



MALTA TAX LAW UPDATE

Update 18

EDITOR'S NOTE

The lower courts are reacting to the Constitutional Court's judgment in *Angelo v. PM et.* The lower court's conclusions are entirely predictable; lower courts are following the same line of reasoning of the Constitutional Court. A person who is punished with an administrative penalty for a tax offence should not be subject to criminal prosecution for the same offence. For the purposes of the Convention, Maltese tax penalties are criminal charges.

The Administrative Review Tribunal is working at a very steady pace delivering over ten judgments this quarter. The ART's judgment 85/11VG may become a leading case on the interpretation of Article 51 ITA. Coincidentally, Article 51 ITA has been changed in the light of changes imposed by the Parent Subsidiary Directive.

On the legislative front, a bill to implement the budget measures for financial year 2016 has just been published. Important changes were contained in over-arching laws dealing with generic financial matters; they may have passed unnoticed.

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1. LEGISLATIVE CHANGES

1.1 Acts of Parliament

ACT No. XXI of 2015

This Act changes rules relating to the tax treatment of immovable property.

Capital Gains – Own Residence Exemption

The first change refers to the 'own residence' exemption. Act XXI amends Paragraph 5 (c) of article 5 ITA.

The words:

"including land which the individual has for his or her own occupation and enjoyment with that residence as its garden or grounds up to an area (exclusive of the site of the dwelling house) not exceeding two times the area of the house and transferred through the same deed with the principal residence";

will be substituted by the words:

*"including land, transferred through the same deed with the principal residence, which the owner has for his own occupation and enjoyment with that residence as its garden or grounds consisting of an area which, **regard being had to the size and character of the dwelling house, is required for the reasonable enjoyment of it as a residence**";*

The unpopular size restriction introduced previously has been rendered more flexible. The 'two times' test has been replaced with a much more sensible subjective test. The same approach has been adopted in the amendment which refers to additions required for the reasonable enjoyment of a property as a residence.

The phrase:

"Any part of the house which is used exclusively for commercial purposes for any time within two

years of the transfer shall not be considered as "own residence" and this part shall be apportioned on the basis of the area occupied for this purpose as a proportion of the whole area of the relative dwelling house:"

is being substituted with the phrase:

*"Any part of the house, **garden or grounds** which is used exclusively for commercial purposes for any time within two years of the transfer, or **which is not required for the reasonable enjoyment of it as a residence** shall not be considered as "own residence" and this part shall be apportioned on the basis of the area occupied for this purpose as a proportion of the whole area of the relative dwelling house, garden or grounds."; and*

The proviso to the paragraph has been deleted.

Rental Income

Article 31D ITA providing for a special rate of tax on rental income has been amended to cover both properties leased as garages and residence as well as properties **used** as garages and residences.

In definition of the word 'tenement' in paragraph (a) of sub-article (8) the words:

"or a garage, excluding a tenement which, for the purpose of the said letting, is required to be licensed by virtue of the Malta Travel and Tourism Services Act, or any Act which may be substituted therefor; and"

shall be substituted by the words;

"or a garage; and"

implying that MTTA licensed premises will no longer be excluded from the purview of this beneficial tax regime.

ACT No XXXIII of 2015

ACT No XXXIII of 2015 introduces two important provisions dealing with international tax avoidance. The first amendment consists in the addition of a new paragraph within the general anti-abuse in Article 51 ITA. The new paragraph reflects the most recent changes to the Parent Subsidiary Directive. The second change relates to the ITMA; it empowers the Minister to enact rules relating to exchange of information.

The following paragraph has been added to Article 51 ITA:

"(b) The benefits of EU Council Directive 2011/96/ EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (as amended) shall not be granted to any arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of the said EU Council Directive 2011/ 96/EU, are not genuine having regard to all relevant facts and circumstances.

For the purpose of this paragraph –

- (i) an arrangement may comprise more than one step or part;
- (ii) without prejudice to any remaining genuine steps or parts of any particular arrangement, an arrangement or a series of arrangements shall be regarded as not genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality; and
- (iii) where a single step or part in an arrangement or a series of arrangements is, by itself and without regard to the remainder of the arrangement or series of arrangements, not genuine, the provisions of this paragraph shall apply only to such step or part that is not genuine, without prejudice to the remainder of the arrangement or series of arrangements that are genuine.

