



THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

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**ADVANCED INTERNATIONAL TAXATION
(JURISDICTION)**

Suggested solutions

Question 1

Part 1

Rental income is taxable in terms of 31D and is subject to 15% final tax. The amount allocated to the FTA is an amount representing profit after tax.

Gozo Ltd holds a PH in the Italian company; dividend is subject to the participation exemption.

Gozo Ltd holds a PH in the Cayman Company; dividend is subject to the participation exemption. The third anti-abuse condition is met because Cayman Company does not derive its income from passive interest and royalties.

Bank interest subject to FWT is allocated to the FTA, net.

Malta's treaty with Kuwait provides for a Stock Permanent Establishment. Profits attributable to a foreign PE are subject to the Participation Exemption.

This figure represents annual market rent of 250 x 130.

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Dividend distributions from the FTA are not subject to any further tax.

Part 2

Persons in the general business of insurance are subject to special computational rules.

Total income is ascertained by adding up:

- Technical provisions at the beginning of the year;
- Equalization reserve at the beginning of the year;
- Gross premiums written;
- Reinsurance recoveries received;
- Income from investments received;
- Profit from the sale of investments (including capital gains);
- Realized differences o exchange;
- Other technical income; and
- Any other profits.

You must then deduct:

- Technical provisions at year end;
- Equalization reserve at year end;
- In addition to 'normal' deductions, claims paid, reinsurance premiums paid, and losses from the disposal of investments.

Question 2

Part 1

The Maltese tax treatment of income derived by DWL

DWL did not establish a PE in Malta and, in terms of its double tax treaty, is not taxable in Malta on its business profits.

Should, for the purposes of the Treaty with the UK, DWL's income be classified as 'interest' income, Malta would, in theory, have the right to charge a withholding tax of 10% but Maltese domestic law provides for an exemption on interest income paid to non-residents and its 'Malta source' interest income would be exempt from tax in Malta.

The Maltese tax treatment of income derived by DWEL

DWEL is taxable on its rental income at 35%.

The 15% regime does not apply to DWEL's rental income because DWEL receives its rent from a company and not an individual. The 15% regime applies to rental income charged to individuals.

Because of 26 (h) ITA DWEL cannot deduct interest paid to DWL.

DWEL's income would be allocated to its IPA and no further tax would be charged on the dividend distribution of such income. No refunds on IPA distributions are due.

The Maltese tax treatment of income derived by DWFL

DWEL is taxable on its finance income at 35%.

26 (h) ITA does not apply and DWFL is entitled to deduct interest paid to DWL.

DWEL's income would be allocated to its MTA. The 6/7 refund and the FIS would apply to upstream dividend distributions of such income.

Part 2

Mr Robin's cession of his rights to assets (1-4) is, in principle, classified as a transfer subject to income tax on capital gains.

The 'close-relatives' exemption does not apply to transfers to cousins, a cession of rights is a donation treated as a deemed sale made at market value.

The cession of units in the CIS is not tax exempt because the CIS is a property company.

The case of (1) is special because Mr Robin could opt-out of property transfers tax and pay income tax on capital gains because his is a non-resident.

The tax exemption on 'royalties' does not apply to the intellectual property being transferred because the cession will not give rise to a 'royalty'.

Cession of tenancy rights to a property situated in Malta is subject to property transfers tax.

Notwithstanding the above, Malta double tax treaty with the UK excludes Malta's right to tax deemed gains from the alienation of assets other than immovable property and shares deriving their value from immovable property situated in Malta (i.e. the shares in the property company).

Question 3

Part 1

BL's tax treatment

BL is incorporated outside Malta and should be treated as a company that is not domiciled in Malta.

BL is managed and controlled in Malta meaning that for Maltese domestic tax purposes BL is Maltese resident.

For tax treaty purposes, BL is a resident of Malta because it is effectively managed and controlled in Malta.

In terms of domestic law BL is taxable in Malta only on:

- Income arising in Malta;
- Foreign source income received in Malta.

BL's royalties from Germany will not be taxed in Malta because they are classified as passive foreign source income that is not received in Malta.

BL's Dutch royalties will be taxed in Malta. BL would pay tax at 35%.

