

L.N. 348 of 2019

**INCOME TAX ACT
(CAP. 123)**

**European Union Anti-Tax Avoidance Directives Implementation
(Amendment) Regulations, 2019**

IN EXERCISE of the powers conferred by articles 52B and 96 of the Income Tax Act, hereinafter referred to as "the Act", the Minister for Finance has made the following regulations:-

1. (1) The title of these regulations is European Union Anti-Tax Avoidance Directives Implementation (Amendment) Regulations, 2019 and they shall be read and construed as one with the European Union Anti-Tax Avoidance Directives Implementation Regulations, hereinafter referred to as "the principal regulations".

Citation and commencement.

S.L. 123.187.

(2) These regulations shall come into force as follows:

(a) the provisions of regulations 2, 3, 5 and 7 shall apply with effect from 1 January 2020; and

(b) the provisions of regulation 6 shall apply with effect from 1 January 2022.

2. Regulation 2 of the principal regulations shall be amended as follows:

Amends regulation 2 of the principal regulations.

(a) in sub-regulation (1) thereof, the words "Directive (EU) 2016/1164 of 12 July 2016 adopted by the Council of the European Union laying down rules against tax avoidance practices that directly affect the functioning of the internal market", shall be substituted by the words "Directive (EU) 2016/1164 of 12 July 2016, as amended by Directive (EU) 2017/952 of 29 May 2017, adopted by the Council of the European Union, laying down rules against tax avoidance practices that directly affect the functioning of the internal market"; and

(b) immediately after sub-regulation (2) thereof, there shall be added the following new sub-regulation:

"(3) Regulation 10 shall also apply to all entities that are treated as transparent for tax purposes in terms of the Income Tax Acts."

B 2594

Amends
regulation 3 of
the principal
regulations.

3. Regulation 3 of the principal regulations shall be amended as follows:

(a) in the definition "associated enterprise" thereof, immediately after the words "shall also be regarded as associated enterprises;", there shall be added the following:

"For the purposes of regulations 9 and 10:

(i) where the mismatch outcome arises under paragraph (b), (c), (d), (e) or (g) of the definition of "hybrid mismatch" or where an adjustment is required under regulation 9(3) or regulation 10, the definition "associated enterprise" is modified so that the 25 per cent (25%) requirement is replaced by a 50 per cent (50%) requirement;

(ii) a person who acts together with another person in respect of the voting rights or capital ownership of an entity shall be treated as holding a participation in all of the voting rights or capital ownership of that entity that are held by the other person;

(iii) an associated enterprise also means an entity that is part of the same consolidated group for financial accounting purposes as the taxpayer, an enterprise in which the taxpayer has a significant influence in the management or an enterprise that has a significant influence in the management of the taxpayer;";

(b) immediately after the definition of "borrowing costs" thereof, there shall be added the following new definition:

""consolidated group for financial accounting purposes" means a group consisting of all entities which are fully included in consolidated financial statements drawn up in accordance with the International Financial Reporting Standards or any other financial reporting system as may be determined by means of guidelines issued under article 96(2) of the Act;"; and

(c) immediately after the definition "financial undertaking" thereof, there shall be added the following new definitions:

""hybrid mismatch" means a situation involving a

taxpayer or, with respect to regulation 9(3), an entity, where:

(a) a payment under a financial instrument gives rise to a deduction without inclusion outcome and:

(i) such payment is not included within a reasonable period of time; and

(ii) the mismatch outcome is attributable to differences in the characterisation of the instrument or the payment made under it.

For the purposes of sub-paragraph (i), a payment under a financial instrument shall be treated as included in income within a reasonable period of time where:

(A) the payment is included by the jurisdiction of the payee in a tax period that commences within twelve (12) months of the end of the payer's tax period; or

(B) it is reasonable to expect that the payment will be included by the jurisdiction of the payee in a future tax period and the terms of payment are those that would be expected to be agreed between independent enterprises;

(b) a payment to a hybrid entity gives rise to a deduction without inclusion and that mismatch outcome is the result of differences in the allocation of payments made to the hybrid entity under the laws of the jurisdiction where the hybrid entity is established or registered and the jurisdiction of any person with a participation in that hybrid entity;

(c) a payment to an entity with one (1) or more permanent establishments gives rise to a deduction without inclusion and that mismatch outcome is the result of differences in the allocation of payments between the head office and permanent establishment or between two (2) or more permanent establishments of the same entity under the laws of the jurisdictions where the entity operates;

B 2596

(d) a payment gives rise to a deduction without inclusion as a result of a payment to a disregarded permanent establishment;

