

# Features of the Malta tax system

## About Malta

Malta is located in the Mediterranean sea, ninety-three kilometres south of Sicily and 290 kilometres north of Libya. On 1 May 2004 the island became an EU member state and adopted the Euro currency on 1 January 2008.

The English language is an official language in Malta together with Maltese. English is widely spoken and is also the language of legislation, education and business.

## Taxation system

### General

Malta has one of the lowest OECD compliant tax rates within the EU area. Investors can set up tax efficient structures in Malta and benefit from the interaction of the full imputation system of company taxation (whereby dividends carry a tax credit equivalent to the tax paid on the profits out of which the dividends are paid) and the general tax refund system which was also approved by the European Commission in late 2006.

Repatriation of profits is tax free as Malta does not charge any withholding taxes on payment of dividends to non-residents. In addition, interest and royalties paid to non-residents are also free

of tax, increasing the potential for efficient tax planning.

The absence of transfer-pricing rules, thin capitalisation regulations, CFC regulations or annual wealth taxes is an added bonus to investors.

Other tax related benefits in setting up a company in Malta include:

- Dividends received from a participating holding are exempt from tax in Malta so long as certain conditions are satisfied. Proper structuring enables compliance with the said conditions in the vast majority of scenarios

- Gains on the sale of a participating holding are exempt from tax in Malta
- Where the holding of shares in a foreign company does not qualify as a participating holding, tax on dividends and gains is reduced with the application of double taxation relief, namely treaty relief, unilateral relief and flat rate foreign tax credit
- Non-residents are not taxed on gains realised on the sale of securities in Maltese companies, provided that they are not held in a company whose assets consist principally of immovable property situated in Malta.
- So-called “non-dom” companies benefit from the taxation of foreign income solely to

the extent it is remitted to Malta. Foreign gains are not taxed in Malta.

- Companies may be re-domiciled inwards and outwards; no exit taxes are chargeable.
- Malta has a wide treaty network with over 50 countries (see list hereunder under Tax Treaties).

International companies that have set up a base in Malta include:

- insurance sector – Aon Marsh, Munich Re, JLT Insurance, Heath Lambert, Heritage, Nissan, White Rock and Willis; BMW and Vodafone set up their insurance captive in Malta
- fund administrators – AXA, Custom House, HSBC, TMF
- banks – Banif, Deutsche Bank, Fortis, HSBC, Raiffeisen, Saadgroup, Volksbank



## Participating holdings

A holding of shares in non-Maltese entities (companies and partnerships *en commandite* the capital of which is divided into shares) qualifies as a participating holding when any of the following conditions is satisfied:

- a company holds directly at least ten per cent of the equity shares of a company not resident in Malta whose capital is wholly or partly divided into shares, provided that where the shares held confer different percentages of entitlement with respect to votes, to profits available for distribution and to assets available for distribution on a winding up, the lowest percentage figure shall be deemed to be the percentage of equity shares held; or
- a company is an equity shareholder in a company not resident in Malta and the equity shareholder company is entitled at its option to call for and acquire the entire balance of the equity shares not held by that equity shareholder company to the extent permitted by the law of the country in which the equity shares are held; or
- a company is an equity shareholder in a company not resident in Malta and the equity shareholder company is entitled to first refusal in the event of the proposed disposal, redemption or cancellation of all of the equity shares of that company not held by that equity shareholder company; or
- a company is an equity shareholder in a company not resident in Malta and is entitled to either sit on the Board or appoint a person to sit on the Board of that company as a director; or
- a company is an equity shareholder which invests a minimum sum of one million, one hundred and sixty-four thousand Euro (1,164,000) (or the equivalent sum in a foreign currency) in a company not resident in Malta and that investment in the company not resident in Malta is held for an uninterrupted period of not less than 183 days; or
- a company is an equity shareholder in a company not resident in Malta and where the holding of such shares is for the furtherance of its own business and the holding is not held as trading stock for the purpose of a trade.

Investments by Maltese companies in the capital of partnerships *en commandite* the capital of which is not divided into shares qualifies as a participating holding so long as any one the conditions set out above is satisfied.

### Participation exemption

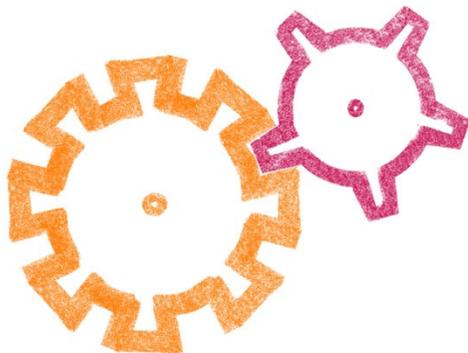
The participation exemption rules provide for the following exemptions:

Gains on the sale of a participating holding - gains are always exempt from tax in Malta wherever the foreign entity is situated. Most of the Malta double taxation treaties provide that gains realised by a Malta company on the sale of shares in foreign companies, provided that the assets of the foreign companies do not consist mainly of immovable property situated in that other contracting state, are taxable solely in Malta. With the provisions of the participation exemption, the gain is not subject to tax. The gain may then be distributed by the Maltese company to a non-resident without the imposition of withholding taxes.

