

FACT SHEET 1 – THE MALTA COMPANY

Introduction

Maltese companies remain one of the most popular vehicles in Europe for the purposes of international trade. A Maltese company is a normal limited liability company that would be charged to tax at the rate of income tax applicable at the time (currently 35% on its chargeable income or net profits) and both Malta residents and non-residents may hold any amount of shares in this company.

The shareholders of the company may be entitled to refunds of tax as applicable to their particular circumstances. In particular, any resulting dividends to non-resident shareholders may qualify for treaty relief in the receiving jurisdiction. Incidentally, Malta has double taxation agreements in place with most of the major European states and a number of other states around the world as will be seen later.

Moreover, Malta recognizes the fact that certain dividends would generally represent income generated outside of Malta. Consequently, where this income is paid out to non-resident shareholders, the dividend distribution will trigger off a series of **refunds of tax** to the said non-resident shareholders.

Tax is paid in the same currency as the company's share capital, which is also the currency in which the company draws up its annual financial statements. The Tax refund is also paid in the same currency, thus there exists no exchange risk for the company.

In terms of the provision of current tax legislation, the Inland Revenue in Malta must pay a tax refund within 14 days from the end of the month in which it falls due. A tax refund is considered to fall due when the audited financial statements and a complete and correct income tax return of the Malta Company are submitted to the tax authorities, the tax due is paid in full and an appropriate application for the refunds is submitted by shareholder or his representative.

The Malta Company fits well and may be used in a variety of scenarios. Besides the actual trading of commodities, good and services, amongst others, a Malta Company can be set up to:

- carry out a Group Treasury function;
- act as Royalty Agent;
- carry out a Commission Agent function and similar situation;

- function as Special Purpose Vehicle;
- act as investment services company.

The fiscal benefits associated with the Malta Company arise once the Company distributes its profits to its shareholder/s. A shareholder may wish to retain the funds in Malta or in the Company itself, or alternatively have them repatriated to a country of his choice.

Malta's unique tax system

Malta's tax system is a full imputation system, the only one of its kind in the EU, which treats residents and non-residents in the same way and is therefore non-discriminatory and does not fall foul of EU law on this count.

A full imputation system that entitles shareholders to claim a credit for the tax paid by the company and ensures that distributions out of taxed company profits are not subject to further tax in the hands of the shareholders and in certain cases the distribution of a dividend entitles the shareholder to a tax refund.

The only feature in Malta's imputation system which required amendment to be fully compliant with ECJ decisions on imputation systems was to allow a credit for foreign underlying corporate tax to individuals in addition to companies where such a credit was already available. Such amendment strengthened the harmony of our tax system by not discriminating in favour of the corporate form.

EU Agreement Background

Apart from this minor amendment to the full imputation system, other changes were necessary to reflect the agreement which Malta reached with the EU Commission, through the EU's Code of Conduct Group for Business Taxation, as regards our tax rules as they apply to Maltese companies operating the Foreign Income Account. While Malta was not in agreement with the Commission that these elements in our tax system constitute State Aid, in the interests of stability and certainty, Malta sought to reach agreement with the Commission on a revised tax system with appropriate transitional arrangements. The Commission sought to ensure that the Maltese Government proposals did not grant unfair advantage and conformed with the principles adopted by the Group.

In effect, the proposals extended the refundable tax credit system to dividend payments made by all Maltese companies to all their shareholders.

The Commission, agreed with the Maltese Government proposals on a revised tax system and in its decision, the Commission invited Malta to implement these with effect from 1 January 2007. On the 28th November 2006, ECOFIN – the EU Finance Ministers - formally approved the agreement reached between the Maltese Government and the EU Commission.

The Amendments in detail

The Government proposal, which received its first reading in Parliament on the 8th January 2007, was to retain the present imputation system of taxation whereby the tax paid by companies will essentially remain a tax prepaid on behalf of the shareholders, the shareholder level being the level where tax is finally determined. The Government proposed to introduce the notion of an economic rent, as well as enhancing the distinction as to how profits are derived, whereby profits from immovable property will be excluded from the tax refund system agreed to with the EU Commission.

These profits needed to be treated differently since land is not a mobile factor and such profits do not only arise as a result of the inputs of capital and labour, but because land has an inherent value relative to its location. For this purpose such profits are, for tax purposes, being allocated to an immovable property account and shall be treated in the same manner as they had been treated before.

