

San Marino

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San Marino: a new financial centre for collective investment services

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Cogniti nobisque incogniti aliis (known to ourselves and unknown to others): for centuries this Latin motto has been the guiding principle for the policy of the Republic of San Marino in international relations. This policy of discretion granted the Republic independence for more than 1700 years, since its foundation in AD 301, and allowed it to become the world's oldest Republic and Europe's oldest existing state.

This was possible even though its location exposed San Marino to shocking events in European history during this period, and even though San Marino is only a small mountain in the Italian peninsula with no army.

Sitting out of the race

The constant application of a policy of discretion has produced positive effects on the economy as well, especially in the last three decades. Although like many small countries it has limited need for a state budget, San Marino has not participated in the international race to the bottom for tax rates.

Companies are subject to a fairly ordinary 19% (15% from next year) tax rate. However, in practice tax rate may be even lower if special regimes are applied. These regimes exist for holding companies, companies holding intellectual property and companies providing intra-group services. In these cases, the effective tax rate can be either 6.5 % or 0%. No withholding tax is applied to dividends.

Although it does not appeal to extreme tax planners, the tax treatment of companies in San Marino was and is interesting to operators desiring substantial tax savings without the inconvenience of dealing with an over-

exposed offshore centre and with the advantage of a company located in the centre of Europe. This has produced a good amount of foreign investments but not a rush to San Marino.

Furthermore, the flow of foreign investors toward San Marino has not been a free one. Incorporating a company in San Marino was not easy until the enactment of the 2004 company law reform. An authorization, given by the government after close scrutiny of the applicant, was required for the incorporation of a Sammarinian company. Hence instead of being known and employed by many, San Marino was chosen by a few distinguished investors, so overexposure in international tax planning was not a problem.

Nobody could accuse San Marino of declaring a tax war against onshore countries, and tax administrations of many on-shore countries did not even take notice of San Marino and did not treat it as an offshore centre.

A fundamental choice

Until a couple of years ago, the financial sector was not much developed either. This was due to the lack of an adequate legal framework for advanced financial operations. The banking sector, on the contrary, flourished because of the traditional secrecy applicable to Sammarinian banks. However, San Marino could not be called a financial centre at the turn of the century.

The government faced a fundamental choice when, at the beginning of the new millennium, a decision about the future of the Sammarinian economy was to be taken: whether to become a financial centre or an offshore centre. The choice was clear: it would be a financial centre.

Since then the Sammarinian legal market has become very exciting. Law commissions have flourished. Many new laws have been enacted: the trust law, the company law, the new law on banking and financial sector, the registry law for aircraft and boats. Regulations

have been issued for insurance and investment funds. All this occurred in a short time: only months passed between the decisions and the actions.

These innovations are implanted in a very stable and traditional legal system – the Sammarinian legal system is still based on Roman law, or more specifically on the *ius commune* – and in a financial system governed by a central bank. The San Marino Central Bank has internationally renowned experts in its ranks, and works closely with the Bank of Italy as part of the international financial system and giving particular attention to the question of money laundering.

San Marino's international relations will certainly help its development as a financial centre. The jurisdiction became a member of the UN in 1992. Although it is not a member of the EU, San Marino has entered into a cooperation agreement with the EU, and is treated as belonging to the EU customs territory. It has also signed various treaties of friendship with Italy. San Marino courts enforce foreign judgments in all cases, except when they contravene Sammarinian public policy.

San Marino only recently entered into the circus of tax treaties but it has done so with good results. It has signed tax treaties with several countries, many of which are leading financial centres (such as Luxembourg, Malta, Cyprus and Austria), obtaining exemption from withholding taxes on flows of interests, royalties and dividends in most cases.

To all these aspects add a long-standing tradition of bank secrecy – whose violation is punished with criminal sanctions – and the recipe is complete.

When you do good things and you do them during a short period of time, it is difficult to maintain a low profile in today's global economy. In December 2006, David Lane published an article in *The Banker* describing San Marino as a “microstate with macro ambitions”, and expressly affirmed that “over the past three years, the tiny state of just

30,000 inhabitants who pack into a small enclave completely surrounded by Italy, has taken measures to make itself attractive to savers, investors, bankers, insurers, lawyers and others who make their living from finance”.

This is a fair representation of what is happening in San Marino. The new legal framework for the financial sector will make it difficult for San Marino to remain “unknown to others” for long. The expected development of an investment fund industry will increase San Marino’s visibility as a financial centre.

Investment funds under Sammarinian law

Under Sammarinian Law, a mutual fund is a sort of unit trust, managed by a *società di gestione* (fund management company). Equity interests in the trust are issued with the purpose or effect of pooling investors’ funds to spread risk and enabling investors to receive profits or gains from the acquisition, holding, management or disposal of investments.

Investment funds are subject to Law 165, the general law on companies, banking and insurance services. They are also subject to the Collective Investment Services Regulations and the recent Accounting Regulations for Mutual Funds. The latter completed the legal framework for investment funds.

The *società di gestione* needs to be authorized by the Central Bank. The regulations impose strict requirements on its shareholders, to insure that they have a good reputation, and provide prudent administration. Member of the board of the *società di gestione* have to meet strict independence and professionalism requirements.

The regulations allow several types of investment funds: open-ended funds, closed-ended funds, funds intended for the general public (retail), reserved funds, alternative funds and guaranteed funds.

Ucits III-type funds are also expressly contemplated and a convention with Italy is under discussion for the distribution of such funds in Italy and the EU.

The regulations contain rules for mergers between funds, the role of the depository bank and a code of conduct to avoid conflicts of interest and excessive frequency of transactions, and to ensure their best execution.

Finally, the regulations set clear rules about cross-border operations, obliging foreign funds to be authorized.

Income produced by the assets included in the investment fund are exempted from income tax, with the exception of rents or capital gains from real estate located in San Marino, which are taxed according to the ordinary rate applicable to commercial companies (17%).

No withholding taxes are levied on the distribution of income from the investment fund or on the capital gains realized by investors when they sell their share in the fund. In certain cases, when the recipient is an EU resident, the withholding taxes imposed according to the EU Savings Directive apply.

Income of companies managing investment funds is taxed at 12%. Furthermore, these companies get a tax credit amounting to 25% of net consideration paid to their employees, further supporting the establishment of investment funds in San Marino.