Malta alert
Notional interest deduction rules introduced

Malta's government introduced a notional interest deduction (NID) regime on 5 October 2017 as envisaged in the 2017 budget. The new regime will be effective as from the 2018 year of assessment.

The NID is designed to align the tax treatment of the cost of equity with that of the cost of debt (i.e. dividends are not deductible, whereas interest on financing is a tax-deductible expense) and, therefore, bring equity financing on a par with debt financing. This will be achieved by allowing Malta companies and partnerships (including Malta permanent establishments of foreign companies or partnerships) to claim a deduction for "interest on risk capital." Specifically, such companies will be able to claim a deduction against their chargeable income for notional interest deemed to be incurred on their equity capital.

Main features of the NID

The NID will be optional for companies—it is not required.

The NID will be calculated by multiplying (i) the notional interest rate (i.e. the risk-free rate set by reference to the current yield to maturity on Malta government stocks with a remaining term of approximately 20 years, plus a 5% premium) by (ii) the entity's total equity at its financial year-end. For this purpose, equity is defined as share capital, including any share premium, interest-free debt, positive retained earnings and any other item reported as equity in the entity's financial statements, including contribution reserves.

The NID claimed in any year will be limited to 90% of chargeable income. However, any excess notional interest may be carried forward indefinitely to be deducted against chargeable income in future years.

Where the NID is claimed, the company's shareholder (or partner in the case of a partnership) will be deemed for Malta tax purposes to have received notional interest income in the same amount. Where a shareholder or partner of the undertaking is not resident in Malta, the deemed interest should be exempt from tax in Malta provided certain requirements are met.

Dividend distributions made out of profits relieved from tax through an NID claim will not be chargeable to further tax at the level of the shareholder or partner.

Specific anti-avoidance rules are included to prevent abusive application of the regime.

As noted above, the new NID will apply as from the 2018 year of assessment, meaning that taxpayers will be able to claim the NID on the profits of the fiscal year ending in 2017 (basis year), which are assessable to income tax in 2018 (year of assessment).

Contacts

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