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The notion of "similar to a company" for the purposes of the Income Tax Acts

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This Position Paper sets out the MIT's views on the characteristics to be considered when determining whether a foreign body of persons may be regarded as "similar to" a Maltese limited liability company

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Position Paper on the notion of "similar to a company" for the purposes of the Income Tax Acts

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Context

Article 2(1) of the Income Tax Act, Chapter 123 of the Laws of Malta (the "ITA") defines the term "company" for the purposes of the Income Tax legislation to refer, in the first place, to companies incorporated under domestic legislation, specifically:

> *(a) (i) a limited liability company constituted under the Companies Act or under the Commercial Partnerships Ordinance; or*
>
> *(ii) any other company constituted as such under any other law in force in Malta;*

Pursuant to sub-article (b)(i) of the definition, the term "company", for the purposes of the applicatin of the provisons of local Income Tax legislation also includes:

> *(b) (i) "any body of persons constituted, incorporated or registered outside Malta, and of a nature similar to a company referred to in sub-paragraphs (i) or (ii) of paragraph (a) above".*

The purpose of this paper is to examine the notion of "similar to" in the context of assessing whether a given body of persons constituted, incorporated or registered outside Malta can be regarded as a "company" for the purposes of the relevant provisions of local Income Tax legislation.

The notion of "similar to"

The expression "similar to" is a fundamental aspect of the qualitative analysis required by the law in determining whether a body of persons constituted, incorporated or registered outside Malta (hereinafter the "Tested Legal Form") should be characterized as a company in terms of article sub-article (b)(i) of the definition of "company" in article 2(1) of the ITA.

The expression "similar to" is not defined in the ITA. The Malta Institute of Taxation is not aware of any supplementary sources of local interpretation concerning the expression, whether in terms of administrative guidelines or judicial pronouncements.

It is submitted that, in light of the ordinary meaning of the expression "similar to", the Tested Legal Form is not required to be identical to a limited liability company incorporated under the laws of Malta. Rather, the Tested Legal Form must have sufficiently similar attributes to a limited liability company incorporated in accordance with the Laws of Malta (hereinafter a "Maltese company").

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Assessing whether the Tested Legal Form is "similar to" a company incorporated under the laws of Malta

It is our view that, in assesessing whether a Tested Legal Form is of a nature "similar to" a Maltese company, reference should be made to (a) the foreign law in terms of which the entity is constituted, incorporated or registered (as the case may be) and (b) to the constitutive documents of the Tested Legal Form. The features of the Tested Legal Form as emerge from the relevant foreign legislation and legal documentation should then be compared to the features and characteristics of a Maltese company (see below) in order to determine the similarity or otherwise of those relevant features.

It is the view of the Malta Institute of Taxation that the characterisation of the Tested Legal Form for tax purposes in the jurisdiction of its incorporation should not be considered as a relevant factor in the analysis of whether the said Tested Legal Form can be said to be "of a nature similar to a company" for the purposes of article 2 of the ITA.

The Malta Institute of Taxation considers the following to be the key characteristics of a Maltese company:

i. A Maltese company is vested with legal personality, separate from that of its directors and member/s, which enables it to enter into contracts and be the subject of rights and obligations at law.
ii. A Maltese company is formed by means of capital divided into shares or stock which are held by its member/s.
iii. The liability of the member/s of a Maltese company is limited to the amount, if any, which is unpaid on the shares held respectively by each of them, subject to any mechanisms contemplated in terms of the laws of Malta governing the extension of liability to the Maltese company's owner/s or administrators in those circumstances as contemplated by the relevant law.
iv. A Maltese company's constitution and existence is governed by a Memorandum and Articles of Association, which outline, amongst other things, the member/s' rights to votes, to profits, and to assets upon a winding up.
v. A Maltese company is managed by a board of directors, or equivalent administrators, who exercise all of the company's powers, other than those which are limited to the member/s.

The Malta Institute of Taxation supports the application, in practice, of a qualitative methodology to the Tested Legal Form, taking into account all the relevant facts and circumstances. The Institute is of the view that it would not be practicable to, at the outset, ascribe a weighting to any of the above-mentioned individual characteristics or features, and each case should be assessed on its own merits. While the outcome of an assessment may be clearer where all factors point toward the same conclusion, it is noted that many cases are not as straightforward. While meeting the majority of these factors would be

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important to the overall analysis and final assessment, it is, in the Institute's view, important to consider that different factors / features may in the circumstances carry a different weighting when arriving at the final determination.

In formulating its position, the Institute has considered the approach adopted under English law, in particular, the approach adopted by the UK Court of Appeal in Memec plc v CIR[1] (70 TC 77), which has since been endorsed in the UK by His Majesty's Revenue and Customs (HMRC) in INTM180010. The *Memec* case did not deal specifically with a determination as to whether a foreign entity was to be regarded as "similar to" a UK company. Nevertheless, it is the view of the Malta Institute of Taxation that the principles and approach emerging from *Memec* are a helpful methodological guide that may be referred to when assessing whether a foreign company is to be regarded as "similar to" a Malta Company.

Note: It is the view of the Malta Institute of Taxation that any reference to practices and/or interpretation adopted in terms of English law to support an assessment of the notion of "similar to a company" for the purposes of the ITA, should be made exclusively in the context of the analysis of the features of the Tested Legal Form against the features of a Maltese Company identified in (i) to (v) above.

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[1] In this particular case, the UK Court of Appeal considered the characteristics of English partnerships and Scottish partnerships in order to assess which features are relevant to an entity being treated as transparent, with a view to determining the extent to which such features are shared by a silent partnership. In summary, in its judgement, the UK Court of Appeal identified a number of elements should be taken into account when determining the classification of a foreign entity for UK tax purposes:

- Whether the entity is legally distinct from the partners of whom it is composed;
- Whether the entity issued something that serves the same purpose as share capital;
- Whether, in terms of liability for business debts, the responsibility falls either on the entity itself or on the persons who have an interest in it;
- Whether the entity itself or persons who have an interest in it are the owners of the assets used in business activities;
- Whether the persons who own an interest in the entity are automatically entitled to a share of its profits, or if their share of the profits is determined by the decision of the entity or its members after the profits have been generated.

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