

At a glance: security interests and guarantees in Cyprus

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Security interests and guarantees

Collateral and guarantee support

Which entities in the organisational structure (eg, parent companies, holding companies and sister companies) typically provide collateral and guarantee support for bank loan financings? Are there limitations (regulatory, tax or otherwise) on which entities in the organisational structure are permitted to provide (or are customarily selected to provide) such support?

Typically, parent companies provide collateral to creditors (directly or through a security agent) to secure obligations of their subsidiary, being the primary debtor. Other group companies may also provide collateral and guarantees.

What types of obligations (eg, swap and hedging obligations or treasury services obligations) typically share with the bank loan obligations in the collateral and guarantee support? If so, are all such obligations equally and ratably covered by the collateral and guarantee support?

Cyprus banks typically require collateral over the current and future assets of the debtor (or the security provider) as security for credit facilities. Such assets may include movable and immovable property. Guarantees are also typically requested as security, which see the security provider guarantee the obligations of the primary debtor. Overall, typical securities given to secure obligations under bank loans comprise share pledges, fixed and floating charges, mortgages, assignments of receivables and guarantees.

Commonly pledged assets

Which categories of assets are commonly pledged to secure bank loan financings? Describe any limitations on the pledge of assets.

Pledges over the following assets are regulated under statute:

- share certificates;
- bonds (except as secured by mortgage of immovable property);
- promissory notes; and
- bills of exchange.

A pledge over share certificates can be created under statute. A secured creditor who has a pledge in a Cyprus law pledge over share certificates can enforce the pledge (to sell or appropriate the shares concerned) without recourse to court (ie, Cyprus law allows for out-of-court enforcement of a pledge over share certificates).

Creating a security interest

Describe the method of creating or attaching a security interest (or other lien) on the main categories of assets.

Pledges over shares

Pledging share certificates is a common form of security in financing transactions in Cyprus. A share pledge aims to achieve actual or constructive delivery of possession over the share certificates. In the event of default by the debtor, the pledgee may obtain ownership of the shares pledged or proceed to sell the shares, without having to obtain a court order.

Regarding dematerialised securities, a charge can be taken over the special account of the investor's share account.

Fixed charges

Fixed and floating charges are also regularly used as collateral to secure obligations under an underlying facility. A charge does not grant proprietary rights or interests in the relevant assets but rather provides rights over the asset and proceeds derived from the asset, for the purpose of securing the underlying debt obligations. A fixed charge applies on specific assets with a view to preventing dealings with or disposal of such assets (such as, for example, bank accounts).

Floating charges

A floating charge is a security interest that 'floats' until an event of default occurs or the company goes into insolvent liquidation, at which time the floating charge 'crystallises' and attaches to the relevant assets. In practice, floating charges are usually placed over the entire assets and undertaking of the entity granting the security.

Assignments

Other types of security include the assignment of receivables or contractual rights.

Mortgages

Real estate can be mortgaged to secure the borrower's obligations.

Perfecting a security interest

What steps are necessary to perfect a security interest (or other lien) on the main categories of assets? What are the consequences (including in a bankruptcy or insolvency proceeding) of failing to perfect a security interest (or other lien)?

In certain cases, the security interest created under contractual arrangements must be filed with the Cyprus Registrar of Companies (the Registrar). A security not duly registered will be invalid against a liquidator where the company concerned is placed in winding-up.

For all security granted by a Cyprus company, details of the security must be entered in the register of charges of the company. Additional perfection requirements apply to certain pledges, including a pledge over share certificates.

Regarding equitable securities such as assignments and charges, a common law perfection requirement provides that the first security holder must give notice to the relevant contracting third party, to gain priority over the remaining equitable interests in the property.

A legal mortgage over immovable property must be registered with the Land Registry. Once registered, a charge over the property is created and dealings with the property are restricted.

Agreements and ancillary documents concerning property or proprietary rights situated in Cyprus or matters to be performed in Cyprus, irrespective of where the document is signed (subject to certain exceptions), are subject to stamp duty in Cyprus. Stamp duty is not a perfection requirement, but is a prerequisite for enforcement of the document concerned in Cyprus courts, among other purposes.

Special rules apply with respect to charges over certain assets such as aircraft and ships, which involve separate registration requirements.

Future-acquired assets

Can security interests (and other liens) extend to future-acquired assets? Can security interests (and other liens) secure future-incurred obligations (eg, post-closing drawings under a revolving credit facility)?

An equitable charge, assignment, lien or charge can be granted over future property.

A legal mortgage cannot be granted over future property.

A pledge can be granted over shares a company issues in the future, subject to satisfying certain requirements under Cyprus law.

