

FACT SHEET 2 – HOLDING COMPANIES AND ‘PARTICIPATING HOLDINGS’

Maltese law does not host a specific *ad hoc* framework regulating holding companies. Nevertheless, tax efficient international holding structures may be created through the interactive application of various tax legislation provisions.

The objects of a company created to act as an international holding structure will need to specify that the company will hold assets, shares or other investments in other companies or institutions. Such international holding companies (IHCs) convey amongst others the following advantages:

- (i) wide double taxation treaty network¹;
- (ii) extensive provisions for double taxation relief other than double taxation treaty relief;
- (iii) no minimum period required for the holding of the investment in the foreign holding;*
- (iv) no requirement that the foreign participation must be an active operating company; and
- (v) no requirement that the foreign participation be subject to taxation overseas.*

* these considerations may however preclude the IHC for availing of participation exemption option.

An IHC is taxed at the normal corporate tax rate, currently set at 35%. Nevertheless, fiscal benefits may arise at both shareholder and company level.

At company level

Relief from Double Taxation

At company level, an IHC investing in securities and other investment instruments overseas, may invoke the mechanisms for double taxation relief available under Maltese law namely:

- (a) The wide network of double taxation agreements;
- (b) Unilateral relief and
- (c) The Flat Rate Foreign Tax Credit.

(a) Double Taxation Agreements

Malta has entered into Double Taxation Agreements with practically **fifty-three** countries including all the EU states,

Switzerland, Libya, India, Australia, China and the United States amongst others.. Further agreements have been initialled or negotiated and are awaiting ratification. These agreements are mainly based on the Organisation for Economic Cooperation and Development (OECD) model. (*vide Fact Sheet 4 – Double Taxation Relief*)

(b) Unilateral Relief

Relief from double taxation is also possible on a *unilateral* basis where tax is suffered overseas on income received from a country which does not have a treaty with Malta, irrespectively of whether that income is remitted to Malta. The overseas tax suffered, limited to the Malta tax charge on the income, is allowed as a credit against tax chargeable in Malta.

(c) Flat Rate Foreign Tax Credit

Another mechanism is the *Flat Rate Foreign Tax Credit*, which is available to a Malta company that generates income or capital gains overseas. It is generally utilised where the company is not in a position to provide evidence of the overseas tax paid to the satisfaction of the Commissioner of Inland Revenue.

The Flat Rate Foreign Tax Credit is calculated at 25% of the overseas income or gain received in Malta. The income plus the deemed tax is subject to Malta corporate tax with relief given for the deemed credit. This is illustrated in Table 1 at the end of this Fact Sheet.

A company which does not have a participating holding may reduce the effective tax rate in Malta to 6.25% or lower, and a company which has a participating holding may reduce the cash flow implications of the tax payment (from 35% to 18.75%) by the application of the Flat Rate Foreign Tax Credit (FRFTC). This credit is available to a Maltese company, which is in receipt of income that stands to be allocated to the foreign income account. A certificate from an auditor confirming that the income in question stands to be allocated to the Foreign Income Account is sufficient to enable the company to claim the FRFTC.

¹ Pls Refer “Double Taxation Relief – Fact Sheet 4”

Refunds of tax to non-resident shareholders

At shareholder level, non-resident shareholders may avail of a refund system in relation to tax paid on dividends received and/or capital gains earned from an IHC.

Any dividends distributed out of the profits of an IHC and which represent income from overseas holdings, participations or business activities that are paid out to non-resident shareholders would enable the said non-resident shareholders to claim a **refund** of two-thirds of the Malta tax paid by the company in respect of the said profits.

Moreover, where the profits so distributed are derived from a '*participating holding*' or from the disposal of such holding, a claim may be made for a **full (100%) refund** of all the Malta tax paid in respect of those profits.

In terms of Malta tax laws, a '*participating holding*' (PH) is deemed to exist where the Malta company satisfies **ANY** of the following criteria:

- (i) a holding of **at least 10%** of the shares in an overseas company; **or**
- (ii) holding gives entitlement to **call for and acquire** the entire balance of the equity in an overseas company; **or**
- (iii) holding gives entitlement to **right of first refusal** in the event of the disposal of balance of the equity in an overseas company; **or**
- (iv) holding gives entitlement to **either sit on or appoint a Board member** of an overseas company; **or**
- (v) holding represents an investment of not less than **€1,165,000** (or equivalent) in an overseas company, and such investment is held for a minimum uninterrupted period of **183 days**; **or**
- (vi) a holding in the furtherance of own business, and **not held as trading stock** for the purpose of a trade.

Furthermore the applicability of the **participation exemption** (i.e. exemption from tax of dividends and capital gains from PH), is available if the holding is in an entity which satisfies **ANY** of the following criteria:

- i. Is resident or incorporated in a **EU** state or territory; **or**
- ii. Is subject to a foreign **tax** of at least **15%**; **or**
- iii. Has not more than **50%** of its income derived from **passive interest or royalties**; **or**
- iv. Satisfies **BOTH** of the following requirements:
 - a) Holding in overseas company are not held as a portfolio investment, **and**
 - b) The overseas company or its passive interest or royalties have been subject to at least 5% tax.

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 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 IHC are submitted to the tax authorities, the tax due (unless participation exemption is availed of) is paid in full and an appropriate application for the refunds is submitted by the non-resident shareholder or his representative.

The operations of the full imputation system adopted in Malta, as well as the refund mechanism, are illustrated in the following examples. Examples are given for a company with a participating holding, with and without the operation of the FRFTC and for a company with a non-participating holding which claims FRFTC – and for comparative purposes of a company involved in international trade.

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.