Dividends received from a participating holding - dividends received by a Malta company from a participating holding are exempt from tax when:

- The foreign company or partnership (hereinafter referred to as “entity”) is situated in another EU member State; or
- The income of the foreign entity does not consist of more than 50% of passive interest and royalties; or
- The profits of the foreign entity are taxed at the rate of at least 15%; or
- The holding is not a portfolio investment and the income and interest and royalties received by the foreign entity is subject to foreign tax of at least 5%.

**Note** – a foreign company carrying on treasury functions or IP licensing for the group may be deemed not to be one which is in receipt solely of passive interest or royalties. A ruling may be obtained that the company is actively trading and therefore the participation exemption may still apply.



#### Practical applications

Malta may be used to repatriate profits from low tax jurisdictions into the EU. Equally, in the absence of withholding taxes on dividends, interest and royalty payments, profits may be transferred out of Malta to low tax jurisdictions.

## Holdings not qualifying as participating holdings

If the holding of shares does not qualify as a participating holding, then the gains and dividends are taxed in Malta at the rate of 35%. However, upon the distribution of these profits and gains to the shareholders, the latter may claim a tax refund of the tax paid by the company on the profits so distributed. The tax refund can amount up to six-sevenths ( $\frac{6}{7}$ ) of the tax credit.

Alternatively one may claim flat rate foreign tax relief whereby the effect is that the initial rate of tax is reduced from 35% to 18.75%. A tax refund may also be claimed but this will amount to  $\frac{2}{3}$ <sup>rd</sup> of the Malta tax credit.

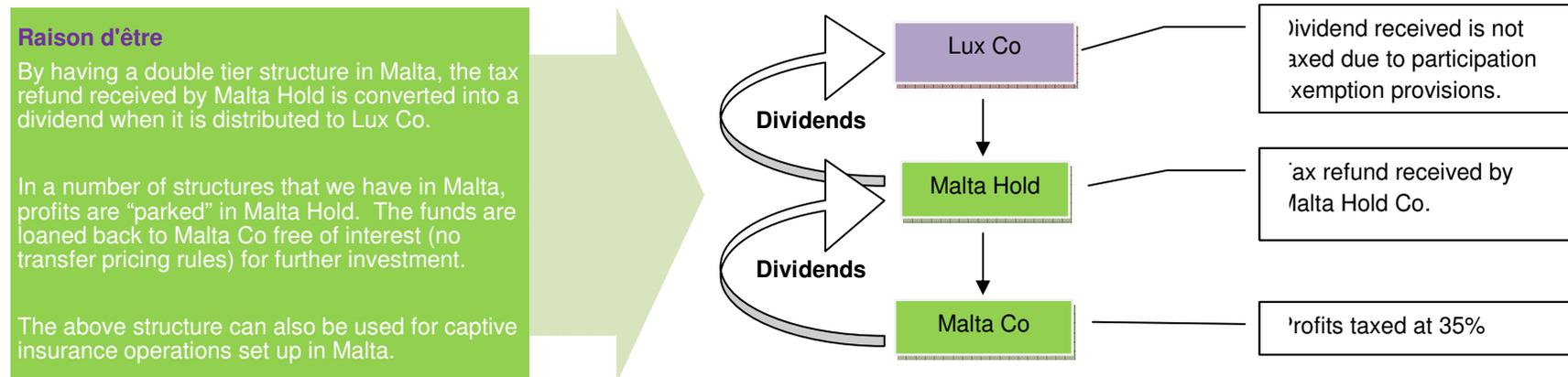
### Tax refund provisions

The corporate income tax rate in Malta is a flat 35%. However, upon the distribution of dividends, the shareholder may claim a refund of six-sevenths ( $\frac{6}{7}$ ) of the tax credit if the dividend is distributed from active trading income and five-sevenths ( $\frac{5}{7}$ ) when it is distributed out of passive interest and royalties.

We generally set up a two-tier structure in Malta, a holding company and a subsidiary. The subsidiary may carry out both trading activities and investment activities.

Consider a structure where Lux Co holds the shares in Malta Co. Assuming Malta Co's trading profits amount to 100, tax payable in Malta is 35. Malta Co distributes all post tax profits and Lux Co claims a tax refund of 30. Such a structure will not work since even though the dividend is not taxed in the hands of Lux Co as a result of the participation exemption provisions, the tax refund received by Lux Co will be taxed as other income in Luxembourg. The tax refund is not a dividend.

For this reason a double tier structure is used in Malta as follows:



### Non-dom companies

Companies incorporated and managed and controlled in Malta are in terms of our tax legislation both domiciled and resident in Malta. They are taxed on their world-wide income and capital gains, subject to certain exemptions. In addition when such companies have foreign branches, branch profits are subject to Malta tax with relief for foreign taxes.