The tax treatment of dividend distributions paid by BL to its shareholder

The profits mentioned in the question will be sitting in BL's UA (German royalties) and MTA (the Dutch royalties provided they are not attributed to a Dutch PE, otherwise they would be allocated to the FIA).

Distributions from the UA are not subject to any further tax.

Distributions from the MTA/FIA would be subject to the 5/7 refund (passive royalties).

The tax treatment of the loan

Loan between related parties that are not entered into at arm's length are undesirable but, in any case, interest paid to non-residents is tax exempt meaning that from a tax avoidance angle the arrangement does not constitute abuse.

Part 2

The concept of fixed establishment is important for the purposes of jurisdiction to tax.

Fixed Establishment determines place of supply. The general rule on place of supply of services provides that the place of supply of services to a taxable person acting as such is the place where that person has established his business but if those services are provided to a fixed establishment of the taxable person located in a place other than the place where he has established his business, the place of supply of those services shall be the place where that fixed establishment is located. In the absence of such place of establishment or fixed establishment, the place of supply of services shall be the place where the taxable person who receives such services has his permanent address or usually resides.

The place of supply of services to a non-taxable person is the place where the supplier has established his business but if those services are provided from a fixed establishment of the supplier located in a place other than the place where he has established his business, the place of supply of those services shall be the place where that fixed establishment is located. In the absence of such place of establishment or fixed establishment, the place of supply of services shall be the place where the supplier has his permanent address or usually resides.

In *Gunter Berkholz v Finanzamt Hamburg-Mitte-Altstadt* (case 168/84) the ECJ held that a fixed establishment is regarded as a fixed establishment if it entails the permanent presence of both the human and technical resources necessary for the provision of services.

Question 4

Part 1

The words and concepts applied in Article 12 ITA bring to mind the 'force of attraction of the permanent establishment' concept used in the articles on interest and royalties in the OECD Model Convention.

Article 12 (1) (c) (i) ITA exempts from tax interest, discount, premium or royalties accruing to or derived by non-residents. The exemption is subject to two important provisos. The exemption applies provided that the non-resident who derives the income:

- is not in the relevant year engaged in trade or business in Malta through a permanent establishment situated therein; and
- where the royalties or the debt claim in respect of which the interest, discount or premium, is paid are NOT effectively connected with such permanent establishment.

The anti-avoidance provision in the proviso to Article 12 (1) (c) ITA refers to the topical concept of beneficial ownership too.

It is not the only provision in the Income Tax Acts which refers to this important concept in tax law. The ITA uses the term and concept many times. The concept of 'beneficial ownership' is used in:

- Articles 5 (9) ITA (degrouching charge and intragroup exemption);
- 5 (13) (b) ITA (value shifting);
- 5 (25) ITA (transfer of shares involving fiduciary relationships); and
- Article 26 (h) ITA (restriction on interest deductibility) and the deemed distribution order framework.

Part 2

Mr Francois is ordinarily resident in Malta because he visits Malta regularly and has established a home in Malta.

Mr Francois will not be considered as being domiciled in Malta because he is not staying in Malta with the intention to live in Malta permanently.

Mr Francois is subject to the remittance basis of taxation (taxable only on income and chargeable gains arising in Malta and foreign source income received in Malta).

Mr Francois is a resident of Malta because he spends more than 183 days in a calendar year in Malta implying that he is entitled to use resident rates.

Mr Francois is a permanent resident implying that he is taxed on his foreign source income at the beneficial rate of 15% subject to a minimum tax requirement.

For the purposes of the tax treaty with France, Mr Francois should be considered to be a resident of Malta.

The acquisition of a Maltese passport should not 'disturb' Mr Francois's tax residence status. It will strengthen his Maltese residence for tax treaty purposes.

Question 5

Part 1

The leading tax case on management and control is *The Calcutta Jute Mills Co Ltd v Nicholson* heard with *The Cesena Sulphur Co Ltd v Nicholson* when the Court rejected the incorporation test establishing management and control as the place where the company's real and substantial business was carried on, the place where the company's centre point was situated. The Court held that once it was the directors who 'called the shots' and that management and occurred where directors took their decisions.

