



THE TAX ADVISER

**AN IN-HOUSE NEWSLETTER FOR MEMBERS OF THE MALTA
INSTITUTE OF TAXATION: ISSUE NO 4: OCTOBER 2015**

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FROM THE PRESIDENT'S DESK

Dear Members,



So the holiday period is now over (well, at least for those who managed to take holidays!), and we're all back at work. Our hard working staff only managed to take off the odd half day, and I must thank them on behalf of our members for the efforts put in. Our latest intern from northern Europe gave us the usual useful contribution during summer, but she is now back home in colder Estonia.

A lot of work has devolved upon us in connection with the furtherance of one of the major functions of the Institute, namely education. During this period we also took the unusual step of holding seminars in summer. These were open to the public, and proved to be extremely successful, particularly the one held on 3rd August during which Mr. Marvin Gaerty, Commissioner for Revenue, and Dr Neville Gatt and Dr Steven Gingell, both from PriceWaterhouseCooper, gave us a detailed run down on what one hopes will be the final position for some years to come regarding the taxation of transfers of immovable property. The speakers gave us an extremely important and authoritative rundown on what has become a rather tangled corner of our tax code. Their efforts are much appreciated and we are taking the unusual step of loading on our web-site (members' section only) the slides used during the discussion.

We are glad to confirm that the National Commission for Further and Higher Education has now officially granted recognition to the Institute as a teaching organisation and that our Course leading to the Professional Certificate in Taxation (formerly the extremely popular Diploma Course) has been graded by the Commission at level 6MQF which is essentially a degree level. The first of the new

Courses has already started, after being heavily over-subscribed. Our other principal tax course, the Foundation Course in Taxation, is being restructured and the new version should be launched next year.

Members will be pleased to learn that we have finally reached agreement with the University on the introduction of a Masters Course in Taxation. This will be part of the curriculum offered by the top educational establishment in Malta, and we hope to attract foreign students as well. We feel that Malta is ideally situated to offer such a course which has long been a holy grail assiduously followed by the Institute, and we now hope to have the course in place by the 2016/2017 academic year.

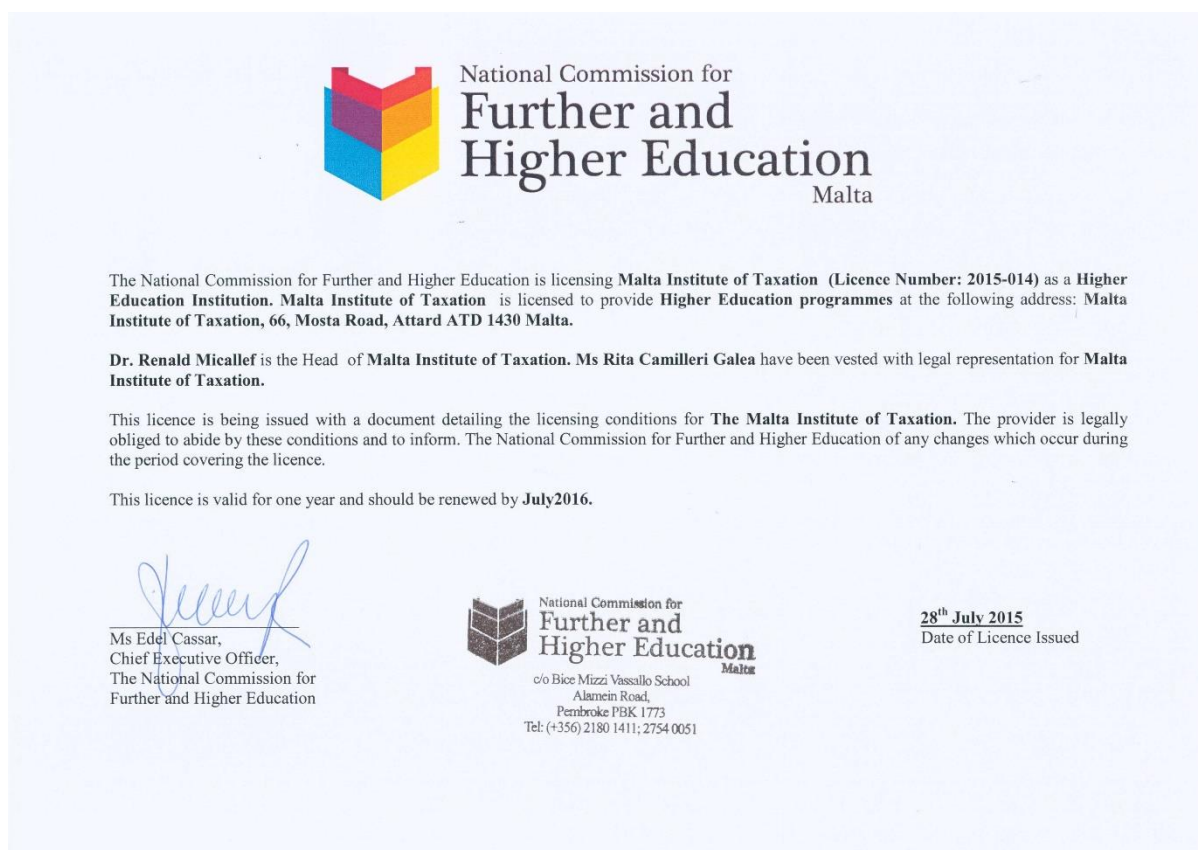
Sincere thanks must go to all those who have worked so hard to enable us to achieve these results.

FAREWELL VISIT BY OUR LATEST INTERN



During the past few summers we have been hosting interns under the Erasmus programme of the E.U. The above photo shows our latest guest from northern Europe, Ms Liisa Hansar from Estonia, who spent ten weeks with us helping on various Institute projects. Liisa is a student of tax law (mostly re customs duties) and had already enjoyed intern visits to other countries. The photo records her farewell visit before returning home to continue her studies.

THE INSTITUTE LICENSED AS A HIGHER EDUCATIONAL INSTITUTION BY THE NATIONAL COMMISSION FOR FURTHER AND HIGH EDUCATION



RACHEL GALEA ON

BASE EROSION AND PROFIT SHIFTING (BEPS)¹

Globalisation, digitalisation, fluid movement of capital and rapidly changing business models are factors that allow companies to exploit gaps in international tax rules so as to avoid taxation through a reduction of their taxable base by the shifting of profits to low/no tax jurisdictions. Media focus on tax strategies by multinational enterprises to minimize their tax burden has repeatedly brought this activity to public and political notice. Action groups and media campaigns have triggered public interest in the tax strategies employed by large companies (as well as high profile individuals) at

¹ A report on the proceedings a seminar held on 7 July 2015. Parallel activities by individual taxpayers were not dealt with in the seminar.

a time when the economy is creating pressure on such taxpayers to demonstrate their contribution to society.

