

HOLDING COMPANIES

Malta, an EU Member State since May 2004, has developed into a leading and reputable financial centre and offers an attractive and competitive environment for international business and investment. Its culture, multilingual population, geographical position, qualified professionals, opportunities for efficient tax structuring, relatively low costs for management and administration, and its state of the art telecommunications, gives the added advantage over other jurisdictions.

The Participation Exemption

Maltese holding companies are suited for a number of activities, in particular for the holding of shares in companies which in turn invest in EU Member States and other countries.

An important tax exemption, referred to as the 'participation exemption' provides for the exemption from corporate income tax of dividends and capital gains in relation to a qualifying investment in an affiliated company or limited partnership, known as a 'participating holding'.

The participation exemption is subject to some anti-abuse rules, but is generally available for dividends received from a participating holding that is either:

- (i) resident or incorporated in an EU country; or
- (ii) is subject to foreign tax of at least 15%; or

(iii) does not derive more than 50% of its income from passive interest and royalties.

However if none of the above are satisfied, a participation exemption may be applicable on that income, where the income from the participating holding has been subject to foreign tax of at least 5% and the investment in the non-resident entity does not constitute a 'portfolio investment' in terms of Maltese law.

Capital gains derived from a participating holding are not subject to the anti-abuse rules described above. A Maltese company may therefore claim the participation exemption on capital gains derived from the alienation of shares held in a participating holding without having regard to the above.

Many countries subject payments of dividends to withholding tax and it is not unusual that their domestic legislation also provides for taxation of a capital gain derived by a foreign shareholder from the disposal of domestic shares. Withholding tax is often reduced if the shareholder is a Maltese resident under the relevant double tax treaty which the country of residence of the company has with Malta. Moreover, the double taxation treaties often prohibit the foreign country to levy tax on the capital gain.

Malta does not withhold tax on outbound dividend distributions made by a Maltese company in most circumstances. It may be clear from the above that the participation exemption in combination with the application of tax treaties and/or the parent subsidiary directive makes Malta a very attractive location for holding companies.

Participation Exemption and Refunds of Tax

A Maltese company in receipt of dividends or capital gains from a participating holding may at its option, either apply the participation exemption whereby the dividends or capital gains received by the Maltese company are exempt from tax in Malta or include the income as part of its chargeable income for the year and pay tax at the rate of 35%. In the latter case, upon a dividend distribution, its shareholders may make an application for a full refund of the tax suffered on the company's profits out of which the dividend has been distributed.

Advance Revenue Rulings

The International Tax Unit within the Inland Revenue Department is responsible for providing advance revenue rulings. Revenue Rulings give the comfort of legal certainty to international investors. A Revenue Ruling may be requested to confirm the tax treatment or tax position such as:

- The position regarding general anti-avoidance provisions;
 - Whether an equity holding is in the course or furtherance of a company's business for the purposes of determining whether that equity holding qualifies as a participating holding;
 - The tax treatment of any particular financial instrument;
 - The tax treatment of any transaction which involves international business.
- Revenue Rulings may be obtained for a period of 5 years and are renewable every five years thereafter. The Revenue Rulings survive a change in legislation giving a grace period of 2 years from the date of entry into force of any such new law.

Other important considerations:

- No withholding taxes on dividend, interest or royalty payments
- No thin capitalisation
- Malta has no specific transfer pricing regulations
- No stamp duties on disposals/acquisitions of securities in companies owned by non-residents
- Under re-domiciliation provisions it is possible to migrate companies into and out of Malta
- No exchange control regulations and business may be conducted freely in any currency
- Malta's financial services legislation and tax laws are compliant with EU Directives
- Malta has strong and effective Anti-Money Laundering Laws and Regulations

Dividend, Interest and Royalty payments from Malta

Unlike many other countries, Malta does not levy withholding tax on dividend, interest and royalty payments or similar payments by a Maltese company. As a result, in many tax treaties Malta has negotiated low withholding tax rates with third countries, adding to the attractiveness of the Malta tax treaties.

EU parent-Subsidiary Directive, Interest-Royalty Directive and Mergers Directive

Malta has implemented all of these EU Directives into its domestic legislation. These Directives have great significance for international groups. The Parent-Subsidiary Directive generally eliminates withholding taxes on profits distributed by a subsidiary to its parent and generally eliminates double taxation of those profits in different EU Member States. The Interest-Royalty Directive also seeks to eliminate the double taxation of interest and royalty payments between companies which are resident in different EU Member States. The Mergers Directive ensures that pan-European group re-organisations (mergers, de-mergers, share for share exchanges etc) can be structured with minimal tax incidence.

Other Investments

Maltese companies deriving income from investments that do not qualify as a participating holding may still benefit from favourable tax treatment. Although the chargeable income so derived would be subject to tax at the standard rate of 35%, the company may be eligible for double taxation relief in terms of Maltese fiscal legislation. Upon a dividend distribution, the shareholders would be eligible to a refund of 2/3rds or 6/7ths of the Malta tax depending on the form of double taxation relief claimed in the income.

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