The provisions of this paragraph –

- (i) implement EU Council Directive 2015/121 of 27 January 2015 amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States; and
- (ii) shall not preclude the application of any other provision in the Income Tax Acts or any rules issued thereunder concerning the prevention of tax evasion, tax fraud or abuse."

The following addition refers to Article 10A ITMA:

"(5) The Minister may make rules for the collection and maintenance of information, even where arrangements between Malta and other relevant jurisdictions, or their tax authorities, for the purposes of exchange of information for tax purposes, are not in force:

Provided that the person that is obliged to collect and maintain such information according to such rules shall not be obliged to provide such information to the Commissioner before an arrangement between Malta and the other relevant jurisdiction, or its tax authorities, for the purposes of exchange of information for tax purposes, enters into force."

1.2 Legal Notices

L.N. 362 of 2015 INCOME TAX ACT(Cap. 123) Double Taxation Relief (Taxes on Income) The Republic of Mauritius) Order, 2015(L.N. 409 of 2014)

This LN brings the Treaty into force.

1.3 Bills

1.3.1 Bill 120 of 2015 - Budget Measures Implementation Act, 2016

The Bill proposes the following important changes:

- Addition of a new proviso to the definition of 'company' (introduction of special rule relating to securitisation vehicles);

- Computational rules relating to Property Transfers Tax;

- New tax rate for property acquired causa mortis;

- A Tax deduction limitation rule;

- A new definition of the term 'tenement' for the purposes of Article 31D;

- New tax rates;

- Sunset clause for returned migrants;

- Beneficial tax rate applicable to emoluments for sports activities.

1.3.2 Addition of a new proviso to the definition of 'company' (introduction of special rule relating to securitisation vehicles)

Every cell of a securitisation cell company and that part of a securitisation cell company in which non-cellular assets are held will be deemed to be a separate company. Immediately after the first proviso of the definition "company" will be added the following new proviso:

"Provided further that in the case of a securitisation cell company as defined in the Securitisation Cell Company Regulations (in this proviso referred to as 'the Securitisation Regulations'), as may be amended from time to time, or in any other law or regulations replacing the Securitisation Regulations, for all intents and purposes of the Income Tax Acts, every cell of a securitisation cell company and that part of a securitisation cell company in which non-cellular assets are held, shall each be deemed to be a separate company and any words and expressions in the Income Tax Acts which are relevant to a company shall be construed accordingly. The interpretation of such words and expressions insofar as applicable to a securitisation cell company shall be made on the basis of the relevant provisions of the Securitisation Regulations."

1.3.3 Computational rules relating to Property Transfers Tax

Most of the measures relate to the re-transfer of donated property and the determination of cost of acquisition in such cases.

1.3.4 New tax rate for property acquired causa mortis

Tax will be of 7% of transfer value on the re-transfer of:

Property acquired causa mortis before the 25th November, 1992; or

Property acquired causa mortis on or after the 25th November, 1992 and the property is transferred by means of a judicial sale by auction,

1.3.5 A Tax deduction limitation rule

A new tax deduction limitation rule will be added in paragraph (5) of article 14. Expenses that refer to supplies subject to VAT are deductible only if the taxpayer retains adequate VAT invoices and mandatory documentation. The new rule will read as follows:

"(5) Notwithstanding the other provisions of this article, when a person incurs expenditure for a supply of goods or services in respect of which the supplier is required to issue a tax invoice or other document in terms of article 50 or 51 of the Value Added Tax Act, no deduction shall be allowed under this article in respect of that expenditure unless that person is in possession of a tax invoice or other document issued in accordance with the said article 50 or 51 and produces such tax invoice or other document if required to do so by the Commissioner."

1.3.6 A new definition of the term 'tenement' for the purposes of Article 31D

The definition of tenement (property subject to the beneficial rate of tax) will be extended to include commercial tenements. The rental of commercial property to or from related parties has been excluded from the purview of the regime. The new definition will read as follows:

"(i) a tenement, not being a commercial tenement as defined in article 1525 of the Civil Code, which consists of either a dwelling house or part thereof which is to be occupied or is occupied as a home or residence by the occupier or a garage; or

(ii) a "commercial tenement" or a "club", both terms having the meaning assigned to them respectively in article 1525 of the Civil Code, when the tenement is not rented to or from a related body of persons, and for the purpose of this sub-paragraph –

(A) a body or persons is related to an individual if it is owned or controlled, directly or indirectly, as to more than twenty-five percent by that individual; and

(B) two bodies of persons are related if they are owned or controlled, directly or indirectly, as to more than twenty-five percent by the same persons."

