

# Taxation Newsflash

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## New Law on Retirement Funds

'The Special Funds (Regulation) Act' (Act XVII of 2002), has set up a regulatory framework for Retirement Funds. The Minister of Finance has, by Legal Notice 277 of 2002, appointed the 1st October, 2002 as the day when the provisions of the law regulating such funds came into force. The Malta Financial Services Authority (MFSA) has been appointed as the Competent Authority for the purposes of this Act. The MFSA is a public autonomous body which regulates the whole spectrum of financial services in Malta, including banking, investments and insurance.

A Retirement Fund, is a company established for the principal purpose of holding and investing the contributions made to one or more Retirement Schemes or to one or more Overseas Retirement Plans (the non-Maltese equivalent of a Retirement Scheme). A Retirement Scheme can only invest in Retirement Funds in accordance with the Scheme Document. The Retirement Scheme is a scheme or arrangement established by contract which governs the rights and responsibilities of the Retirement Scheme Administrator and Contributor. Under this arrangement, payments are made to Beneficiaries for the principal purpose of providing Retirement Benefits.

Both the Scheme and the Fund have to be approved by the MFSA. However a Retirement Fund must be registered in Malta, while a Retirement Scheme is to be registered in Malta only if it is situated in Malta. The net effect is that a non-Maltese Scheme i.e. an Overseas Retirement Plan, need not redomicile in Malta but only needs to be approved by the MFSA

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## Permanent Residence Permits in Malta

Malta's Permanent Residence Permit Scheme allows foreigners to settle down in Malta and benefit from an attractive tax rate. While a Permit holder cannot conduct any business in Malta, he or she can still conduct business overseas and this is also possible through a Maltese International Trading Company.

To qualify for a Permit, the foreigner must meet the following requirements:

1. an annual income equivalent to Lm10,000 or capital equivalent to Lm150,000;
2. remit annually to Malta an income equivalent to Lm6,000 and Lm1,000 in respect of each dependant (spouse, children under 21 years of age and/or a parent or grandparent who is wholly dependent on the applicant);
3. either purchase immovable property valued at not less than Lm50,000 (Lm30,000 in the case of an apartment), or lease/rent property for not less than Lm1,800 per annum.

Permanent residents are taxed at the rate of 15% on all income arising in Malta and on all income arising outside Malta (except capital gains) remitted to Malta. The minimum amount on which the tax will be payable is on Lm12,000 covering all members of the family. Therefore the minimum tax is Lm1,800 per annum. The first Lm2,500 is tax free in the hands of a married person, while the amount of Lm1,800 is tax free in the hands of a single person.

A Permit holder can import used household and personal effects, furniture and other domestic articles (excluding firearms and weapons of all kinds) free of import duty if imported within six months of arrival in Malta to take up residence. In such cases import licences are not required. One private motor-vehicle may also be imported free of VAT, although registration tax is still payable at rate of 11% (under 1500cc engine) or 16.5% (1500cc engine or larger).❖

and invest in Retirement Funds registered in Malta.

More detailed Directives on the regulation of Retirement Funds and Retirement Schemes are in the process of being prepared by the MFSA. It is anticipated that such Directives would essentially be based on the regulations which govern collective investment schemes in general.

To be registered in Malta a Retirement Fund must at least satisfy the following criteria:

1. It must be constituted as an Investment Company with fixed share capital (INVCO) or an Investment Company with variable share capital (SICAV) under the Companies Act of Malta;
2. The memorandum of association must state that its objectives are limited to: (a) the receipt of contributions made by one or more schemes, and or by one or more Overseas Retirement Plans and the investment of such contributions and all returns on such contributions in instruments (namely any type of security) or immovable property with the aim of maximising the return on such contributions, (b) the payment of Retirement Benefits to the Beneficiaries of the Schemes or the Overseas Retirement Plans which have invested in such Retirement Fund; (c) to carry on all matters or functions connected or ancillary to the objectives abovementioned.
3. Its name must be one which, in the opinion of the MFSA, is not misleading and;
4. It must have its head office in, and operated in, Malta.
5. It must have at least three Directors;
6. the promoters, the directors and the Retirement Fund Administrator are fit and proper persons to offer the Retirement Fund concerned;
7. the directors, the Retirement Fund and the Retirement Fund Administrator will comply with and observe the provisions of the Act and any regulations or directives prescribed thereunder.