(e) a payment by a hybrid entity gives rise to a deduction without inclusion and that mismatch is the result of the fact that the payment is disregarded under the laws of the payee jurisdiction;

(f) a deemed payment between the head office and permanent establishment or between two (2) or more permanent establishments gives rise to a deduction without inclusion and that mismatch is the result of the fact that the payment is disregarded under the laws of the payee jurisdiction; or

(g) a double deduction outcome occurs:

Provided that for the purposes of this definition:

(i) payment representing the underlying return on a transferred financial instrument shall not give rise to a hybrid mismatch under paragraph (a) where the payment is made by a financial trader under an on-market hybrid transfer provided the payer jurisdiction requires the financial trader to include as income all amounts received in relation to the transferred financial instrument;

(ii) a hybrid mismatch shall only arise under paragraphs (e), (f) or (g) to the extent that the payer jurisdiction allows the deduction to be set off against an amount that is not dual-inclusion income;

(iii) a mismatch outcome shall not be treated as a hybrid mismatch unless it arises between associated enterprises, between a taxpayer and an associated enterprise, between the head office and permanent establishment, between two (2) or more permanent establishments of the same entity or under a structured arrangement:

Provided further that for the

purposes of this definition and regulations 9, 10 and 11:

"deduction" means the amount that is treated as deductible from the taxable income under the laws of the payer or investor jurisdiction. The term "deductible" shall be construed accordingly;

"deduction without inclusion" means the deduction of a payment or deemed payment between the head office and permanent establishment or between two (2) or more permanent establishments in any jurisdiction in which that payment or deemed payment is treated as made (payer jurisdiction) without a corresponding inclusion for tax purposes of that payment or deemed payment in the payee jurisdiction. The payee jurisdiction is any jurisdiction where that payment or deemed payment is received, or is treated as being received under the laws of any other jurisdiction;

"disregarded permanent establishment" means any arrangement that is treated as giving rise to a permanent establishment under the laws of the head office jurisdiction and is not treated as giving rise to a permanent establishment under the laws of the other jurisdiction;

"double deduction" means a deduction of the same payment, expenses or losses in the jurisdiction in which the payment has its source, the expenses are incurred or the losses are suffered (payer jurisdiction) and in another jurisdiction (investor jurisdiction). In the case of a payment by a hybrid entity or permanent establishment the payer jurisdiction is the jurisdiction where the hybrid entity or permanent establishment is established or situated;

B 2598

"dual inclusion income" means any item of income that is included under the laws of both jurisdictions where the mismatch outcome has arisen;

"financial instrument" means any instrument to the extent that it gives rise to a financing or equity return that is taxed under the rules for taxing debt, equity or derivatives under the laws of either the payee or payer jurisdictions and includes a hybrid transfer;

"financial trader" is a person or entity engaged in the business of regularly buying and selling financial instruments on its own account for the purposes of making a profit;

"hybrid entity" means any entity or arrangement that is regarded as a taxable entity under the laws of one (1) jurisdiction and whose income or expenditure is treated as income or expenditure of one (1) or more other persons under the laws of another jurisdiction;

"hybrid transfer" means any arrangement to transfer a financial instrument where the underlying return on the transferred financial instrument is treated for tax purposes as derived simultaneously by more than one (1) of the parties to that arrangement;

"inclusion" means the amount that is taken into account in the taxable income under the laws of the payee jurisdiction.

A payment under a financial instrument shall not be treated as included to the extent that the payment qualifies for any tax relief solely due to the way that payment is characterised under the laws of the payee jurisdiction. The term "included" shall be construed

accordingly;

"mismatch outcome" means a double deduction or a deduction without inclusion;

"on-market hybrid transfer" means any hybrid transfer that is entered into by a financial trader in the ordinary course of business, and not as part of a structured arrangement;

"person" means an individual or entity;

"tax relief" means a tax exemption, reduction in the tax rate or any tax credit or refund (other than a credit for taxes withheld at source);

"structured arrangement" means an arrangement involving a hybrid mismatch where the mismatch outcome is priced into the terms of the arrangement or an arrangement that has been designed to produce a hybrid mismatch outcome, unless the taxpayer or an associated enterprise could not reasonably have been expected to be aware of the hybrid mismatch and did not share in the value of the tax benefit resulting from the hybrid mismatch;"

4. Paragraph (b) of sub-regulation (5) of regulation 4 of the principal regulations, shall be substituted by the following:

Amends regulation 4 of the principal regulations.