Central management and control is linked to the seat of the director's meeting but it was clear from the outset that a company is managed and controlled in the country in which real business is carried on. Thus it was held, in *Unit Construction Ltd v Bullock*, that if a parent company effectively usurps the functions of the Board of Directors of the subsidiary, then one cannot say that the company is managed and controlled where the board of directors of the subsidiary meets.

The judgment in *Bullock* was discussed in *Wood and Another v Holden* when the Court held that if the board of a directors is a sham the company resides in the country where real authority is exercised. The latter principle was applied in 2004 in the cases *Regina v. Allen* and *Regina v Dimsey*, a criminal case.

Another important decision on the issue of 'real control' was delivered in 2006 in the case *Wood and another v Holden (HMIT)* when the court differentiated between management and control and 'influence'.

The concept of management and control is used in the Income Tax Act prevalently for the purposes of determining residence of a body of persons.

In a VAT context the concept of management or control is important for the purposes of establishing the personal liability of representatives.

Part 2

Sale of house in Vittoriosa through an estate agent

ITA

Taxable at 12% of market value but transferor can opt-out of property transfers tax and pay income tax on capital gains on profit determined in term of the CGR.

DDTA

Transfer will attract duty at the rate of 5% (payable by buyer).

VAT

Transaction is out of scope of duty.

Donation of chalet in Switzerland to a friend

ITA

Transferor is ordinarily resident and domiciled in Malta. Transfer of chalet is taxable in Malta. Transfer is not subject to property transfers tax but capital gains is payable on a deemed profit.

DDTA

No duty is chargeable in Malta unless use of the document executed outside Malta is made in Malta in terms of the DDTA (produced in Malta for its enforcement).

VAT

Outside the scope of VAT.

Sale of coin collection at auction in Malta

ITA

Not subject to tax because transfer of capital asset outside the scope of income tax on capital gains.

DDTA

Not subject to duty.

VAT

Transfer not subject to VAT but VAT payable on auctioneer's fees.

Sale of securities in his Dutch registered family company (a controlling interest) to his nephew

ITA

Subject to income tax on capital gains in Malta. Transfer not tax exempt because relationship with nephew is 'too distant').

DDTA

Given that transferor is a resident of Malta such transfer is subject to duty in Malta. Transferor would be tax exempt if done through an ISA.

VAT

Out of scope of VAT.

Question 6

Part 1

Double Tax Treaty Malta/Netherlands

Given that both companies are Dutch residents they are taxable in the Netherlands but both companies will be establishing PEs in Malta.

Services BV will establish a branch and the nature of Explorations BV's activities in Malta creates a PE too (place of extraction of natural resources/project continuing for more than 12 months).

Both Dutch companies will be taxed in Malta on business profits attributable to their Maltese permanent establishments.

ITA

The Dutch companies' activities fall plainly and squarely within the special regime contemplated for profits from the production of petroleum.

For the purposes of the provisions on profits from the production of petroleum, Explorations BV qualifies to be treated as a 'Contractor' implying that its chargeable income is arrived at by deducting recoverable costs in terms of the PSA from the total of the value of the cost recovery petroleum and of the share of the petroleum.

Unabsorbed recoverable costs are carried forward.

Profits are allocated to the FTA. Surrendering of losses is not allowed.

For the purposes of the provisions on profits from the production of petroleum, Services BV qualifies to be treated as a 'Subcontractor'. The Contractor should withhold tax on payments made to the subcontractor. Tax must be withheld at 10%. Tax is to be paid within 30 days. At the option of the subcontractor the 10% tax is a final withholding tax.

VAT

Drilling related services qualify to be treated as services connected with immovable property, hence deemed to take place in the country where the immovable property is situated. In this case given that such immovable property is situated on Malta's continental shelf such a supply is deemed to take place in Malta and subject to Maltese VAT. Given that the supplier is established in Malta for VAT persons, the person liable to charge/pay the VAT is the supplier/service provider.