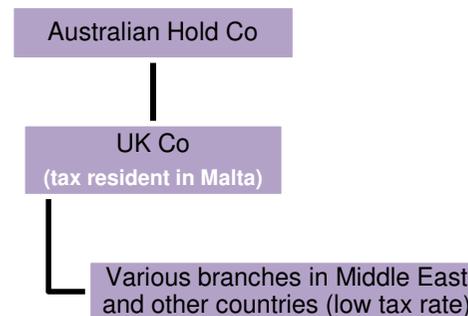
Foreign companies (companies incorporated outside Malta) are generally taxable in the jurisdiction in which they have been incorporated. However, their tax residence may be moved to Malta by transferring the effective management and control of their business to Malta. In such cases, though the companies become resident in Malta for tax purposes, they are still foreign companies and in accordance with the provisions of our tax legislation, they are not domiciled in Malta.

The following tax principles apply to companies resident but not domiciled in Malta:

- a. Income and gains arising in Malta are taxed in full in Malta (tax refund provisions also apply when profits are distributed by way of dividend);

- b. Income arising outside Malta is taxed in Malta but only to the extent that such income is remitted to Malta;
- c. Gains arising outside Malta are not taxed in Malta even if such gains are remitted to Malta.

We have created a number of structures using this methodology and below is an example of one of the structures:



In this case, UK Co did not have any activities in the UK. The profits of UK Co's foreign branches were subject to UK corporation tax (world-wide basis of taxation). Australia also introduced the participation exemption and dividends from the UK Co were not subject to tax in Australia.

Management and control of UK Co was transferred to Malta. UK Treasury consent was obtained. The effect of this transfer of management and control may be summarized as follows:

- a. UK Co became resident for tax purposes solely in Malta; it is, however, not domiciled in Malta;
- b. Foreign branch profits are not taxed in the UK; they are taxable in Malta only on the amount that is remitted to Malta. In practice we negotiate a tax leakage of about 1.5% to 2% with the Maltese authorities, a much lower amount of tax than that previously paid in the UK.
- c. Dividends distributed by UK Co are not taxed in Australia in view of the participation exemption provisions in Australia.

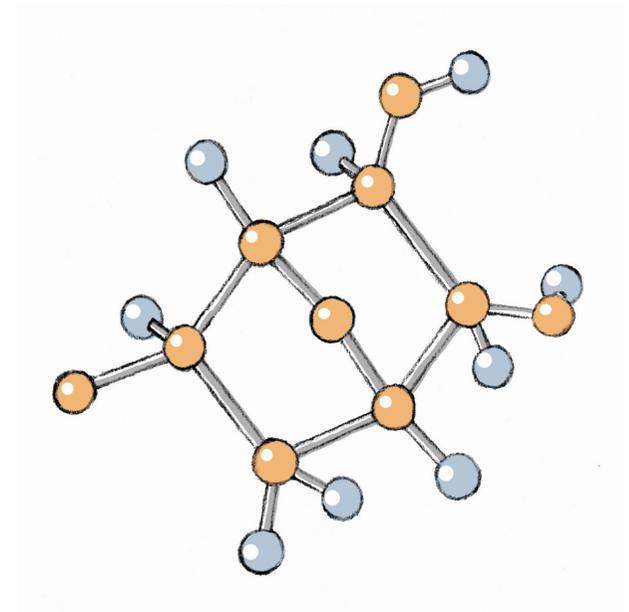
The same Non-dom Companies principle can also be applied to:

- cash box companies with a considerable cash balance for investment purposes
- loan and financing operations (under Maltese legislation no transfer pricing regulations exist with respect to inter-company loans)
- IP licensing and royalty companies

## Tax treaty countries

Albania	Hungary	Pakistan
Australia	Iceland	Poland
Austria	India	Portugal
Barbados	Ireland	Romania
Belgium	Isle of Man (wef 1.1.11)	San Marino
Bulgaria	Italy	Singapore
Canada	Korea (rep)	Slovak Republic
China	Kuwait	Slovenia
Croatia	Latvia	South Africa
Cyprus	Lebanon	Spain
Czech Republic	Libya	Sweden
Denmark	Lithuania	Syria
Egypt	Luxembourg	Tunisia
Estonia	Malaysia	UAE
Finland	Montenegro	UK
France	Morocco	
Germany	Netherlands	
Greece	Norway	

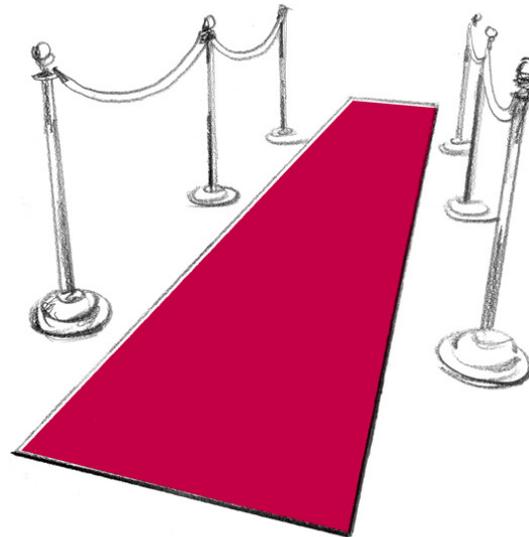
Treaties have been signed with Georgia, Jersey, Qatar, Russia, Serbia, Switzerland and the USA and are awaiting ratification.



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