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Doing Business In...

Malta

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WH Partners

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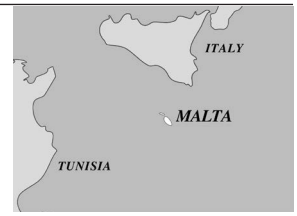
MALTA

Law and Practice



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1. Legal System

1.1 Legal System and Judicial Order

The Maltese legal system is mixed. For many centuries it was based on Roman law as codified by the Emperor Justinian, with the civilian influence being further strengthened during the rule of the Order of St John, which resulted in a predominantly civil law system. Years of British rule introduced several significant legal institutions derived from the English legal system, such as trial by jury, the rules of evidence and the structure of the courts. In time and over the centuries Malta's legal system therefore evolved into a predominantly a civil law system predominantly, incorporating some elements from the common law traditions.

The judicial order is organised into a Constitutional Court, which has limited competence, a Court of Appeal that is competent for all jurisdictions, and first instance civil and criminal inferior and superior courts. There are, in addition, several administrative tribunals, from which an appeal can be made to the inferior Court of Appeal.

2. Restrictions to Foreign Investments

2.1 Approval of Foreign Investments

Malta seeks to attract foreign direct investment by implementing incentives' legislation across a number of economic sectors. Exchange controls were abolished on Malta's joining the EU. There is no requirement for foreign investments to be approved by authorities. A specific approval framework exists with regard to the purchase of real estate in Malta by non-residents.

2.2 Procedure and Sanctions in the Event of Non-compliance

See **2.1 Approval of Foreign Investments**.

2.3 Commitments Required from Foreign Investors

See **2.1 Approval of Foreign Investments**.

2.4 Right to Appeal

See **2.1 Approval of Foreign Investments**.

3. Corporate Vehicles

3.1 Most Common Forms of Legal Entities

The most common type of corporate vehicle in Malta is the limited liability company, which may be private or public. Other forms of corporate vehicles available under the Maltese legal system include a general partnership ("*partnership en nom collectif*"), a limited partnership ("*partnership en commandite*"), which may have its capital divided into shares), a civil partnership, a foundation and the association. Joint ventures are recognised but are not usually required to be registered and do not have distinct legal personality. Whereas limited companies are frequently used in business and trading, foundations and associations are frequently encountered in connection with charitable or social setups. Partnerships are more common among smaller or more traditional businesses.

Liability of shareholder in both forms of limited liability company is limited up to their shareholding. A private limited company can have a single member and single director, provided the company is an exempt company. There is a 50-shareholder limit for private companies, and transfers of shares in such companies must be restricted. If the number of members in a company exceeds 50, it must convert to a public company. The minimum share capital for a private company is EUR1,165.69, paid up at least 20% on incorporation; whereas for a public company it is EUR46,597.47, at least 25% paid up.

3.2 Incorporation Process

The steps involved in incorporation vary depending mainly on the type of an entity being incorporated. A company is formed upon subscription by shareholders to a memorandum and articles of association, and their delivery to the Malta Business Registry together with key ancillary documents, that include evidence of paid up minimum share capital and compliance documentation. Once delivered to the Malta Business Registry, the incorporation can be complete in around one working day.

Other forms of corporation, such as a foundation, are set up either by means of a public deed or through a last will, in each case published in Malta and executed before a notary public.

3.3 Ongoing Reporting and Disclosure Obligations

Private companies are subject to at least annual reporting obligations to the Malta Business Registry, consisting of annual returns and annual financial statements, which unless a company is registered as a private exempt company, must be audited. Other corporate changes, such as changes to directors and officers, changes to shareholding and to ultimate beneficial ownership, amendments to the Company's Memorandum and Articles of Association and other significant corporate events are also subject to disclosure to the Malta Business Registry within applicable timeframes. Where a company is subject to licensing and regulation, it is subject to additional reporting and disclosure obligations to the relevant licensing body or authority.