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The VAT consequences of sale of unrefined oil depend on the manner in which such products will be sold:

- In case the oil will be dispatched to a country outside of the EU by or on behalf of the seller such a supply would qualify as an exempt export (exempt with credit from Maltese VAT).
- In case the oil will be dispatched to a customer established in another EU Member State such a supply would qualify as an exempt Intra Community Supply (exempt with credit from Maltese VAT on the basis the customer is EU VAT Registered and there is proof of transport).
- In case it will be sold domestically it will be subject to Maltese VAT (18%). Such Maltese VAT can obviously be claimed by the customer provided it is related to a subsequent taxable/exempt with credit supply that will be performed by the customer.

DDT

No duty implications.

Part 2

The VAT Act and the Income Tax Act prescribe that the onus of proof is on the taxpayer but, in Malta, tax assessments always combine assessments to raw tax with assessments to additional tax.

In John Geranzi Limited v. KTI, the Constitutional Court classified additional tax as a criminal charge.

In the wake of the John Geranzi judgment the Administrative Review Tribunal (rik.76/12VG) has consistently applied an inversion of the onus of proof.

Question 7

Part 1

Determine whether Mr Schiffer is entitled to benefit from the Highly Qualified Persons Rules, the Global Resident Programme Rules and the High Net Worth Individual Rules. Give reasons for your decisions.

Mr Schiffer is not entitled to benefit from the Highly Qualified Persons Rules because he will not hold an eligible office.

Mr Schiffer is not entitled to benefit from the Global Residence Programme Rules because he will not be taking up residence in Malta.

Mr Schiffer is not entitled to benefit from the High Net Worth Individual Rules because he is not a citizen of an EU/EEA Member State.

Based on the projected income and costs discussed above determine Mr Schiffer's chargeable income.

Mr Schiffer's taxable income will consist of:

- The dividend of €5,000,000. No further tax will be charged on the dividend payment.
- The salary of €375,000 that will be paid via the FSS system. Tax is payable at non-resident rates.
- The performance bonus of €150,000. This too is subject to FSS and taxable at non-resident rates.
- The private use of the Company's Private Jet (the annual value of the benefit will be of €200,000). This is a taxable fringe benefit. The conditions of the exemption contained in L.N. 292 Fringe Benefits (Amendment) Rules, 2010 are not met because the employer is not an aviation company.
- The entertainment allowance of €2,500. Subject to FSS and taxable at non-resident rates.
- The cost of tax equalisation.

The Following items will be excluded from chargeable income:

- Reimbursement of business travel costs of €15,000 because the payment will be a pure reimbursement.
- Private use of the company's chauffeur driven car (the annual value of the benefit will be of €1,000) because the car will be used for the company's benefit.
- Health insurance that will cost the company €2,000 per annum is an exempt fringe benefit.

In principle, CISs established as companies should be considered tax treaty subjects but, at an international level, the special tax treatment that our law accords to CISs seems to have complicated matters. CISs established as Maltese companies are fiscally opaque entities because under domestic law companies incorporated in Malta after 1994 are considered to be Maltese tax residents that are eligible to tax treaty benefits. Unlike partnerships which are fiscally transparent CISs are opaque and pay tax on some of their income. From a Maltese point of view CISs are eligible to treaty benefits. Recent changes to the OECD Model Convention suggest that at international level CISs should be granted tax treaty recognition too because treaty benefits apply to 'any person who, under the laws of that State, is liable to tax...' Maltese CISs are liable to tax on income from immovable property situated in Malta and investment income to which article 41A(a) ITA refers.

A CIV which is an opaque company should qualify to be treated as a person. The crucial question is whether a CIV qualifies to be treated as a resident of a Contracting State.

Part 2

A 10 year old office building situated in Malta in respect of which Mr Bonello had availed himself of initial allowance

Not subject to DDTA and VAT but, for income tax purposes, transfer could give rise to a balancing charge.

A 3 year old commercial motor vehicle in respect of which Mr Bonello had availed himself of wear and tear allowance and credit for input VAT

Not subject to DDTA VAT but, for income tax purposes, transfer could give rise to a balancing charge. For VAT purposes an adjustment would have to be done in terms of Value Added Tax (Adjustments Relating to input tax on capital goods) regulations.

Cash in hand and at bank

Not subject to tax.

Business goodwill

In principle, subject to income tax on capital gains but a tax exemption applies (sole settlor is sole beneficiary).