Jurisdiction to Tax

JOANNA SPITERI

The main legislative provision under Maltese law which provides for jurisdiction to tax is article 4 sub-article (1) of the Income Tax Act ('ITA').[1] Such article deems as taxable any income of a person, accruing in or derived from Malta or elsewhere, and whether received in Malta or not, in respect of:

i. Gains or profits from any trade, business, profession or vocation, including the profit arising from the sale of a property acquired for the purpose of profit-making by sale, or from the carrying on or carrying out of any profit-making undertaking or scheme;
ii. Gains or profits from any employment or office, including the value of any benefit provided by reason of any employment or office;
iii. Dividends, premiums, interest or discounts and any pension, charge, annuity or annual payment;
iv. Rents, royalties, premiums and any other profits arising from property.[2]

The proviso to article 4 provides that in the case of income arising outside Malta to a person who is not ordinarily resident in Malta or not domiciled in Malta, the tax shall be payable on the amount received in Malta. Such proviso deems capital gains arising outside Malta to a person who is not ordinarily resident in Malta or not domiciled in Malta, or to a person who is charged to tax at the rate of fifteen cents in the euro, as not subject to tax. As regard to any person charged to tax at the rate of fifteen cents in the euro, the tax payable is only in respect of any income or capital gains arising in Malta and on any amount of income arising outside Malta and received in Malta.

Hence, in a nutshell, Malta establishes its right to tax individuals and bodies of persons on the basis of territoriality, ordinary residence, domicile and remittance. Mainly, Malta has jurisdiction to tax income and taxable capital gains arising in Malta; income and taxable capital gains arising abroad to persons who are ordinarily resident and domiciled in Malta; foreign source income derived by persons who are ordinarily resident but not domiciled in Malta which is remitted

[1] Chapter 123 of the Laws of Malta, Income Tax Act
[2] Income Tax Act, article 4 sub-article (1)

to Malta; and foreign source income derived by persons who are domiciled in Malta but not ordinarily resident in Malta which is remitted to Malta.

TAXABLE CAPITAL GAINS

In terms of article 5 sub-article (1)(a) of the ITA, **taxable capital gains** include:

i. Gains or profits arising from any transfer of the ownership or usufruct of any immovable property or the assignment or cessation of any rights over such property;
ii. Gains or profits arising from the transfer of the ownership or usufruct of or from the assignment or cessation of any rights over any securities, business, goodwill, business permits, copyright, patents, trademarks and trade-names;
iii. Gains or profits arising from a transfer of the beneficial interest in a trust;
iv. Gains or profits arising from a deemed transfer of securities and from a transfer of value in securities (value shifting); and
v. Gains or profits arising from the transfer of the ownership or usufruct of or from the assignment or cessation of any rights over any interest in a partnership.

DOMICILE

The term **domicile** is not defined in the ITA. It borrows the notion of domicile from British Common Law. Domicile refers to the physical presence in a country as an inhabitant of it. It is noteworthy that domicile is not only about a physical stay, but is also about the intention to live permanently in a country.[3]

Every individual acquires the domicile of his father at birth, known as the domicile of origin. Domicile of choice is acquired by the combination of residence and the intention of permanent or indefinite residence.[4] This means that if the necessary intention is present, an existing domicile of choice can sometimes be abandoned and another domicile is acquired. A person must always have a domicile and such person may only have one domicile at the same point in time.

A body of persons is domiciled in its place of incorporation, being its country of registration.

RESIDENCE AND ORDINARY RESIDENCE

The term **ordinary residence** is not defined in the ITA. The said Act only defines the term **resident**, but the terms **residence** and **ordinary residence** are not synonymous terms in the case of individuals.

An individual can be a resident of Malta without being ordinarily resident in Malta. Ordinary residence requires more than residence because it requires

3 Robert Attard, Principles of Maltese Income Tax Law (Malta Institute of Management, 2013) p 172
4 *ibid*

residence in a place with a degree of continuity. Ordinary residence means residence which is normally part of an individual's everyday life.[5]

In the case of bodies of persons, **residence** and **ordinary residence** have the same meaning. Article 2 of the ITA states that a company is resident in Malta if it is either incorporated in Malta, or if it is managed and controlled in Malta.

The place of management and control means the place where the Board of Directors meet and where the main trading and strategic decisions are taken.[6]

AN OVERVIEW OF INCOME TAX ON CAPITAL GAINS VS PROPERTY TRANSFER TAX

Prior to the introduction of income tax on capital gains, the parties in a transfer of immovable property could more easily under-declare the price of the property; thus having a direct impact on the rate of duty payable on such transfers.

Following the introduction of income tax on capital gains, it became in the interest of the buyer to declare a more realistic transfer value, so that in a subsequent transfer, he would not be liable to a higher incidence of income tax on capital gains.[7]

However in those instances where the cost of acquisition is very low relative to the transfer value, property owners might prefer to postpone income tax on capital gains indefinitely rather than selling the property and paying income tax on capital gains that approximately would amount to one-third of the profit made.

While the 12% Property Transfers Tax ('PTT') may appear attractive to owners of vacant property held for a long time to place the property on the market, this option only benefits transactions which result in a mark-up below the 52.17% threshold.[8] Nonetheless, it is better for the taxpayer to opt to be taxed under the 'old' tax system (i.e. taxed at 35% on capital gains made) where the seller makes a loss on sale because if he opts to be taxed under the 'new' tax system (i.e. 12% PTT), he still has to pay 12% tax on the value of the property regardless of whether he has realised a gain from the transfer of the property in question.[9]

The 12% PTT system was initially deemed to be unfavourable since the tax is

---

5 Robert Attard, Principles of Maltese Income Tax Law (Malta Institute of Management, 2013) p 171
6 Robert Attard, Principles of Maltese Income Tax Law (Malta Institute of Management, 2013) p 179
7 Maria Paloma Micallef, Malta's Tax System and European Community Law: Areas of Tension or Concern (LL.D, University of Malta 2009) p 94
8 Calculated in Kathleen Zerafa, Transfers of Immovable Property: Fiscal Implications under the Income Tax Act (Bachelor of Accountancy (Hons), University of Malta 2006) p 40
9 Enzo Refalo, The Fiscal Liability of the Alienor on Transfers of Immovable Property (LL.D, University of Malta 2006) p 115

payable on the transfer value.[10] This issue was resolved by fine-tuning the 12% PTT system several times whereby the taxpayer is now allowed to choose to be taxed up to 35% on profits provided that the transfer takes place in the first twelve years after the acquisition of the property.

As mentioned earlier, Malta establishes its right to tax persons on the basis of territoriality, ordinary residence, domicile and remittance. Malta taxes persons on the sale of immovable property situated in Malta on the basis of territoriality. It is important to point out that the 'old' tax system applies to sale of immovable property situated in Malta or elsewhere whereas the 'new' tax system applies to sale of immovable property situated in Malta only. This means that when a person sells property situated outside Malta and such person is resident and domiciled in Malta and thus taxed in Malta on a worldwide basis, he cannot opt to pay tax under the 'new' system.

[10] Kenneth Swain, Tax on Capital Gains and on Property Transfers (Malta Institute of Taxation, Diploma Course in Taxation 2008/2009) p 3