3.4 Management Structures

The board of directors of a company is charged with its management and administration. Members of the board of directors are

usually appointed by the shareholders of a company, and the appointed directors are required to be stated in the company's Memorandum and Articles of Association. Although the concept is not recognised under the Companies Act, directors may be appointed in an executive or non-executive role in practice.

In certain cases, the Maltese legal system also recognises shadow directors: these are persons who, although not appointed to the board, act as though they were directors, and liability qua directors may attach to such persons. Two-tier management structures are not formally recognised under the Companies Act, however a board is free to regulate its procedure and may create a de facto two-tier management structure composed of committees that report to the board.

3.5 Directors', Officers' and Shareholders' Liability

Directors are generally jointly and severally liable with respect to any liability arising from acts or omissions by any member of the board. However, where a particular duty has been delegated to one or more directors, only such directors are liable in damages. Since Maltese corporate law has its roots in English company law, it also borrows the concept of "piercing the corporate veil", although this is applicable in very limited circumstances, such as upon a finding of fraudulent or wrongful trading, or in the event of an unlawful distribution to a member in breach of the Companies Act, where at the time of the distribution, the member knows or has reasonable grounds for believing that it is made in contravention of the Companies Act.

4. Employment Law

4.1 Nature of Applicable Regulations

The legal situation under Maltese law in relation to employment is principally regulated by the Employment and Industrial Relations Act (EIRA) under which a number of subsidiary laws provide sectoral or national norms. Furthermore, with respect to established conditions of employment the law prescribes individual contracts (for an indefinite or definite duration), which is the most commonly used form; as well as collective contracts of employment in the form of industrial agreements. Industrial agreements have the force of law between the parties. In the case where a contract of service is not entered into in writing, the provisions of the EIRA serve as the conditions of such a contract.

4.2 Characteristics of Employment Contracts

The EIRA establishes the minimum conditions of employment which should be included in every employment contract, namely: wages, the period of employment, the hours of work and leave and any other conditions related to the employment, including any benefits, terms of engagement, terms of work participation, manner of termination and the mode of settling and differences which may arise between the parties to the agreement.

Although the law stipulates what the minimum conditions of employment are, other conditions not in breach of the law may be negotiated. If a negotiated condition is less advantageous to the employee than those set out in the EIRA, the less advantageous condition shall not apply and shall be replaced ipso jure with the condition laid down in the EIRA. This comes to show that the EIRA is catered to protect employees and therefore in such a case, the fundamental principle of pacta sunt servanda established under the Maltese law of contract shall not apply in the case of less favourable conditions.

Once the employee engages with the employer, the latter is to explain to the employee the provisions of the conditions of employment and shall deliver to the latter a written statement about the prescribed conditions by not later than eight working days from the start of employment.

4.3 Working Time

Under the Information to Employees Regulations (Subsidiary Legislation 452.83) the employer must inform the employee of the normal rates of wages payable and the normal hours of work within eight working days from the commencement of employment. The contract of employment may, in addition, provide for the allowance payable in respect of hours worked in excess of the normal hours of work.

An employer may only oblige an employee to work overtime where the employee has consented to in writing, and where the total hours of week's work, including overtime, does not exceed 48 hours (48 hours being the maximum stipulated under the Organisation of Working Time Regulations (Subsidiary Legislation 452.87)). In terms of the Protection of Maternity (Employment) Regulations (Subsidiary Legislation 452.91) employees shall not be obliged to work overtime during pregnancy and for a period of 12 months from the date of birth or effective date of adoption.

Various Wage Regulation Orders (WRO) set out the minimum overtime rates of particular industries. If the industry in which the employee works is not covered by the WRO, then an employee shall be paid one and a half times the normal rate for work carried out in excess of a 40-hour week averaged over a four-week period or over shift cycle. Part-time workers are not entitled to overtime payment unless they work over 40 hours per week.

Under the Overtime Regulations (Subsidiary Legislation 452.110), the employer may choose to implement schemes to

bank hours whereby 376 normal annual working hours in each calendar year are "banked", which thus allows extra hours over and above the normal weekly working hours to be worked during periods of higher work activity, and then compensated during periods of lower activity by having working hours below the normal weekly working hours. However, the rule of the average weekly working time including overtime not exceeding 48 hours should be adhered to nonetheless.