Early in 2014, the E.U. Commission directed jurisdictions to give information on certain advance clearance practices and certain tax regimes. Some states co-operated whilst others refused, preferring to have the issue solved at a state level. In June 2014, the E.U. opened several in-depth investigations concerning transfer pricing arrangements in various jurisdictions. In March 2015, the E.U. Commission presented a Tax Transparency Package which included a proposal for the automatic exchange of information.

While recent developments have tackled the problem of 'harmful' tax regimes, and the revision of E.U. tax directives, the G-20 indicated that they endorse the development of a multilateral instrument to facilitate the implementation of tax treaty-related B.E.P.S. measures. Corporations, on their part, are seeking a responsible approach to the management of taxes – one which is able to deliver sustainable outcomes that are right for the business and which would still feel right should the media spotlight settle upon them. The information that businesses share about their taxes is being examined by a widening range of interested parties. Some companies have responded by explaining their position more fully in their financial reporting or other published details. At the same time, regulators are requiring some companies to at least furnish more tax information.

To be able and ready to set out its tax situation, an organisation has to take into account its stakeholders' attitudes and requirements so that it can explain its position better by setting out the context and background management policies. Companies have to evaluate their options pro-actively and systematically in order to deliver a sustainable tax strategy, remain agile in the face of on-going change, and manage key stakeholders' expectations in real time.

In 2014, Deloitte conducted its first OECD Base Erosion and Profit Shifting survey to gauge the views of multinational companies regarding the increased media, political and action groups' interest in responsible tax and B.E.P.S., as well as the expected resulting impact on their organisations. In early 2015, a follow-up survey was conducted to see how clients' views on the tax landscape had evolved. Over 90% of respondents are anticipating that their tax compliance burden will increase substantially as a result of additional reporting arising from the B.E.P.S. recommendations concerning country-by-country and transfer pricing reporting. Some 55% of respondents are anticipating that significant unilateral changes will take place to protect national tax bases that remain uncoordinated with other countries, and over 75% are anticipating that double taxation will occur as a result of B.E.P.S. action.

Respondents agreed that one of the main hurdles to the project will be achieving consistency between several countries, and regulating how burdensome the reporting

factor will become. There exists a belief that countries standing to lose revenue from B.E.P.S. initiatives are likely to opt out of the proposals. There is also a feeling that some key countries would simply not sign up to a multi lateral treaty. Over 90% of respondents to the survey agree that tax structures are under greater scrutiny by tax administrations than a year ago. Over 50% of respondents are anticipating significant legislative and treaty changes in their countries as a result of the B.E.P.S. initiatives, which is a significant increase from last year, while 74 % agree that reputational risks are now of much greater concern when preparing cross-border tax planning. Some 58% agree that the B.E.P.S. project will have greater impact on their organization than what they originally thought based on the OECD's work. This follows from the consequential increased momentum to the B.E.P.S project and countries' commitment to implementing its measures.

The main concern about "responsible tax" and the B.E.P.S. initiative is that it is a one-sided agenda: companies are automatically presumed to be engaged in tax avoidance. Tax planning will become increasingly difficult, meaning tax departments will end up working on higher levels of compliance instead of adding value. Companies are also wary that a broad implementation of B.E.P.S. may fail, and that each country could proceed to implement parts of the suggested changes on its own, thus making the tax situation even more complicated. Actually, the main hurdle to achieving cooperation between countries in implementing the OECD's recommendations is that no country wants to lose out. Agreement and consensus on policies will be difficult, thereby increasing the risk of unilateral action.

Companies, on their part, have been unpleasantly surprised with the pace and breadth of the B.E.P.S. movement. This is evident from the apparent willingness of the OECD, many member governments, and the media to assert, or at least imply, that all corporate taxpayers are committing tax fraud when they set up legitimate structures to reduce their global tax burden.

The crucial aim of B.E.P.S. activity is to create a single set of consensus-based international tax rules to address this problem, thus protecting tax bases but at the same time offering increased certainty and predictability to taxpayers. The primary scope is to avoid double non-taxation while the new rules should not result in double taxation, unwarranted compliance burdens or restrictions on to legitimate cross-border activity. Consideration must be given as to what a country needs to do in order to convert the recommendations into law. Companies will only be able to achieve a justified tax result and be in line with their local law and with international treaties if certain legal issues are tackled, including group structure simplification, the adapting of inter-company agreements and, more generally, the aligning of legal structures.

In order to implement B.E.P.S. measures in a fast and effective manner, the B.E.P.S. Action Plan provides for the development of a multinational instrument: a multilateral legally binding instrument which will at least incorporate tax treaty

related BEPS measures. The E.U. is of the view that a multilateral instrument is both desirable and feasible, and that it is the most effective way of implementing treaty outcomes under the BEPS project. In fact, work on the development of the multilateral instrument began on 27 May 2015 in Paris. Following the linked O.E.C.D./G-20 mandate, the ad hoc group was to complete its work, with 80 countries participating, by mid-August.

SNIPPETS

CLAWBACK OF D.T.R. ON DISTRIBUTION OF DIVIDENDS

Article 59(1)(a) of the Income Tax Act provides that: “Every company registered in Malta shall be entitled to deduct from the amount of any dividend a tax at the rate paid or payable by the company, relief of double taxation being left out of account, on the income out of which such dividend is paid”. The underlined wording was introduced by Act XLI of 1961, which brought in new arrangements regarding relief from double taxation in anticipation of Malta entering into double taxation relief treaties – even if this wording is actually of general application to all categories of double taxation relief. The wording replaced the text which had existed in the Act ever since the introduction of the tax in Malta in 1948, where section 26(1) had provided that: “Every company constituted under the laws in force in Malta shall be entitled to deduct from the amount of any dividend a tax at the rate paid or payable by the company as reduced by any (double taxation) relief granted on the income out of which such dividend is paid”. Clearly, the two underlined provisions are diametrically opposite. The original 1948 provisions for the familiar tax at source arrangements (and its subsequent set-off when the dividend was eventually taxed in the shareholder’s hands) had the effective result of clawing back from the shareholder any double taxation relief granted to the company. This was of course wrong, and it is not known why the law had been so drafted since the Model Income Tax Ordinance had itself provided: “Every company which is registered in shall be entitled to deduct from the amount of any dividend paid to any shareholder tax at the rate paid or payable by the company (double taxation relief being left out of account) on the income out of which such dividend is paid”. The new arrangements introduced in 1961, therefore, simply reverted the text back to the M.I.T.O. draft, thus eliminating the unwarranted clawback of relief granted at the company level.

PRECEDENTS O.K.....BUT.....