1.3.7 New tax rates

These have been discussed in Update 17. The computational mechanism known colloquially as the short form has been incorporated in the law.

1.3.8 Sunset clause for returned migrants

A five year limitation rule has been introduced.

1.3.9 Beneficial tax rate applicable to emoluments for sports activities

Individuals who derive income from a full-time or part-time sports activity either as a registered player or athlete or as a licensed coach shall, unless they opt to have the said income charged to tax at normal rates be charged to tax on all such income at the rate of seven point five cents (0.075) on every euro.

2 Judicial Decisions

2.1 Judgments of the ART

Rik. Numru. 85/11VG

This judgment is an important judgment relating to the interpretation of Article 51 ITA dealing with tax avoidance. The case involved a company owned by a sole shareholder who restructured his financial affairs. Taxpayer divided his property owning company in two companies both of which were owned solely by him. By virtue of the division, title to an immovable property was assigned to one of the two companies. Subsequently, the property was transferred to a newly constituted company. The shareholder of the new company was the same shareholder of the other companies but another two individuals sat on the board of the new company. Given that the conditions of the intra-group exemption were still met, the tax exemption relating to the transfer was applied for and obtained. At a later stage, new shares were allotted in the company that owned the property. The new shares were allotted to companies owned by the same persons who were serving as directors. When the Commissioner for Inland Revenue got wind of the whole series of transactions he decided to retract the intra-group exemption treating the intra-group transfer as taxable in full. According to the Revenue, the whole series of transactions amounted to a tax avoidance scheme. An assessment was raised, an objection was filed and the case went to the BSC which later transferred the case to the ART. Four years passed and, in the meantime, interest and penalties continued to run at punitive rates.

In front of the ART, the Revenue argued that the series of transactions was a tax avoidance scheme because the sole or main purpose of the chain of events was the transfer of a property tax free. Taxpayer argued that the case involved a genuine restructuring of holdings adding that the unexpected retraction of the intra-group exemption amounted to a violation of his right to legitimate expectations.

The ART agreed with the conclusions reached by the Revenue. The ART held that in ascertaining the legal nature of a transaction (i.e. whether it amounted to a tax avoidance scheme) a Court should not pick out and stop at a step but to consider the effect of the whole combination of transactions. It referred to Commonwealth case law on the definition of tax avoidance. The Tribunal held that the pre-ordained series of transactions lacked a commercial purpose. According to the Tribunal, from the series of transactions, it emerged that the composite transaction's main purpose was tax avoidance (Coincidentally, the Tribunal's reasoning converges with concepts contained in the recent PSD inspired changes). With respect to the interest which had been running since the inception of the case, the Tribunal agreed to abate a part of the interest.

Rikors Nru. 7/11VG Anthony u Michelina konjugi Magro et Vs Kummissarju tat-Taxxi

This case was a duty case. Taxpayer lost the case because, contrary to his claim, the Government's Architect had taken the devaluation of property into account.

Rikors Nru. 10/11VG Deborah Cefai et Vs Kummissarju tat-Taxxi

The ART held for the Revenue imposing additional tax because the ART concluded that taxpayer's version was not credible and the value of the property had been seriously under-declared.

Rikors Nru. 79/09VG Lawrence Pisani et Vs Kummissarju tat-Taxxi

The ART dismissed an appeal involving an assessment to duty on the basis of lack of evidence. It held that taxpayer's version was credible but taxpayer had failed to provide documentary evidence confirming the quantum of deductible expenditure.

Rikors Nru. 37/09VG Salvi Holdings Limited Vs Kummissarju tat-Taxxi

The ART cancelled an assessment because the Tribunal's Architect concluded that the value declared in the deed reflected the fair market value of the property. According to the Tribunal, the Government Architect's valuation of the property was too high and was based on a number of incorrect premises.

