



AUDIT  
OFFICE



REPUBLIC  
OF CYPRUS

## **PROCEDURE FOR THE NATURALIZATION BY EXCEPTION OF FOREIGN INVESTORS**



**AUDIT OFFICE OF THE REPUBLIC  
SPECIAL REPORT no. ΥΠΕΣ/01/2020**

**PROCEDURE FOR THE NATURALIZATION  
BY EXCEPTION OF FOREIGN INVESTORS**

**AUDITED ENTITIES:**

**Ministry of Interior**

**Ministry of Finance**

**Tax Department**

# 1 Summary

Within the framework of the measures encouraging direct foreign investments and attracting individuals of high income levels to settle and become active in Cyprus, in 2013 the Council of Ministers implemented the «Cyprus Investment Programme», which underwent relevant amendments from time to time.

In July 2019, our Office launched an audit, regarding the implementation of the Programme, requesting data from the Civil Registry and Migration Department. In the meantime, and while expecting the data, within the framework of another audit for the examination of the procedures of chartering aircrafts by the Presidency of the Republic, it appeared that the owner of such an aircraft is a foreigner, who was naturalized in the beginning of 2015, under this Programme.

It was therefore decided to audit the specific procedure of naturalization. The aim of the audit was the investigation of the procedures which the Ministry of Interior and the Ministry of Finance followed during the granting of Cypriot citizenship to a foreign citizen and whether he and other persons who participated in transactions in the context of the relevant investments, were properly tax handled by the Tax Department.

The application for naturalization was submitted collectively for the three siblings (one is the above mentioned, who owned the aircraft) and three other persons, that is, a total of six persons. These persons received Cypriot citizenship by a Decision of the Council of Ministers, dated 14.1.2015. With the granting of Cypriot citizenship to the above 6 persons, citizenship was also granted to 36 members of their families (spouses and children), 19 of which were members of the family of the three siblings. For the acquisition of Cypriot citizenship by the spouses and children of the applicants no additional investments were required.

The naturalization was carried out according to the financial criterion A8 «Collective Big Investments», on the basis of which each applicant could invest €2,5 million, inter alia, on immovable property, developments and infrastructure projects or on the purchase of Cypriot businesses, as long as the collective investment was at least €12,5 million.

According to the criteria set, the six persons should have invested at least €15 million (6 persons \* €2,5million). The market value of the permanent owned residence of the applicant investor in Cyprus is not included in the above amount, with the exception of the case in which the investor decides to invest in the purchase of only one residence, valued at more than €2,5 million, in which case he is not obliged to purchase an additional permanent owned residence with a market value of €500.000.

For the reasons which are extensively explained in the present Report, the approval of the application did not comply with the criteria which applied at the date of its examination and therefore the application for naturalization, in our opinion, should have been rejected.

The investments included the purchase of a company. The purchased company had, when it was purchased on 2.10.2014, as its sole assets, a villa (which was built in 1999) and the surrounding land. According to the general valuation, dated 1.1.2013, the value of the villa with the surrounding land was equal to €2,7 million and according to the most recent market prices its value was equal to €3,5 million. With the submission of the application for naturalization, an un-audited statement of financial position of the company as of 30.9.2014 was also submitted. This statement was signed by the Director of the company and the contracting parties, and appears to be an integral part of the above contract, dated 2.10.2014. In this statement the assets of the company are declared as having a value equal to €7,5 million.

On the basis of the above, if the transaction of the acquisition of the villa and the surrounding land had been processed through the Department of Lands and Surveys (and not through the Registrar of Companies in the form of the purchase of the company), then immovable property transfer fees would have been paid on the value of the immovable properties which had been declared to the Ministry of Interior as being equal to €7,5 million.