"(b) all assets and liabilities are valued using the same method as in the consolidated financial statements drawn up in accordance with the International Financial Reporting Standards or any other financial reporting system as may be determined by means of guidelines issued under article 96(2) of the Act."

5. Immediately after regulation 8 of the principal regulations, there shall be added the following new regulations:

Adds new regulations 9, 10 and 11 to the principal regulations.

"Hybrid mismatches.

9. (1) To the extent that a hybrid mismatch results in a double deduction:

(a) the deduction shall be denied if Malta is the investor jurisdiction; and

B 2600

(b) the deduction shall be denied if Malta is the payer jurisdiction and the deduction is not denied in the investor jurisdiction:

Provided that, any such deduction shall be eligible to be set off against dual inclusion income whether arising in a current or subsequent tax period.

(2) To the extent that a hybrid mismatch results in a deduction without inclusion:

(a) the deduction shall be denied if Malta is the payer jurisdiction; and

(b) the amount of the payment that would otherwise give rise to a mismatch outcome shall be included in income if Malta is the payee jurisdiction and the deduction is not denied in the payer jurisdiction.

(3) No deduction shall be allowed for any payment by a taxpayer to the extent that such payment directly or indirectly funds deductible expenditure giving rise to a hybrid mismatch through a transaction or series of transactions between associated enterprises or entered into as part of a structured arrangement except to the extent that one (1) of the jurisdictions involved in the transaction or series of transactions has made an equivalent adjustment in respect of such hybrid mismatch.

(4) There shall be excluded from the scope of application:

(a) paragraph (b) of sub-regulation (2), hybrid mismatches as defined in paragraph (b), (c), (d) or (f) of the definition of "hybrid mismatch" in regulation 3;

(b) paragraphs (a) and (b) of sub-regulation (2), hybrid mismatches resulting from a payment of interest under a financial instrument to an associated enterprise where:

(i) the financial instrument has conversion, bail-in or write down features;

(ii) the financial instrument has been issued with the sole purpose of satisfying loss absorbing capacity requirements applicable to the banking sector and the financial instrument is recognised as such in the taxpayer's loss absorbing capacity requirements;

(iii) the financial instrument has been issued:

(A) in connection with financial instruments with conversion, bail-in or write down features at the level of a parent undertaking;

(B) at a level necessary to satisfy applicable loss absorbing capacity requirements;

(C) not as part of a structured arrangement; and

(iv) the overall net deduction for the consolidated group under the arrangement does not exceed the amount that it would have been had the taxpayer issued such financial instrument directly to the market:

Provided that the provisions of this paragraph (b) shall only apply until 31 December 2022.

(5) To the extent that a hybrid mismatch involves income of a disregarded permanent establishment of a taxpayer resident in Malta which is not otherwise subject to tax in Malta, that taxpayer shall include in its income the income that would otherwise be attributed to the disregarded permanent establishment. This applies unless Malta is required to exempt the income of the permanent establishment in terms of a double taxation treaty entered into by Malta with a third country.

(6) To the extent that a hybrid transfer is designed to produce a relief for tax withheld at source on a payment derived from a transferred financial instrument to more than one (1) of the parties involved, the benefit of such relief shall be limited in proportion to the net taxable income regarding such payment.

B 2602

Reverse hybrid mismatches.

10. (1) Where one (1) or more associated non-resident entities holding in aggregate a direct or indirect interest in fifty per cent (50%) or more of the voting rights, capital interests or rights to a share of profit in a hybrid entity that is incorporated or established in Malta are located in a jurisdiction or jurisdictions that regard the hybrid entity as a taxable person, the hybrid entity shall be regarded as a resident of Malta and taxed on its income to the extent that that income is not otherwise taxed under any other provision of the Income Tax Acts or in any other jurisdiction.

(2) Sub-regulation (1) shall not apply to a collective investment vehicle. For the purposes of this regulation, "collective investment vehicle" means an investment fund or vehicle that is widely held, holds a diversified portfolio of securities and is subject to investor-protection regulation in the country in which it is established.

Tax residency mismatches.

11. To the extent that a deduction for payment, expenses or losses of a taxpayer who is resident for tax purposes in Malta and in another jurisdiction is deductible from the tax base in Malta and in that other jurisdiction, the deduction shall be denied to the extent that the other jurisdiction allows the duplicate deduction to be set off against income that is not dual-inclusion income. If the other jurisdiction is a Member State, the deduction shall be denied only if the taxpayer is not deemed to be resident in Malta according to the double taxation treaty between Malta and the other Member State concerned."