Rikors Nru. 122/11VG Cornelius M. Scifo Diamantino Vs Kummissarju tat-Taxxi

The ART cancelled an assessment to duty because it held that in his valuation report, the Government's Architect had ignored material facts.

Rikors Nru. 226/11VG Spinola Development Company Limited Vs Kummissarju tat-Taxxi

The ART cancelled an assessment in part. The ART concluded that the Government's Architect had not taken material circumstances into account.

Rikors Nru. 227/11VG Spinola Development Company Limited Vs Kummissarju tat-Taxxi

The conclusions of this judgment are identical to those contained in Case 226.

Rikors Nru.230/11 VG Thea Pisani u Nicole Pisani Vs Kummissarju tat-Taxxi

The ART cancelled an assessment on the basis that the assessment was based on the inaccurate premise that a particular contract was still in force when it transpired that the contract had been rescinded. Given that the parties had not informed the Commissioner of the rescission the contract, the Tribunal awarded costs against the taxpayer.

2.2 Judgments of the Court of Appeal

Appell Numru: 73/2009 EXCLUSIVE PROPERTY BUREAU LIMITED (C20719) VS DIRETTUR GENERALI (TAXXI INTERNI)

The Court of Appeal confirmed a judgment of the ART upholding an appeal from duty because the Court of Appeal held that, contrary to the Revenue's submissions, the ART had correctly applied the law. The Court held that the ART's decision to deduct from the transfer value the cost of improvements borne by the buyer post-transfer was correct.

Appell Numru: 194/2011 DENNIS FARRUGIA (ID 604981(M)) VS DIRETTUR GENERALI (TAXXI INTERNI)

The Court of Appeal confirmed a judgment of the ART which held that taxpayer had failed to prove his case.

Appell numru: 77/2010/1 Hal Mann Properties Limited Vs Kummissarju tat-Taxxi Interni

This case consisted in a challenge to an executive title with respect to duty which was final and conclusive. The Court held that taxpayer had failed to utilise the ordinary contestation procedure and his action to rescind the executive title was null and void.

Avviz 4/2012AE Inserv Ltd Vs Il-Kummissarju tat-Taxxa Fuq il-Valur Mizjud

This case involved an assessment to indirect tax which revolved around the correct classification of goods under a particular HS Code. The VAT Appeals Board had engaged the expertise of an employee of the Department of Customs in connection with the use of a particular HS Code for calculators and coin counting machines. In taxpayer's opinion, the VAT Appeals Board's involvement of an employee of the Department of Customs and the MSA had prejudiced the Board's impartiality and the taxpayer based his appeal from the Board's decision on the basis of the right to a fair hearing. The Court disagreed because in its view the consultation with the employee of the Customs Department did not amount to an assignment of its decision making power. In addition, consultation with the MSA was almost necessary. In addition, the Court held that taxpayer had failed to prove that the VAT Department had used the correct HS Code.

Appell numru: 226/2012AE xxxx Vs Kummissarju tat-Taxxa Fuq il-Valur Mizjud

The Court of Appeal delivered yet another judgment confirming that taxpayers should be granted full access to the contents of their own tax files. This judgment was delivered by the new judge of the Court of Appeal. The new judge expressed reservations with respect to the description of a tax file as being taxpayer's personal property. Nonetheless, the Court of appeal confirmed the decision of the ART ordering the Vat Department to grant taxpayers access to their personal files.

2.3 Judgments of the First Hall Civil Court

Rikors Nru. 14/11 JZM Robert Ciantar (316583M) kontra L-Onorevoli Prim Ministru et

This judgment is based on the Angelo Zahra case discussed previously. The imposition of criminal penalties over and above administrative penalties was found to breach the non bis in idem principle. Article 83 (3) of the VAT Act was found to be incompatible with the European Convention on Human Rights. Interestingly, the Court seems to agree that even cumulative administrative penalties infringe the non bis in idem principle.

Citazzjoni Nru: 953/2012 AF Euro Hygene International Ltd (C25887) u Dennis Xuereb vs Il-Kummissarju tat-Taxxa fuq il-Valur Mizjud illum Direttur Generali tat-Taxxa fuq il-Valur Mizjud

This case involved another challenge to an executive title. The case was instituted by a simple application and the Court dismissed the case because it held that the procedure that was followed was invalid.

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