, section 28B.

<sup>15</sup>Banking Law, section 27.

ing business and related permitted activities.<sup>16</sup> It also exercises consolidated supervision on banking groups across the EU if the parent bank has received a license to conduct banking activities from the Central Bank of Cyprus. The Banking Law provides for a detailed framework for cooperation between the Central Bank of Cyprus and the supervisory authorities of other EU member states in relation to banks and banking groups active across the EU.<sup>17</sup>

### § 15:29 Duty to report

According to section 24(1) of the Banking Law, every bank must, within four months of the end of each financial year, submit to the Central Bank of Cyprus a copy of the balance sheet and profit and loss account for that year, in the form prescribed by the Central Bank of Cyprus, duly certified by an approved auditor together with a signed copy of his report in the form prescribed by the Central Bank of Cyprus.

The audited financial statements also must be published within six months of the end of each financial year. Additionally, every bank must submit to the Central Bank of Cyprus within fifteen days of the end of each month, or within such other period as the Central Bank of Cyprus may determine, a certified statement of its assets and liabilities at the end of that month in a form prescribed by the Central Bank of Cyprus.<sup>1</sup>

The information disclosed by banks varies, depending on whether they adopt standardized approaches or advanced models for the calculation of their capital requirements. All banks are required to disclose:

1. Information on their risk management objectives and policies for each separate category of risk;
2. Information on the scope of application of the requirements of the Central Bank of Cyprus Directive in the context of the relationship between the particular bank and its subsidiaries;
3. Analytical information on the composition and amount of the bank's own funds;
4. Analytical information on the compliance by the bank with

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<sup>16</sup>Banking Law, section 39. A Central Bank Directive provides for the supplementary supervision of banks which have obtained a license from the Central Bank and which are part of a financial conglomerate.

<sup>17</sup>Banking Law, section 39(7)–(15).

#### [Section 15:29]

<sup>1</sup>Banking Law, section 25(1).

the requirements of the Central Bank of Cyprus Directive in relation to the minimum of own funds required to cover credit risk, market risk, and operational risk, including a summary of the bank's approach to the assessment of its internal capital adequacy to support current and future activities, and compliance with the set minimum capital requirements in relation to credit risk for each of the prescribed exposure classes;

5. Information regarding the bank's exposure to counterparty credit risk, including information on the bank's credit derivatives both for the bank's own use and in relation to its intermediation activities;
6. Analytical information on the bank's exposure to credit risk and dilution risk, e.g., amount of exposure and distribution of exposure by industry and geographical location;
7. For banks calculating the amount of risk-weighted exposure by employing the Standardized Approach (see text, above), information on the approved rating agencies they use for each of the specified exposure classes;
8. Information on the approaches and methodologies used for the treatment of operational risk;
9. Information on any exposure in respect of equities not included in the bank's trading book; and
10. Information on any exposure to interest rate risk on positions not included in its trading book.<sup>2</sup>

Banks that calculate their risk-weighted exposure amount in relation to their credit risk using the Internal Ratings Based Approach should disclose information on the approval of their approach by the Central Bank of Cyprus, an overview of their internal rating systems including the control mechanisms for safeguarding their reliability, a description of the internal ratings process for the various exposure classes, i.e., central governments and central banks, institutions, corporate, retail and equities, and analytical data for each of these exposure classes, e.g., total exposure per class, the exposure-weighted average risk weight, and the bank's estimates of actual outcomes over a longer period.<sup>3</sup> Banks also must submit to the Central Bank of Cyprus information relating to:

1. The establishment or closure of a subsidiary or a branch;
2. A change of name;
3. Any amendment to the memorandum and articles of association;

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<sup>2</sup>Central Bank of Cyprus Directive, Unit A, Annex XI, Part 2.

<sup>3</sup>Central Bank of Cyprus Directive, Unit A, Annex XI, Part 3.

4. The shareholding of the bank in another company if such shareholding exceeds 10 per cent of the share capital of that company;
5. The disposal of the whole or any part of its business by amalgamation or otherwise;
6. The composition of the administrative board and the management; and
7. The appointment, removal, or resignation of auditors.

Additional reporting obligations are provided by the regulatory framework on corporate governance, restricted activities, and the applicable anti-money laundering regulations.