In order to register a Scheme the Scheme Document must contain written terms and provisions which will state:

1. that the principal purpose of the Scheme is to provide Retirement Benefits, that all contributions to the Scheme will be invested exclusively in one or more Retirement Funds, except for ancillary cash;

2. that the Scheme is designed and operated for the exclusive benefit of the Beneficiaries specified in such Scheme;
3. the specific means to be used to identify all current and future Contributors of the Scheme together with their respective obligations;
4. the specific means to be used to identify all current and future Beneficiaries of the Scheme together with the specific means to be used to determine the amount of their respective Retirement Benefits and the timing of payment of such Retirement Benefits;
5. the name, address and the telephone number and email address if available of the Initial Retirement Scheme Administrator appointed to carry out the administrative requirements of the Scheme;
6. the rules or other criteria governing the valuation of assets and liabilities attributable to the Scheme and the timing of such valuations;
7. the rules governing admissible costs and expenses payable out of the Scheme;
8. the method of appointment, removal, and replacement of the Retirement Scheme Administrator and the Asset Manager, auditor, or actuary of the Scheme;
9. the rules governing the surrender, termination or forfeiture of a Retirement Benefit;
10. the applicable rules in the event of an inability or failure by a Contributor to fulfill its obligations;
11. the rules governing amendments to the Scheme Document;
12. the circumstances leading to the winding up of the Scheme, other than such circumstances established by law;
13. that there exists no statutory provision for compensation in the case where a Scheme or Retirement Fund is unable to satisfy the liabilities attributed to it;
14. that the Registration of the Scheme or Retirement Fund is not an endorsement by the MFSA of the Scheme's or the Retirement Fund's financial performance.

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### Tax implications

No specific tax regime has been set up under the new law on retirement funds. Therefore the tax position of the Fund, the Scheme and the contributors and beneficiaries of the Scheme are regulated by general principles of Maltese income tax law. The Scheme is not a legal person of its own right since it is based on a contract namely the Scheme Document. The Retirement Scheme Administrator is investing in Retirement Funds on behalf of the contributors/beneficiaries and will pass on retirement benefits to the beneficiaries when these are due to be paid. This should lead to the conclusion that the Scheme is tax transparent, leaving to be considered the tax position of the Fund and the beneficiaries.

The tax regime for Funds under Maltese law is based on the classification of funds into prescribed or non-prescribed funds.

- i) a prescribed fund - a fund which has declared that the value of its assets situated in Malta amount to at least eighty-five percent of the value of the total assets of the fund;
- ii) a non-prescribed fund - a fund which has declared that the value of its assets situated outside Malta amount to at least eighty-five percent of the value of the total assets of the fund.

Non-prescribed funds benefit from a tax exemption on all income and capital gains.

Prescribed funds only pay tax on investment income (other than investment income paid by another licensed collective investment scheme) as defined in the Income Tax Act. Investment income arising in Malta received by a prescribed fund is subject to a withholding tax and such income cannot be received by the fund gross of tax. The applicable rate of withholding tax is currently 15% on bank interest and 10% on investment income other than bank interest (e.g. bond interest). Both prescribed and non-prescribed funds are not entitled to a credit or to a refund of such withholding tax.

In respect of both prescribed and non-prescribed funds, capital gains, dividends, interest and any other income from foreign securities may be subject to tax imposed by the country of origin concerned and such taxes may not be recoverable by the Fund

or its Beneficiaries unless a double tax treaty is in force between Malta and the country of origin of the payment.

Turning now to the beneficiaries of a Retirement Fund, under general principles of income tax, the lump sum payment due on retirement or even an annuity paid upon retirement would constitute a payment of accumulated capital not income. Therefore such payments would only be taxable under the rules governing capital gains, namely:

- i) Capital gains realised by non-residents, whether the fund is prescribed or non-prescribed, are exempt from tax in Malta.
- ii) Capital gains realised by Maltese residents on non-prescribed funds are subject to a 15% final withholding tax.
- iii) Capital gains realised by Maltese residents on prescribed funds are not subject to tax as long as the Fund is listed on the Malta Stock Exchange.

The new law on Retirement Funds is another stage in the evolution of Malta as a leading financial services centre in Europe. Top-notch institutions have now been benefiting from Malta's attractive, flexible yet rigorous approach to financial services regulation for a number of years, and there can be no doubt that the same approach will be used under the new law, thereby attracting many more institutions, this time in the retirement funds industry, to Malta. ❖

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