As long ago as 1964, the eminent judge M. Caruana Curran reiterated with a certain degree of emphasis that the Civil Law basis of Malta’s legal system did not admit the principle that decided cases constituted precedents which were binding on the courts in future similar cases. ‘*Lex Scripta*’ is dominant and every judge has, in each case, the responsibility of applying to the best of his ability the written law which he deems to be applicable. This does not, and cannot be taken to mean that in every case the court

is expected or perfectly free, so to say, to re-invent the wheel all over again. The wisdom accruing through gradual incremental decisions is well worth preserving, and our tribunals have had no difficulty in so doing, certainly in tax cases: local and foreign case law as well as authoritative text-books, are freely quoted and followed. The same tribunals have however utilised their freedom of interpretation to good effect to reverse decisions in tax cases which were clearly either manifestly wrong, or which had become too oppressive to be followed. Salient decisions on this issue which may be quoted are the following Court of Appeal decisions:

- ❖ Cases no 25 and 45 as to whether a non-industrial motor vehicle could qualify for capital allowances as Plant or Machinery.
- ❖ Cases 21 and 176 as to whether the filing of a single form of appeal when the relative rules required filing in duplicate was to be deemed to render the appeal null and void.
- ❖ Cases 157, 178 and 185 as to whether the law only set out a time limit for the raising of an assessment, but not also for its service.

In each case, the Court recognised that it was essentially overturning its own decision, but found no difficulty in so doing since it was clear that further consideration of the point at issue revealed that the first decision was not tenable. It must be therefore concluded that our courts have achieved a reasonable *modus vivendi* on this fairly thorny issue.

A RIGHT PROPER MESS UP

There can have been few more unfortunate mix-ups in tax legislation and interpretation in our country than the events and facts emerging from cases nos 99 and 100, both decided by the Court of Appeal on the 27th June 1973. The background to these cases was the perennial problem faced by the Inland Revenue Department in keeping assessment work up-to-date before the advent of P.A.Y.E, P.T., F.S.S. and self assessment. The problem was compounded during the early years of income tax when an inexperienced and untrained staff was required to deal with complex legislation, much of it fairly alien to then current practices in Malta. Staff were few in number and included an appreciable number of employees who had lost their normal means of livelihood during World War II. Everybody was housed in what eventually became a warren of inter-connected residential units eminently unsuitable for the purpose at the bottom of Old Bakery Street, Valletta.

It was soon obvious that the time limit of six years for the raising of assessments would not be sufficient to allow every potential taxpayer's returns to be reviewed in some depth. It was therefore decided to extend this time limit before it had lapsed by extending the six years to eight, but the authorities explained that this extension would only be applicable for the first four years of assessment, namely 1949, 1950, 1951 and 1952. Unfortunately, however, the drafting of the amending legislation (Act XX of 4 July 1955), was rather loose – not to say quite poor. The method used was to

change the word 'six' to 'eight' in the relative provision of the principal Act (i.e. the Income Tax Act as introduced by Act LIV of 1948), and it was then stated in what purported to be 'transitory provisions' that the said amendment would have effect from the commencement of the principal, Act (that is to have retroactive effect) only for the years of assessment 1949, 1950, 1951 and 1952.

For many years, nobody queried that these amendments were in line with Government's declared intentions, but when a reprint of the Income Tax Act was made in 1963 by the Attorney General under the authority of Act XXI of 1963, the notion of limited retroactivity as above set out was omitted, and the reprinted text showed that the time limit had in fact been increased from six to eight years for all years of assessment, and not only for the first four years of assessment.

The correctness of the reprint was challenged in the First Hall of the Civil Court in cases which eventually ended up as published cases nos 99 and 100 before the Court of Appeal. The two taxpayers concerned were entirely different and unconnected, and the cases were initially heard and decided by two different judges both sitting in the First Hall of the Civil Court. Judgement in both cases was delivered on 30th January 1970, but in one case the reprint of the Income Tax Act was held to have been correctly made, while in the other it was held that the reprint was incorrect. In other words, the first judge held that 'six years' had become 'eight years' for all years of assessment, past, present and future, while the second judge held that this had only been done for the first four years of assessment.

The Court of Appeal was inevitably requested to clear up this incongruity, and it did so in very clear terms in the said two cases. The Court agreed that the intention may have been that of changing the time limit only for the first four years of assessment, but it came to the conclusion that the grammatical meaning of the wording used in the amending legislation to give effect thereto did not reflect such intentions, so that the word 'six' had become 'eight' for all years of assessment, past, present and future. The retroactivity expressly indicated in the amending legislation simply meant that retroactivity was to be given in respect of the first four years of assessment: something which was not necessary for other years of assessment. The Court quoted the text-book "Odgers: Construction of Deeds and Statutes" which stated that: 'The intention of the legislature predominates, but where the wording is ambiguous, this intention is best declared by the words themselves'. In other words, if what the legislative authority had enacted did not coincide with what had been its stated intention, the ambiguity between the two had to be resolved in favour of what had been effectively been enacted as law.



MALTA INSTITUTE OF TAXATION

Diploma Course in Taxation 2014-2015: Examination Paper

Date: Thursday, 14th May 2015 Time: 09:00 – 12:00hrs

Premises: IMLI Hall

Instructions:

1. The examination is held in accordance with the Course Regulations. No materials or reference books are to be brought into the exam hall save as allowed by the Regulations.
 2. Black ball-point pens should be used.
 3. Use only one side of each page of the note books provided. Insert full name in block letters and add your identity card number. Sign each page used. Jottings and drafts are to be clearly cancelled.
 4. Candidates are to answer **FOUR QUESTIONS IN ALL**. These should be from three of the sections set out below, so that both questions need to be answered from one of the Sections, while no question will be answered from another Section.
 5. Each question carries twenty-five marks.
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Section 1.

Question 1.

The Sharkey v Wernher principle regarding transfers of business assets to one's private account does not appear to be much in favour currently. What is this principle and how did it emerge in the case in question? Is it applicable in the case of all income chargeable under article 4(1)(a) of the Income Tax Act? Is it a logical measure or just one of those quirks which the theory and practice of income tax seem to throw up from time to time?

Question 2.

Wasting assets, amortisation, repairs and renewals, plant and machinery, implements and utensils, depreciation. What are the arrangements made regarding these matters for income tax purposes? Do you consider these arrangements to be practical and fair?

Section 2.

Question 3.

The Duty on Documents and Transfers Act is the responsibility of the Inland Revenue Department, but it is actually charged and collected by other persons who are not public officials. Explain how this happens, and what measures are prescribed by the law to make certain that, in fact, the duty is charged, collected and passed to the public purse when and as due.

Question 4.