4.4 Termination of Employment Contracts

Probationary Period

The first six months of any employment (whether for a fixed or indefinite term) is a probationary period, unless the parties agreed to a shorter probationary period or, in the case of employees holding technical, executive, administrative or managerial posts, to a longer probationary period.

During the probationary period, either party may terminate employment without the need to assign a reason for termination. However, if the employee has been in employment for more than one month, the party terminating the contract must give a week's written notice of termination to the other party.

Once the probationary period lapses, an employee may terminate an indefinite contract of service for any reason by giving the employer a notice of termination, and the notice period under EIRA depends on the continuous length of employment. The employer may choose to terminate an indefinite contract solely on grounds of redundancy and the employee shall be entitled to re-employment if the formerly occupied post becomes available again within one year from the date of termination of employment. Both parties are dispensed from giving notice and may proceed with immediate termination where the reason for the termination of employment amounts to a "good and sufficient cause".

Fixed Term Contracts, Benefits and Injury

In the case of termination of fixed term contracts after the probation period has lapsed, the parties are expected to perform the contract for its entire duration. If there is no justified reason to terminate employment prior to the agreed expiry date, the party terminating shall be liable to pay the other party a sum equal to one-half of the full wages that would have accrued had the contract of employment remained in force.

Where an employee is entitled to the benefits of maternity regulations any such employee may not be dismissed nor receive notice from the employer. Similarly, any employee who is injured in the course of their employment may not be dismissed from work before the lapse of one year from the accident.

Collective Redundancies

The Collective Redundancies (Protection of Employment) Regulations (Subsiuary Legislation 452.80) define collective redundancies as termination of employment by an employer on grounds of redundancy over a period of 30 days of:

- 10 or more employees in establishments normally employing 20 to 99 employees;
- 10% or more of the number of employees in establishments employing 100 to 299 employees; and
- 30 or more in establishments employing 300 employees or above.

An employer who declares a collective redundancy shall not terminate the employment of the effected employees unless the employees' representative as well as the Director of the Department of Industrial and Employment Relations (Director) are notified in writing.

In doing so, the employer must provide the employees' representative with the opportunity to consult with the employer, which consultation period shall commence within seven working days from the day on which the employees' representative has been notified of the intended collective redundancies. During the seven working day period, the employer shall also provide the employees' representatives with certain information, including the reasons for the redundancy, the number of employees affected, the proposed criteria for the selection of the employees to be made redundant, the period over which the layoffs will be effected and details on the redundancy payments due.

The primary purpose of the consultation period is to discuss and find means of avoiding the collective redundancies, or if impossible to do so, to reduce the number of employees affected and to ensure that any consequences linked to the collective redundancies are mitigated.

Notice of Termination

The notice of termination of employment may start to run from the date of the consultation period. However, termination of employment of any projected collective redundancies notified to the Director shall only take effect on the lapse of 30 days after the employer makes such notification. The employer may be granted a shorted or longer period at the Director's discretion.

Any employer who does not abide by the collective redundancy process shall be guilty of an offence and liable to a fine for every employee that is declared redundant.

In the eventuality that an undertaking or business is transferred, the employment contracts of workers affected by such transfer

are to be preserved and respected by the business or undertaking taking over, in whole or in part, from the previous employer.

4.5 Employee Representations

Consultation and information are compulsory in specific areas, such as the applicable conditions of employment and disciplinary rules. Representation is indispensable in collective bargaining as well as in circumstances giving rise to collective redundancies and transfer of undertakings.

An employee has a right to join a trade union and equally to choose not to do so. Therefore, employee representation must be seen in the context of freedom of association of employees and is regulated by specific norms in the Recognition of Trade Unions Regulations (Subsidiary Legislation 452.112).