As was the case, company profits were to be allocated to tax accounts in order to determine the tax treatment of such profits upon distribution to shareholders as dividends. Within the above economic conceptual framework company profits are divided between profits on which tax will not be available for refund since they are deemed to be the company's contribution towards the country's provision of public goods, and profits which will be allocated to the relevant Tax Accounts on which a tax refund is available. Upon the payment of a dividend from such profits, shareholders, whether they are resident or non-resident, may claim a refund of part or the whole of the tax paid on the distributed profits. The refund will generally be equal to six sevenths (6/7) of the Malta tax paid on the distributed profits from such accounts.

When the distributing company claims double taxation relief, the existing provisions remained unchanged and a tax refund of two thirds (2/3) of the Malta tax paid on the distributed profits may be claimed. These changes did not affect local residents.

Participating Holding

The tax refund however is increased to 100% when the profits distributed were derived by the distributing company from a participating holding. The definition of a participating holding remained essentially the same. However, as the case in other EU members states certain anti-abuse provisions were introduced aimed at distributions received from companies having mainly passive income and where such company is not resident in the EU nor subject to foreign tax at a rate of at least 15%.

With regards to acquisitions of participating holdings made on or after 1 January 2007, where the non resident company, having mainly passive income, was not resident or incorporated in a tax treaty, EU or EEA jurisdiction or a country which levies a tax on corporate profits at a rate of at least 15%, the following additional conditions must be satisfied, namely that:

- (i) the holding of the Maltese company must not be a portfolio investment, and
- (ii) the non-resident company or its passive income must not have been subject to any foreign tax at a rate of less than 5%.

Currently a shareholding in a non-resident company will qualify as a participating holding of a Maltese company if:

- (a) the Malta company holds equity shares in a non-resident company and it:
 - i. has at least 10% of the equity shares in the non-resident company; or
 - ii. is an equity shareholder in the non-resident company and is entitled to purchase the balance of the equity shares of the non-resident company, or it has the right of first refusal to purchase such shares; or
 - iii. is an equity shareholder in the non-resident company and is entitled to either sit on the Board or appoint a person on the Board of that subsidiary as a director; or
 - iv. is an equity shareholder which invests a minimum in the non-resident company of €1,164,000 (or the equivalent in a foreign currency); or
 - v. holds the shares in the non-resident company for the furtherance of its own business.
- (b) the holding is not held as trading stock for the purpose of a trade. It should be noted that the rules under (a) above will remain applicable for participating holdings existing at 31 December 2006 until the end of 2010.

Refund system

A person in receipt of a dividend paid to him by a Maltese company from profits allocated to its Maltese taxed account or its foreign income account may claim a refund of **six-sevenths** (6/7) of the Advance Company Income Tax (ACIT) paid by the company in respect of those profits distributed to him by way of such dividend, provided that such person is for such purpose registered in such manner as may be prescribed:

Provided that where the dividend is paid out of profits:

- (i) consisting of passive interest and royalties the rate of refund shall be of **five-sevenths** (5/7) of the ACIT paid;
- (ii) allocated to the foreign income account and in respect of which profits the company has claimed double taxation relief (including FRFTC) no claim for refund may be made under this category.

Conclusion

Malta's EU accession and its eventual integration into the Euro-zone, did not dilute Malta's benefits to foreign investors, and the agreements reached helped ensure its future ability to continue to be an attractive and competitive environment for international business and investment and boasts a legislative framework in line with the main EU directives and sufficiently flexible and versatile to relate to different legal systems. Malta's paramount anti-money laundering standards have nurtured the financial services sector to the level it is today.

Malta also has an excellent economic track record with sustained growth, economic and political stability and boasts an inflation rate and long-term interest rate within the EU average. In January 2008 Malta successfully adopted the Euro.

Social Capital is the prime resource in Malta, having availability of approximately 10% of the Maltese population who are graduate and post graduate in the labour force. Malta enjoys an open market economy with free movement of capital and labour with an excellent country sovereign credit rating – 'A' rating with a stable outlook by 'Standard and Poor' – indicating a high to medium quality investment.

The information contained in this fact sheet has been prepared by Busuttill & Micallef – Certified Public Accountants · Tax Consultants, Malta. It is of a general nature and is not intended to address particular circumstances of an individual or entity. The fact sheet is intended to provide the reader with an overview of the tax planning and other opportunities in Malta. This information is also subject to any changes that may occur to the relevant legislation. No one should act upon this information without obtaining appropriate professional advice.