The concept of residence for tax purposes has a central part to play in jurisdictional considerations in income tax: both in the Income Tax Act itself and in the Double Taxation Agreements to which Malta is a party. Outline the arrangements made in the said documents and indicate whether there are any material differences between the two.

Section 3.

Question 5.

Many countries where income tax legislation is, like that of Malta, based on the Model Income Tax Ordinance originally drafted in London in 1922, have incorporated in their law provisions for granting relief in respect of foreign employment income (earned income relief) to persons taxable on a world-side basis. You are required to set out what is the current situation in this respect in Malta. Has this evolved satisfactorily over the years?

Question 6.

“Member States’ existing anti-abuse rules often do not properly take into consideration the freedoms of the Treaty and are therefore increasingly challenged” (extracted from an EC Press Release)

A number of Member States apply anti-abuse rules, such as thin capitalisation and Controlled Foreign Company (CFC) regulations, to protect their national tax bases. However, such Member States existing anti-abuse rules often do not take into consideration the freedoms of the European Treaty and are therefore increasingly challenged by the European Court of Justice (ECJ).

Elaborate on the significance of the above statement and supplement your commentary with details of ECJ case law on the subject.

Section 4.

Question 7.

Attire Group is in the business of manufacturing clothing. The goods are manufactured in the UK by Attire UK Ltd (AUL). Its Maltese company Attire Malta Ltd (AML) is the group company which distributes the clothing to the retailers in Malta, France, UK and Germany. AUL sells the clothing to AML which in turn sells the goods to the retailers. All retailers have a valid EU VAT number in their Member State of establishment. Analyse the Malta VAT implications of the following transactions undertaken by AML:-

- (a) The purchase of clothing from AUL and the resale to retailers in Malta. The clothing is dispatched from AUL in the UK to AML in Malta. AML delivers the clothing to the local retailers.
- (b) The purchase of clothing from AUL and the resale to the retailers in France. The clothing is dispatched from the UK directly to France.
- (c) The purchase of goods from AUL and the resale to retailers in the UK. The clothing is dispatched directly from AUL's factory to the retailers.

Question 8.

Mr. Joseph Borg is a local taxi driver. Three years ago, he inherited some fields in Rabat and, with the help of his wife, he started to sell agricultural produce therefrom. Due to EU funding opportunities, he is hoping to purchase a new sowing machine from Italy, costing around €30,000. The Italian company has asked him for details about his VAT registration in Malta to determine whether they should charge Italian VAT or otherwise. He considers himself to be a small sole trader but lately, his agricultural turnover has been increasing at a steady rate. He is confused over compliance with VAT laws as he intends to keep both his driving and agricultural activities.

Mr. Borg approaches you for advice on his VAT position in Malta to make sure that he is in line with the law. From the VAT certificate which he has shown you, it can be seen that he is registered in terms of Article 11 of the VAT Act of Malta. You are required to prepare a short synopsis for your client to clear his difficulties about his VAT position.

2015 GRADUATION CEREMONY



DOI - Photo - Pierre Sammut

MINISTER'S ADDRESS

For Malta to succeed in converging with the European average *per capita* income in the foreseeable future, it must ensure that its economic growth rate keeps increasing more than the EU average year on year, Finance Minister Prof. Edward Scicluna said on Thursday, 24th September 2015. He was addressing a graduation ceremony of the Malta Institute of Taxation held at the International Maritime Law Institute. Minister Scicluna pointed out that, at the moment, Malta's *per capita* income stands at between 75 and 78 per cent of the EU median. He said that in this context, Malta remains adamantly against tax harmonization in the EU, warning that it would restrain economic growth in developing countries and sound their death knell. Minister Scicluna stressed that taxation is a very serious affair: if not handled well, it can ruin an economy, while higher taxation stifles entrepreneurship and initiative. 'Taxation changes one's behavior and we have to be careful to change in the right direction', said Prof. Scicluna. 'We are working to make work pay, by reducing income tax. We are proud to be doing this while maintaining – and even switching marginally to – consumption taxes. At the moment Malta is first in the EU for the least level of taxation on labour.' At the end of the ceremony, the Minister presented the certificates to 49 students who graduated Diploma in Taxation.

TRUST LAW IN MALTA²

BASIC CONCEPTS AND DEVELOPMENTS OVER THE YEARS

As has been noted in this series of articles, Malta's first trust law was essentially based on the trust law which had been enacted in 1984 by Jersey, Channel Islands. This was a brief but extremely lucid document, and it covered all the fundamental principles and essential points regarding trusts which had flourished in a Common Law environment. Malta's version of this legislation was enacted on 2nd December, 1988 as the Offshore Trusts Act³. Inevitably, the Maltese version had to be tailored to meet local requirements, and the main changes effected were set out in the first article in this series. In a fairly rapid process of development which has taken place over the years since its first enactment, trust law in Malta has developed quickly: shedding the initial 'offshore' orientation, and evolving to meet the requirements of modern commerce and society in general, while not forgetting the original family concepts which had given rise to the institute in the first place. Better and further alignment with the normal laws of Malta has also been effected: at the same time, fiscal laws were amended in line with these amendments.

This article is divided into two parts: the first part sets out the main fundamental and generally accepted aspects of a trust, while the second part traces the process of development in the law in Malta over the years, and its re-orientation towards modern requirements. Inevitably, cross references to what is the actual position in Malta are not absent in the first part.

The Fundamental Concepts

The person who creates a trust is known as the settlor. The person who holds the property of the trust for another's benefit is known as the trustee. The person who is benefitted by a trust is known as the beneficiary. The property (of any kind) which is comprised in a trust is the trust property. Suppose that a parent signs over some shares to a trust company to manage for one of his children, with instructions to give the child a certain part (or all) of the income till he is 25 years of age, at which time the trust will be terminated and all the property therein will be handed to the child. The parent is the settlor, the company is the trustee, the shares are the trust property and the child is the beneficiary.

² This is the second in a series of articles on Trusts in Malta prepared by Edwin A Vella.

³ Act XXXIV of 1988.

A fiduciary relationship exists in the law and practice of trusts whenever a settlor relies on the trustee and places special confidence in him. The trustee must act in good faith, as a *bonus pater familias*, with strict honesty and due regard to protect and serve the best interests of the beneficiaries. A fiduciary relationship also exists between the trustee and the beneficiaries. The trustee takes legal title to the trust property, which means that the trustee's interest in the property appears to third parties to be one of complete ownership and possession, but the trustee does not have the right to receive any benefits from the property: the right to such benefit lies solely with the beneficiary. The terms of the trust are the duties and powers of the trustee and the rights of the beneficiary as determined and set out by the settlor on the creation of the trust. Any breach of duty imposed on a trustee by law or by the terms of the trust, and any act or neglect on the part of the trustee which is not authorized or excused by law or the terms of the trust is defined by law as a breach of trust⁴, and may render the trustee subject to civil (and possibly also criminal) penalties.