The appointment of an employee representative is a requirement in cases of collective redundancies and transfer of businesses or undertakings, for those businesses or undertakings employing at least 50 employees. In those cases where there exists no recognised union, the non-unionised employees may select from amongst themselves a representative elected by means of a secret ballot called by the employer. However, if the previously non-unionised employees become represented by a recognised trade union, the term of office of the elected employee representative shall be automatically terminated on the date of the granting of recognition of the respective category of employees to the trade union by the employer.

Procedure When a Ballot is Called

When a ballot is called by the employer for the election of an employee representative, the employer must not only ensure that the ballot procedure is fair but must also supply the Director General responsible for Employment and Industrial Relations with the election process at least one month before the projected date of the ballot. Employees who have passed their probationary period shall be entitled to stand as candidates in the ballot. The appointed representative shall not hold office for more than a period of three years from the date of appointment.

Once an employee representative is appointed, the employer is obliged to inform the employees in writing of the identity of the employee representative and shall hold an information and consultation meeting within two months from the date of appointment. At least one meeting must be held every six months after the date of each preceding meeting. An employer must provide information to the trade union and/or employee representative(s) on:

- The development of the undertaking's activities and economic situation;
- The situation, structure and probable development of employment within the undertaking including any anticipatory measures envisaged where there is a threat to employment; and
- Decisions likely to lead to substantial changes in the work organisation or contractual relations.

Ultimately, an employee representative or trade union is there to protect employees and their rights and interests and to interfere, where necessary, in the relationship between the employer and the employees. It is imperative for employers subject to compulsory election of employee representative to ensure that employees can effectively exercise their right to information and consultation.

5. Tax Law

5.1 Taxes Applicable to Employees/Employers

Income Tax

Employees are subject to tax in Malta where the income earning activity is performed in Malta (source state), irrespective of their nationality, domicile and residence. Where the employees are either resident in Malta or domiciled in Malta, but not both resident and domiciled in Malta, tax would be due on employment income generated in Malta and where applicable on foreign sourced employment income remitted to Malta. Malta resident and domiciled employees are subject to tax on their world-wide employment income irrespective if it is remitted to Malta.

Employees and other work permit holders, individuals working in Malta on short term engagements (ie, holding a work permit for up to six months) and holders of a temporary visa who are either retired or based temporarily in Malta and working abroad are considered as expatriates in Malta and are subject to tax on any employment income arising in Malta, subject to double taxation treaty relief.

Tax on employment income is levied at progressive rates, starting from 0% to 35% (unless benefitting from a special tax program in Malta in which case a 15% flat rate may apply). It varies depending on the gross chargeable income of the employees and their status, whether they are married, single, a parent, a resident or a non-resident. Tax payments are mainly affected through the Final Settlement System (FSS), where the employer withholds the tax at source.

Benefits

Under Maltese legislation employment income includes fringe benefits, bonuses, gifts and other gains or profits provided in the context of employee – employer relationship. These, therefore, are to be taken into account when calculating the gross

amount for tax purposes. It is important to highlight that certain fringe benefits like for instance share options and share award schemes are deemed distinct and separate from the employees' other income, and while tax on the gains is deducted at source the tax rate may vary from the progressive one. In the case of share options and share award schemes, tax is charged at a flat rate of 15% on the taxable value.

Additionally, employees who are ordinarily residents but non-domiciled, and who are not benefitting from a special tax status under a Malta tax programme are subject to a minimum tax of EUR5,000 per annum where the foreign income exceeds EUR35,000 and is not received or not fully received in Malta.

Social Security
Both the employee and the employer have the obligation to make weekly social contributions. These are split equally between the employer and the employee. Depending on the conditions of the employment and the type of person employed, whether the employment is part-time or full-time, social contributions will vary between EUR6.62 to EUR46.53 weekly.

There are also maternity fund contributions that the employer is obliged to pay.

Maternity fund contributions
Private sector employers are obliged to pay a monthly contribution to the maternity fund through the FSS system for each employee. The amount of contribution to be paid depends on the category under which the employee falls and ranges from EUR0.20 to EUR1.44 weekly for basis year 2020.