Maintenance

Describe any maintenance requirements to avoid the automatic termination or expiration of security interests (and other liens).

Parties are free to contractually agree on specific maintenance terms.

Release

Are security interests (or other liens) on an asset automatically released following its sale by the debtor? If so, are the releases mandated by law or contract?

The terms of release of a security can be contractually agreed between the parties.

On release of a security, relevant entries should be made in the corporate registers of the entities concerned.

Where the security is also registered with the Registrar, a relevant notice must be filed with the Registrar to deregister the charge registered against the security provider.

To release a legal mortgage over immovable property, the parties must carry out certain formalities with the Land Registry.

Non-fulfilment of guarantee obligations

What defences does a guarantor have against claims for non-fulfilment of guarantee obligations? Can such defences be waived?

Cyprus law provides for certain defences for guarantors under which their contractual obligations are automatically discharged, which would depend on the precise circumstances.

Unless otherwise provided in the relevant agreement, mere failure by the creditor to initiate legal proceedings or take remedial measures against the principal debtor does not release the guarantor from its guarantee obligations.

In the case of co-guarantors, the discharge of one guarantor by the creditor does not presuppose the discharge of the others, nor the released guarantor is discharged from liability against the other guarantors.

Lastly, where a guarantee is declared void, the person who has gained any benefit under the guarantee is obliged to restore such benefit or pay damages to the person from whom such benefit was obtained. Circumstances that can lead to a guarantee being declared as void include fraudulent misrepresentation and non-disclosure of material facts to the guarantor in relation to the guaranteed transaction.

Parallel debt requirements

Describe any parallel debt or similar requirements applicable in a secured bank loan financing where an agent acts for multiple investors.

Cyprus does not prevent an agent from acting for multiple investors in a financing where a Cyprus company is being financed. An agent can also conclude security arrangements with the borrower and security providers on the part of multiple investors.

Enforcement

What are the most common methods of enforcing security interests (and other liens)? What are the limitations on enforcement (including bankruptcy and insolvency regulations)?

Typically, the financing and security documentation will regulate enforcement of securities in an event of default or otherwise.

A Cyprus law-governed pledge over share certificates can be enforced out of court and the pledgee has the right to sell the pledged share certificates and charged shares.

A floating charge will crystallise over the secured assets in the event of default. The secured lender (or its receiver) may then liquidate the securities in settlement of the owed debt. Unless crystallised prior to the commencement of the liquidation or under their terms, floating charges will rank for payment after liquidation costs and preferential payments. However, floating charges that are not crystallised would rank before other unsecured creditors to the extent that the company's existing assets do not suffice to satisfy unsecured creditors.

A common enforcement mechanism is the appointment of a receiver over the assets of the debtor company, which can take place out of court. A receiver is typically envisaged under floating charges. An appointed receiver can sell the debtor's assets to satisfy the secured debt.

Fraudulent conveyance and similar doctrines

(Briefly) Describe the impact of fraudulent conveyance, financial assistance, thin capitalisation, corporate benefit and similar doctrines on the structure of bank loan financings (including in the context of acquisition financing).

Fraudulent preference

Any conveyance, charge, mortgage, delivery of goods, payment, execution or similar act that took place within six months before the commencement of a winding-up may be considered as a fraudulent preference and be set aside. A preference is fraudulent if it is intended to put a creditor in a better position on liquidation of the company than they would have otherwise enjoyed. Creditors of a fraudulent preference must repay any benefit obtained.

Financial assistance

Financial assistance is prohibited by a company for the purchase of, or subscription for its own shares, or those of its holding company. English case law offers guidance on the definition of financial assistance, where it is apparent that the granting of any loan, guarantee or security falls within the meaning of financial assistance. The Cyprus Companies Law, Cap. 113, as amended, provides for financial assistance whitewashing in respect of a private company.

Corporate benefit

Directors owe a duty to act in good faith for the benefit of the company. The company's benefit in acting as a guarantor is easier to prove when it concerns a subsidiary in a downstream guarantee, in contrast to a subsidiary providing guarantee to the parent in an upstream guarantee, or by a group company in a cross-stream guarantee. Corporate benefit may also be difficult to establish where the amount guaranteed exceeds or equals the asset value of the guarantor.

In addition, directors owe fiduciary duties to the company including the general duty to avoid conflicts of interest. A director of a company who is in any way, whether directly or indirectly, interested in a contract or a proposed contract with the company is under a duty to declare the nature of their interest.

Thin capitalisation

There are no thin capitalisation restrictions under Cyprus law. However, there are general anti-avoidance rules in place and professional tax advice should be obtained on a case-by-case basis.

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