A trustee must be loyal to his beneficiaries, administering the trust solely for their benefit, and to the exclusion of personal profit or advantage. Trustees are not entitled to any fees for their services, except as may be set out in the trust deed. They are however entitled to reimbursement of expenses incurred on behalf of the trust. But a trustee who sells trust property to himself would be guilty of a conflict of interest and hence may fall into a breach of trust. The trustee must defend the trust against baseless claims, but he should not waste trust assets in defending claims which are manifestly valid. It is a fundamental rule (howsoever written into any legislation) that the trustee cannot intermingle the trust's estate with his own estate. Apart from anything else, of course, this is a basic common sense principle which every administrator should follow. The trustee will generally be given directives in the trust document as to how he should dispose with income and capital, and he should seek to follow such instructions in the best way possible as circumstances may indicate over the years. As a *bonus pater familias*, it is essential that the trustee does his utmost to conserve the capital (or the property) of the trust over the years in the light of events over the years. Advice as necessary should be taken for this purpose from qualified sources.

Trusts in Malta can only be created by will or other written instrument, but a declaration of trust is accepted as valid as long as it is clear. There was no provision for oral trusts, which could therefore not be considered to be available in Malta⁵. Trusts comprising immoveable property must be created by public deed to be enforceable. When a trust is created by will, the resulting testamentary trust will only

⁴ Trust and Trustees Act, Cap 331: article 4.

⁵ Possibility of oral trusts was introduced later: see below re amendments by Act XIII of 2004.

be valid if the will itself conforms to the requirements of civil law regarding wills. Trusts cannot override forced heirship and other mandatory provisions of civil law (such as the rules regarding the institute of the community of acquests), but it is specifically provided that the local rules prohibiting entails are not to apply where trusts are concerned. A problem which sometimes exists abroad as to whether the words used by a person, such as desiring, wishing or hoping that something will happen or is to be done, constitutes the creation of a trust or not, does not seem to arise in Malta. In view of our well established culture on wills and testamentary dispositions, such desires, wishes and hopes may create a moral obligation but are not legally enforceable⁶. The settlor must indicate that he wants to create a trust immediately, and proceeds to do so: demonstrating an intention to create a trust in the future is ineffective. It goes without saying that trusts cannot be created for any illegal purpose, but neither can it be created for purposes which are considered to be contrary to public policy – a very fluid term, and which may vary from country to country. If the offending provision pertains to the whole trust, the trust fails in its entirety, but if the offending provision does not affect the entire trust, it is simply struck out and the trust given effect to without it.

Every known trust law has a rule against perpetuity: this does not, however, apply in the case of charitable trusts (see below as to what constitutes a charitable trust). This rule usually states that a trust cannot exist for more than 100 years, but the time limit in Malta is now 125 years. This time limit must be calculated from the moment in time that the trust legally comes into existence⁷. This rule, like most other rules regulating trusts, emerges historically from the United Kingdom. Some centuries ago a trust was created specifically to accumulate wealth over the years, and it was feared that the trust would eventually take over and stagnate the economy of the country. Though in fact nothing of the sort happened, the rule against perpetuity was brought in, but it appears that moves are now afoot to rescind such time limits and let trusts prosper or shrivel in natural fashion. This is not likely to be acceptable in Malta as it would reintroduce entails under another name.

⁶ It may be interesting to note that it is known that the large and important institute subject matter of income tax Court of Appeal case no 26 was created in consequence of an expressed death-bed wish of the person whose name it eventually carried. Another wish expressed by a parent following the disruption of his plans through the removal of entails is also known to have been given effect to by the family after his death. The first person mentioned was domiciled abroad, but all family members concerned in the second case were resident and domiciled in Malta.

⁷ The dispensation granted under the Trusts and Trustees Act from the rules regarding entails must be closely linked with this time limit. There would of course be no sense in putting a time limit to charitable trusts either in recognition of the 125 years time limit or the more general prohibition of entails.

An essential element of every trust is the existence of trust property. This must exist and be definite or definitely ascertainable at the time the trust is created, and during the continuance of the trust. Immovable property, stocks and shares, bonds and bank deposits are the usual types of trust property, but any property interest that can be freely transferred may be put in trust. A traditional rule that mere expectancies cannot be held in trust has been largely overcome by initially creating the trust with a small amount of cash, but granting the trustees power to accept further settlements of property in the future. This enables long term planning to be effected in respect of property that may not be immediately available for settlement on trust, and is particularly useful in family trusts. If the trust property is totally lost, destroyed or distributed to the beneficiaries, the trust automatically terminates. Any insurance or other recoveries, however, becomes trust property and has to be dealt with accordingly. Termination of a trust will not affect any right of action which the beneficiaries may have against the trustees.

In theory, any person who is not incapacitated at law can act as a trustee, but Maltese law severely restricts and qualifies the right to act as trustee. Non-residents can, however, act as trustees, as can companies: but it is difficult to conceive unincorporated associations so doing, though certain professional associations may be acceptable as trustees, in which case the individual components of the associations would probably be deemed to be personally the trustees.

A trustee cannot resign without giving adequate notice to specified authorities and to the settlor or to at least one beneficiary. The trust instrument may however provide otherwise, and the beneficiaries who are legally capable can, by unanimous agreement, dispense with trustees and terminate the trust itself. No problems usually arise in connection with the withdrawal or resignation of a trustee if it can be shown that continuing to act would be an unreasonable, or inappropriate burden for the trustee, and that resignation would not be detrimental to the trust. Moreover, the trust instrument itself may indicate when a trustee can be removed, but a trustee can also be removed for improper personal conduct, dishonesty, incompetence in handling trust property or the dissipation of the trust's estate. Mere friction or incompatibility between the trustee and the beneficiary is insufficient, however, for the removal of a trustee unless it endangers the trust property or makes the accomplishment of the trust purposes impossible.

Every trust which is not a charitable trust must have a designated beneficiary or one so described that his identity can be readily identified at the appropriate time. It becomes a question of fact whether this requirement has been met in any particular case. Thus, a trust to benefit one's children is completely clear, but a trust for one's

family may be deemed not to be. When an ascertainable class exists, a settlor may grant the trustee the right to select beneficiaries from that class. However, a trust created for the benefit of any person selected by the trustee is not enforceable. If the settlor's designation of an individual beneficiary or a class of beneficiaries is so vague or indefinite that the individual or group cannot be determined with reasonable clarity, the trust will fail.