## **V. LICENSING AND REGULATION OF FOREIGN BANKS**

### **§ 15:30 In general**

The relevant licensing section of the Banking Law does not distinguish between a banking business license granted to a legal person established in Cyprus (i.e., a locally incorporated bank) and a banking business license granted to a legal person established in a third country, which registers a place of business (i.e., branch) in Cyprus. Consequently, the licensing requirements applied by the Central Bank of Cyprus are almost identical for both cases.

However, where the applicant is a legal person established in a third country, it must be a bank. If its application is successful, the bank will be granted a banking business license to establish a branch in Cyprus. Importantly, the license is not granted to the branch since it is not a separate legal entity. Once a license is issued the Central Bank of Cyprus will only supervise the activities of the branch in Cyprus.

Branches of banks established in a third country are subject to the same obligations as locally incorporated banks, with respect to their organization, their operating conditions, and accounting and prudential standards. Branches are, therefore, subject to the Central Bank of Cyprus's regulations designed to safeguard the interests of customers, the principle being that users of banking services must be protected in the same way, irrespective of whether the services are provided by a locally incorporated bank or by a branch of a foreign institution.

Accordingly, branches of third country banks also are members of the deposit guarantee scheme. Branches are, however, allowed a certain degree of flexibility with regard to prudential requirements (they may be exempt from solvency requirements and limits on large exposures).



The licensing procedure does not apply to EU credit institutions wishing to establish a branch in Cyprus. As noted previously, credit institutions licensed by competent authorities of another member state of the EU may, under the provisions of section 10A of the Banking Law, establish a branch in Cyprus without the need of obtaining a banking business license from the Central Bank of Cyprus. In order to facilitate such expansion, the Central Bank of Cyprus has issued a guideline document for EU credit institutions seeking to establish branches in Cyprus.<sup>1</sup>

## VI. BANK TAKE-OVERS AND MERGERS

### § 15:31 In general

Bank shares are traded on the Cyprus Stock Exchange in accordance with the Stock Exchange Regulations of 1997 which harmonizes Cyprus law with the *acquis communautaire*. The Regulations, referred to as the “Mergers and Acquisitions Regulations”, provide a number of procedural requirements for those purchasing shares in these companies and those wishing to make a public takeover bid. An offer document is required within 10 days of the announcement of a takeover bid, and it must specify a deadline for acceptance between 30 and 45 days from its becoming available to the public.

However, the Central Bank of Cyprus also has powers both to monitor and control significant shareholdings and Central Bank of Cyprus approval is required before any proposed disposal or amalgamation may be completed.

Additionally, parties involved in a proposed take-over or merger must have regard to potential competition issues. Of particular relevance is the Control of Concentrations between Undertakings Law.<sup>1</sup> Under section 3(2) of the Law, a concentration of undertakings is deemed to arise and be of major importance if:

1. The aggregate turnover achieved by at least two of the participating undertakings exceeds, in relation to each one of them, is €3,417,202;
2. At least one of these undertakings is trading within Cyprus; and
3. At least €3,417,202 of the aggregate turnover of the

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#### [Section 15:30]

<sup>1</sup>See <http://www.centralbank.gov.cy>.

#### [Section 15:31]

<sup>1</sup>Law Number 22(I) of 1999, as amended by Law Number 154(I) of 2000.



participating undertakings altogether relate to the disposal of goods or the provision of services within Cyprus.

If a proposed merger or take-over would give rise to such a concentration, notification of the proposed transaction must be given to the Competition Authority within one week of the agreement, bid announcement, or acquisition of control. Clearance for the transaction to proceed is required. This process is split into two stages, and it may take up to four months to complete.

Additionally, Cyprus competition law generally prohibits agreements between undertakings which prevent, restrict, or distort competition (for example, by price fixing, limiting production, sharing markets, discrimination, or imposition of arbitrary terms) or which are perceived as being an abuse of a dominant position.

## VII. CONCLUSION

### § 15:32 In general

The Cyprus banking system is one of the main pillars of the Cyprus economy and it has been instrumental in the positioning of Cyprus as an international financial center. Both the banking and the anti-money laundering legislative frameworks in place in Cyprus are generally regarded as meeting the highest international standards both in theory and in practice.

In a time of global financial crisis the Cyprus banking system has remained relatively strong thanks to an abundance of deposits by non-residents and a minimal exposure to “toxic assets”. The Central Bank of Cyprus has shown itself to be a robust and prudent supervisory body that has been pivotal in enabling the Cyprus banking system to avoid the significant financial turbulence experienced elsewhere.