Also, if the transaction of the acquisition of the villa and the surrounding land had been processed through the Department of Lands and Surveys, then an obvious difficulty would exist, for a property which was so recently purchased for the amount of €3,5 million (and had a value of a general valuation equal to €2,7 million) to be presented to the Department of Lands and Surveys as having a value equal to €7,5 million. In this case, even if the declaration concerning the value of the property was accepted, an amount of capital gain tax would automatically arise, having as a basis the amount of €7,5 million and not the amount of €5,5 million which was later declared to the Tax Department, as the value of the property of the company.

Therefore, by approving the application, at the time when it was obvious that there was an overpricing («inflation») of the declared values of the property, the State lost taxes and fees of around €1 million.

The specific relaxation of the criteria was not created especially for the case of the naturalization of the six investors under examination, however, in this specific case, there was a loss of tax income and immovable property transfer fees, even though the Tax Department was informed. In essence, the Ministry of Finance applied criteria which did not have the approval of the Council of Ministers and, due to its actions, there was a loss of tax income of around €1 million.

We do not have evidence which proves that the naturalized persons remained as the beneficiaries of the company which acquired the immovable property and of the company to which the villa belonged for the period of three years as required by the Programme. It also appears that there is no procedure in effect at the Ministry of Interior for examining this aspect. However, it is a fact that information was submitted to us that at least 2 of the naturalized persons, including the naturalized person under reference who is the owner of the aircraft, continue to have business activities in Cyprus.

From an investigation conducted by our Office, it was determined that, according to data of the Department of Lands and Surveys, the «Value of General Valuation» of immovable properties which were purchased in October 2014 for €20.245.000 (€19.806.723 + €438.277 as VAT), on 1.1.2013 and on 1.1.2018 amounted to only €9.397.000 and €9.101.900, respectively. A distortion of overpricing arises which may possibly be due to the existence of mediators and/or the taking advantage of the foreign investors by local businessmen and/or to other reasons which are related to unsound practices or to a combination of the above.

The question which arises, regarding the villa, relates to the allocation of the money which corresponds to the difference between the actual value of the immovable property and the amount of €7,5 million which was paid, and why the Tax Department did not seek all those who received amounts, possibly in the form of commissions, so that it is assured that, at least, they will pay the corresponding tax. A similar audit should have been also conducted for the other transactions of the specific procedure, as well as, in general, with every similar transaction of the investment Programme. Also, it appears that possibly the Unit for Combating Money Laundering (ΜΟΚΑΣ) should have been informed about the possibility that some of the local businessmen who received the inflated (compared to the actual value) amounts, paid commissions outside the framework of the legislation.

The companies of the naturalized persons have not submitted any tax returns since 2014. The Tax Department informed us that these companies have been asked to submit tax returns and in the

event that they do not do so within the time period given to them, then the Department will proceed with their criminal prosecution.

Our Office considers the role of the three-member Committee which was appointed on 6.11.2019 by the Council of Ministers as very important<sup>1</sup>. To avoid a possible unnecessary parallel audit, our Office will not proceed with the wider audit of the granting of the Cypriot citizenship which we had decided to launch in July 2019. This however does not stop our Office from proceeding with the audit of individual cases, such as the present one, if it deems it necessary. Neither do we consider that the powers held by our Office can be restricted due to the appointment by the Council of Ministers of other audit bodies or committees, without this meaning in any way that we do not recognize the authority of the Council of Ministers to proceed with such appointments, according to the Commission of Inquiry Law or otherwise.

On the basis of section 4 of article 111 of the Civil Registry Law, as amended in 2019, from 31.1.2020 onwards, the naturalization of foreign investors is prohibited, except if the terms and conditions as defined in the Regulations are fulfilled, which are drawn up by the Council of Ministers and approved by the House of Representatives. We consider that this will become a strong safety net for the protection of the Programme from distortions and we suggest that, both the Council of Ministers and the House of Representatives, take into account the findings of the present Report, so that they introduce the appropriate provisions in the said Regulations, with the aim that they become effective.

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<sup>1</sup> The task of the Committee was to examine whether all cases of investor naturalization from 2007 to May 2018 had been approved in accordance with the applicable regulations and criteria at the time of the approval of their application