Charitable trusts are different from normal trusts in two fundamental matters: there is no fixed period for their existence, and the beneficiaries must consist of an identifiable segment of the public at large: say families having disabled children. In no case will a charitable trust be recognized if there is a private link between the settlor and the beneficiaries: say the disabled members of one's family. This does not mean that a trust cannot be set up in the latter case, but simply that it will not be accepted as a charitable trust entitled to such benefits as the state may desire to grant to such institutions – say tax exemptions. The public character of charitable trusts was emphasised in the leading income tax case of *Pemsel v Special Commissioners*⁸, where it was held that the legal meaning of charity comprises four principal divisions: trusts for the relief of poverty, trusts for the advancement of education, trusts for the advancement of religion, and trusts beneficial to the community not falling under any of the preceding heads. The said case, which has been regularly followed in Malta, represented a modern crystallisation of thinking in the United Kingdom on the matter which had first expressed itself in the so called Statute of Elizabeth. Today, many local laws (including the Trusts and Trustees Act) contain a definition of what constitutes charity for the purpose of the law in question, but nothing much has been added except that certain activities, such as the advancement of sport, are today specifically considered as being beneficial to the community.

Whether a trust is charitable or not does not depend on the expressed wishes of the settlor, or on what is set out in the trust deed. In case of conflict, the courts will examine the alleged charity and evaluate its social benefits within the above context. The main bone of contention continues to be whether the trust is of a public character. This requirement does not mean that everybody can be entitled to benefit from the trust, but that beneficiaries must be a definite segment of the community composed of indefinite persons, and that persons from that segment will from time to time receive benefits accordingly⁹.

⁸ 3 T.C. 53.

⁹ The leading Court case in Malta on this subject remains the fairly old case no 27 where the Court accepted the proposition that a legacy made to provide funds to help the process of declaring a specified person to be a saint of the Catholic Church was of public interest, even though the would be saint was the brother of the person making a legacy.

Development through amendments

There have been several amendments made to the law regarding trusts in Malta since the enactment of the legislation in 1988. These have seen the law moving from Offshore Trusts, to simply Trusts and eventually to Trusts and Trustees. This article will now review the main amendments so made and the principal developments in the theory and practice of trust in Malta. The original law is not itself being examined in detail as it mostly followed the admirable Jersey codification of the classical provisions of trust law referred to above. It will also be appreciated that many amendments made in the legislative process are merely of a 'house-keeping' nature: correcting printing and other similar errors, substituting references to other laws as these are themselves amended and following developments and requirements of European regulations. These amendments are mostly being left out of the review though they obviously have their own importance.

Act XIV of 1989. This amendment was enacted barely six months after the principal law had itself been passed. Most of the amendments made were of a housekeeping nature referred to above, but the prohibition of offshore trusts owning immovable property in Malta was extended to companies owning immovable property or any other company registered in Malta that was not itself an offshore company. A fixed date for the payment of tax due by offshore trusts and by beneficiaries from such trust was also introduced. There was no definition of what constituted income received by beneficiaries, but presumably this would be some sort of annuity. In any case, none of these provisions are any longer operative.

Act XX of 1994. This was actually a separate law entitled Recognition of Trusts Act and it ratified the Hague Convention on the law applicable to trusts and their regulation. It also set out in detail which sections of the Convention were to be considered as forming part of the Laws of Malta and made provision for safeguarding certain mandatory rules of Malta's Civil Law which were to continue to supersede the provisions of the Convention. These included provisions for:

- (a) The protection of minors and incapable parties;
- (b) The personal and proprietary effects of marriage;
- (c) Succession rights, testate and intestate, especially the indefeasible rights of spouses and relatives;
- (d) The transfer of title to property and security interests in property;
- (e) The protection of creditors in matters of insolvency;
- (f) Protection of third parties acting in good faith.

The Second Schedule to Act XX of 1994, however, also made various amendments to the Offshore Trusts Act, which was now renamed the Trusts Act. These provisions were intended to bring offshore trusts onshore through the surgical removal of this concept. It made provision regarding the proper law of trusts and for foreign trusts in general. This seems to have been intended to correct an error made when transposing the Jersey law to Malta, but are not being detailed as they can only be of limited interest. Further amendments allowed trusts to change their name (something not very usual elsewhere), and recast the provisions relating to protective trusts in the case of beneficiaries becoming bankrupt or insolvent. Act XX of 1994 also wrote in the concept that the beneficiaries may, by unanimous decision, require the termination of the trust, and the distribution of its assets between them. Safeguards were however introduced where termination could harm such persons as minors, interdicted persons or persons still to be identified.

The Second Schedule introduced formally into the law the office of Protector of a trust. Certain minimum powers of protection were suggested, and it was laid down that, in the exercise of his office, a protector was not to be deemed to be a trustee. The normal concepts regarding a possible breach of trust activities cannot, therefore, be invoked against a protector. There appears to be no prohibition from a protector being one of the trustees, even though this would be somewhat of a contradiction.

Clear provisions were made for following and recovering trust property which had been alienated through breach of trust, but *bona fide* purchasers acting without knowledge of the breach were given protection. Protection was also given to trust assets in cases where the trustee himself became bankrupt or insolvent.

ACT XIII of 2004. The amendments introduced by this Act gave the definitive shape to the law as we know it today. It was an extremely lengthy piece of legislation: 119 pages in total, of which only 55 pages (Part I of the Act) concerned directly the Trusts and Trustees Act. The remaining 64 pages concerned other laws which required alignment to cater for the reality of having a trust law as part of the normal legislative set-up of the country. Part XIV, however, repealed the Recognition of Trusts Act and transferred all matters regarding the Hague Convention to the Trusts and Trustees Act. The other laws affected by the amendments now brought in were:

Civil Code: Cap 16¹⁰

Notarial Profession and Notarial Archives Act:

Cap 53

Income Tax Act: Cap 123

External Transactions Act: Cap 233

Merchant Shipping Act: Cap 234

Immovable Property (Acquisition by Non-

Residents

¹⁰ A review of the important additions made to the Civil Code by this Act can be seen at the end of this article.

Land Registration Act: Cap 296	Act: Cap 246
Duty on Documents & Transfers	Malta Financial Services Act: Cap 330
Act: Cap 364	Investment Services Act: Cap 370
Banking Act: Cap 371	Income Tax Management Act: Cap 372
Prevention of Money Laundering	Financial Institutions Act: Cap 376
Act: Cap 373	Companies Act: Cap 386
Arbitration Act: Cap 387	Insurance Business Act: Cap 403
Legal Procedures (Ratification	
Of Conventions) Act Cap 443	

As regards the Trusts and Trustees Act, the amendments made include several 'housekeeping' adjustments which are not being mentioned. Comments are being restricted to the more important issues, of which there were several.

Several new definitions were brought in, including one which states that a trustee must be 'an approved person'. This continued the tradition that only persons licensed by the Financial Services Authority are allowed to act as trustees. This appears to be an unjustified restriction in this day and age, and contrasts with the position in most other jurisdiction. Only limited exceptions are made, as set out below. The tight rules made by the law regarding trustees should be more than sufficient safeguard against would be 'cowboys', and settlors setting up a trust should be free to select anybody whom they trust to act as trustee. This amending law has also amplified more than sufficiently the status of trustees and their obligations

A full-blown definition of 'charitable purpose' was also introduced: this was more than welcome. As a matter of principle, 'charitable purposes' was defined to include "any charitable and philanthropic purpose', but specific examples were also given: these were later still further expanded by Act XIII of 2007 which is dealt with below.

A very wide definition is given in respect of 'commercial transaction'. The list was also made extendible by administrative action by the Minister. This definition is important because trusts have constituted very useful tools in certain commercial transactions facilitating, among other things, the solution of structural, procedural or financial problems. Some of the areas beneficially affected are retirement schemes, unit trusts, security offerings and time share arrangements. Linked with parallel income tax provisions, this has opened up new possibilities which may have previously been unavailable in Malta, or at least not clearly understood in the context of trusts. Collective Investment Schemes set up under the Investment Services Act were released from the normal perpetuity clause in trusts.

Proper recognition was given to foreign trusts and, as indicated above, all matters relative to the Hague Convention were transferred to the Trust & Trustees Act. It was

also made clear that the anti-entail rules of Maltese laws could not inhibit trusts. There was also an expansion upon the mandatory rules in Maltese Law which could not be thwarted through the use of trusts, but it was made clear that trusts recognized by Malta (including both local and foreign) could not be prohibited from infringing mandatory rules of other jurisdictions. Power was also given to the Court, where a beneficiary was domiciled in Malta, to order in case of discretionary trusts, the trustee to give due consideration to persons who might be entitled to maintenance.

This amendment reintroduced into our law the possibility of having oral trusts; these had been omitted from the original text but were now admitted, linked with the provisions of the Civil Code relative to mandate and deposit. On the other hand, a provision which has been hotly debated elsewhere regarding a trustee's obligation to not only safeguard the property of the trust, but also to do his best to enhance its value, was deleted. It remains dubious whether this is a proper function to be expected from a trustee.

Beneficiaries were given certain rights of requesting details, and trustees were now saddled with reporting requirements, particularly where charitable trusts were involved. Adequate safety has been given to third parties dealing with trustees. Rights of creditors were strictly limited to a beneficiary's interest in the trust. Further amendments restated the circumstances when a trust was to be deemed to have failed and what was to be done with any trust property still in existence. Arrangements were specified as to how a trustee could resign his post and be replaced, and what was to be done in case of his death. The much dreaded possibility of conflict of interest of trustees was also given attention.

Very detailed provisions were introduced regarding court proceedings. It appears that most, if not all, proceedings regarding trusts have now been assigned to the Court of Voluntary Jurisdiction, the Civil Court, Second Hall, whose decision has been made final and not subject to appeal. Where a trustee feels that the normal rules regarding confidentiality may be infringed during court proceedings, he is now authorised to seek guidance on the matter from the M.F.S.A.

A vast array of conditions was introduced regarding who may act as trustee for the purposes of the law, even though in principle everybody can act as trustee. As indicated above, the basic assumption that trustees must be persons approved by the M.F.S.A. still holds good, but several exemptions from this requirement were introduced – together with exceptions to the exemptions! A basic condition to the exemptions appears to be that the trustee concerned would only incidentally be acting in that capacity, and that he does not publicly hold out himself to be a trustee by profession. Detailed provisions were also made in respect of companies acting as

trustees. The M.F.S.A. was given powers to issue regulations in this regards, but it does not appear that this has been done except in the case of notarial trusts¹¹. All in all, however, so many complicated provisions have been written into the law that it becomes difficult to specify exactly who is and who is not authorized to act.

This amendment also introduced the concept of a private trustee, that is to say trustees who were not required to be authorised by the Malta Financial Services Authority to Act. Such persons had however to be either close relatives or long standing friends of the settlor. If the trust was constituted by testamentary disposition, the trustee has to prepare an inventory, while if it was created inter vivos, it had to be done via a notarial deed with a notary who became to be known as the depositary notary. Such trustees could not be remunerated in any way, nor could they hold out themselves to be trustees or act for more than five settlors. A depositary notary was to hold all acts and he could also be a trustee, but not for a trust of which he was the depositary notary. Strict confidentiality was imposed on depositary notaries, while provisions were made for changes in depositary notaries as well as of trustees. This was a simplified and valuable way of creating trusts, but its simplicity has been seriously affected by the provisions enacted as subsidiary legislation above referred to. These were intended to bring the system of depositary notaries more into line with the normal legislation regulating notaries and their archives but, all in all, these cannot but be considered retrograde steps.

Detailed provisions were made regarding the method of applying to the M.F.S.A. to function as trustees. Powers were given to the Authority to grant, revoke or make other orders regarding trustees, including their removal, as it deemed appropriate. M.F.S.A. were authorised to make thorough investigations regarding trustees, as well as of other persons who, though unauthorised, were functioning as trustees. Information could be demanded from practically everybody, except where this was prohibited by the rules of professional secrecy. Duties and obligations in respect of international commitments of operators holding good under the Malta Financial Services Authority Act were made applicable to trustees. The M.F.S.A. could now apply to the Court to have disqualification orders issued against persons prohibiting them from acting as trustees. Rightly or wrongly this power had previously been assumed by the Authority to be vested solely in it. Various offences and sanctions were now detailed and extensive powers of issuing binding rules were vested in the Authority. Finally, extensive transitory provisions were enacted to cater for existing trusts and trustees. (These still appear in the Ministry of Justice web-site).

¹¹ See Subsidiary Legislation 331.05 and 331.06, both dated 15 January 2015.

The above description of the new rules and powers given to the Authority indicates an extensive tightening up procedures and the introduction of fairly draconian rules and regulations. Perhaps as a sop to this process, a right of appeal was introduced against decisions of the Authority. This can be made to the Financial Services Tribunal constituted under the Malta Financial Services Authority Act.

Act XII of 2006. This was the next Act which amended trust legislation, but it actually was the Insurance Intermediaries Act of 2006. This Act also amended other laws which required up-dating to fall in line with the new financial scenarios it contemplated. The Trusts and Trustees Act had also to be amended as regards retirement schemes which have to be handled by the insurance industry. Effectively, such schemes constituted under the Special Funds (Regulation) Act were granted exemption on the same footing as charitable trusts. Furthermore, trustees registered under the said Act were released from the obligation of registering as trustees under the Trusts and Trustees Act.

ACT XIII of 2007. This was actually a law to amend the Civil Code, but the occasion was taken to amend various other laws, including the Trusts and Trustees Act. A new definition was brought in retaining the principle that ‘charitable purpose’ means any charitable or philanthropic purpose, but the following items were specifically included:

- *the advancement of education, including physical education and sports;*
- *the advancement of religion;*
- *the advancement of health;*
- *social and community advancement;*
- *the advancement of culture, arts and national heritage;*
- *the advancement of environmental protection and improvement;*
- *the protection of animals;*
- *the promotion of human rights, conflict resolution, democracy and reconciliation;*
- *the promotion or protection of the interests of other social purpose organisations;*
- *other purposes as may be prescribed by the Minister.*

There is however a detailed prohibition of political activities from being considered to be charitable purposes.

The amendment also made certain provisions relating to trustees of trusts created by wills. These were to override certain provisions of the Civil Code. As by this time the Second Schedule had been added to the Civil Code, regarding legal persons, power was granted to the Minister to issued rules regarding the conversion of one sort of body into another – including trusts. It does not appear that this has been done, at least in respect of trusts.

ACT III of 2009 and ACT X of 2011. These amendments were mostly of a 'housekeeping' nature and need not be considered further in this context.

ACT XVI of 2011. This amendment linked up with new pension arrangements being worked out for the country in that it provided for schemes set up under the Retirement Funds Act and constituted as a trust.

ACT XI of 2014. Though a lengthy piece of legislation, this amendment was largely 'housekeeping' in nature. This resulted in several new definitions and adjustments which hardly added anything to the law, though they did emphasise important matters, such as the addition of 'social' to 'charitable' and 'philanthropic' to the list of 'charitable' trusts (clearly 'social' matters were already contemplated under the latter two terms, apart from being included in qualifying activities).

Several more substantive amendments were however also made. Thus, persons who did not possess the normal qualifications to join the ranks of approved trustees (i.e. not having legal, accounting, financial or fiduciary warrants) could now still be given a licence if in actual fact they proved that in practice they had all the necessary knowledge and skills. It was also made clear that settlors could reserve for themselves certain rights and that, when this was done, trustees acting by following the exercise of such rights could not be accused of breach of trust. More detailed provisions were also introduced regarding termination and lapse of trusts, death of trustees, liquidation of trustee companies and allied matters.

Further tightening up of duties and liabilities of trustees was also effected. Trustees were now also expected to draw up an inventory of the assets of the trust assets when they took up office. It is not clear why this inventory is now required, and what is to be done with it. 'Conflict of interest' was further elaborated upon, and a rather vague possibility given to a trustee to seek guidance from the Court 'as the case may be' when one of the beneficiaries is subject to tutorship or curatorship. It is of course well known that a substantial proportion of family oriented trusts are set up precisely to cater for such individuals.

An important development was the introduction of the office of Enforcer who could be appointed to act as a sort of supervisor of charitable trusts. Such an appointment must be contemplated in a trust deed, which also has to set out how such an Enforcer can be removed and replaced. It is not clear why this additional layer of responsibility was deemed necessary. Another important development is the power now vested in the court to permit the alteration of the charitable purposes of a trust when the original purposes, and reasons for setting up the trust, have become rather clouded over by the natural evolvement of society in general.

There was a further tightening up of the various provisions regarding trustees which had been brought in by the 2004 amendments, while arrangements were introduced

for trust companies set up to act as trustee for a specified family trust. Auditors of trustees (*not of trusts*) were now required to report to the M.F.S.A. when the trustee was in any way infringing his obligations, whether under the law or otherwise. This applies clearly only to trust companies, and the requirement supersedes any other rules regulating auditors. The competent authority, no doubt the M.F.S.A., was also given powers to take steps to protect the public interest where circumstances so warranted through the cancellation or suspension of licences to act as trustees. The provisions regarding following E.U. Regulations were up-dated. Further transitory provisions were also introduced.

ALIGNMENT OF THE CIVIL CODE WITH TRUST LEGISLATION

Act XIII of 2004 introduced, inter alia, amendments to the Civil Code specifically aimed at aligning the Code with the new realities emerging from the introduction of the law on trusts¹². Thus, as a matter of principle, property held under trust is to be regulated by the special law on trusts¹³ and, to the extent applicable, the rules of the Code relating to trusts. The wording used is rather ambivalent, but it is clear that an alignment between the two legal instruments was being sought.

All transactions of property in and out of trusts are to be regulated by the provisions of trust legislation, but the transfer of ownership, or of rights over ownership, is to be made in accordance with the rules of the Civil Code. The guiding factor is whether the trustee has the legal right to effect the transactions. Reserved portions are not exempt from the above rules, but the proceeds from the sale of any such portion continue to appertain to the person having the right thereto. A parallel provision is made for cases where the Code provides for the limitation of rights of enjoyment of benefits, with a consequential reduction in settlements. This provision would apply to such cases as where benefits are due to persons who are incapable at law of receiving property, or where the settled property is in excess of what is allowable to be left by will to a spouse. The normal rules of the Civil Code are to be applicable but fairly complicated rules are specified as to how this is to be given effect to. There is an added safeguard that these provisions are not to be considered to infringe the mandatory provisions of the Civil Code regarding such matters.

Persons who under the Civil Code are deemed to be unworthy of receiving by will, are likewise to be deemed unworthy of receiving benefits via a trust. Clearly the limitation operates only in the case of a trust set up by a person from whose estate one

¹² Now found at articles 958A to 958J of the Civil code.

¹³ Obviously the Trusts & Trustees Act, Cap 311.

would be considered to be unworthy of inheriting. Possible benefits from other trusts are in no way affected.

Further complex provisions are made in respect of settlements which, like donations, have to be reduced or collated to the settlor's estate. It is made clear that a trustee appointed in terms of a testamentary trust is not, thereby, to be deemed to have been instituted as testamentary executor. Where, however, the same persons is appointed both as a trustee and as a testamentary executor, the executorship aspect is to be regulated in terms of the Civil Code until this has been exhausted (or fulfilled as the Code sets out).

An important provision is made in respect of trusts created by a non-domiciled person in respect of property, whether movable or immovable, situated in Malta. If such person is of full age and of sound mind under the laws of his own domicile and of Malta, the normal rules of the Civil Code relating to succession and to reserved portions are not to apply. This settles definitely (at least in respect of Malta) a problem which as indicated in other articles in this series has caused many headaches in Civil Law jurisdictions regarding this issue.

There has also been introduced in the Civil Code limitation to, or non applicability of certain perhaps less important provisions of the Code. These are not being reviewed.