5.2 Taxes Applicable to Businesses

Corporate Income Tax
Companies which are incorporated in Malta are automatically considered as ordinarily resident and domiciled in Malta and therefore liable to corporate income tax their worldwide income at a standard rate of 35%. Foreign companies may also be subject to tax in Malta upon migrating their tax residency to Malta or if they have a place of business in Malta as per the Double Tax Treaties.

Malta operates a full imputation system of taxation, whereby when dividends are distributed to shareholders out of the taxed profits of the company, the dividends carry an imputation credit of the tax paid by the company on the profits so distributed.

Upon receipt of the dividends, the shareholders may claim a refund of the tax paid at the level of the Malta company. The refund depends on the type of income of the Malta company, with the most common being that of six sevenths, which brings the effective tax rate down to 5% upon certain conditions being satisfied. Other refunds are the five sevenths refunds and the two thirds refund.

Withholding tax
Dividends
Distributions of dividends by a Malta company are exempt from withholding taxes in Malta. The general rule is subject to an exception where the dividends represent a distribution of untaxed income and it is paid to shareholders who are either Maltese resident individuals or non-resident persons (including companies) who are directly or indirectly owned and controlled by, or act on behalf of, a Maltese domiciled and ordinarily resident individual. Such withholding tax would be of 15%.

Interest and Royalties
No withholding tax is due on payment of interests or royalties by a Malta company provided that the recipients are not directly or indirectly owned and controlled by, or acts on behalf of, a Maltese domiciled and ordinarily resident individual and do not carry trade or business through a permanent establishment in Malta which the interest or royalty income is effectively connected to.

Other withholding tax
Maltese financial institutions are under obligation to withhold 15% of the income derived from interest to resident individuals. For investment income of collective investment schemes, the withholding tax is set in the range of 10% to 15% where the payees are resident in Malta for tax purposes.

Value Added Tax (VAT)
The standard VAT rate in Malta on taxable supplies is 18%. However, a reduced rate applies on certain goods or services. For instance, a 7% rate applies on holiday accommodations and use of sport facilities, while a 5% rate applies on essentials like electricity, printing materials and medical accessories. Maltese VAT law also provides for an exhaustive list of supplies which are zero rated, including food for human consumption and pharmaceutical produces. Other supplies are exempt from VAT like for instance letting of immovable property (not being holiday accommodations).

Available tax credits/incentives
What are the main tax credits and tax incentives offered in your jurisdiction? (Describe the applicable regimes, who can benefit and the criteria/requirements.)

5.3 Available Tax Credits/Incentives

Malta operates a vast number of tax incentives, which are updated and renewed from time to time as well as regimes that make it a compelling jurisdiction to set up and conduct business in. Malta has regimes that encourage the opening of new business-

es as well as support existing ones. Examples of tax incentives operating in Malta are detailed below.

Research &Development (R&D) Tax Credit Schemes

Aid for research and development projects

Companies may claim qualifying expenditures associated with research and development as tax credits to offset their income tax liabilities. The eligible R&D projects must seek to achieve advance in science or technology. It is not a requirement for the R&D to actually be successful to be able to claim the expenditures.

The standard tax credit is set at 25% of the eligible expenses which is increased to 30% if the beneficiary is a medium enterprise and to 45% for small enterprises. The total support awarded is capped at EUR15 million per project.

Research and Development Scheme:

To benefit, companies must be engage in "industrial research and experimental development" the end result of which is development of innovative products or solutions. This scheme offers up to EUR500,000 yearly in cash grants and tax credits depending on the size of the undertaking and whether the project is worked on in collaboration with other undertakings.

Tax Credits for R&D and Innovation Scheme:

The third scheme is related to costs associated with hiring highly qualified persons. Undertakings that have experimental development activities and which employ persons that hold doctoral degree in science, IT or engineering may benefit from EUR10,000 tax credit. The maximum aid that an undertaking may benefit from is capped at EUR200,000 over any period of three consecutive years.

Innovation Tax Credits for SMEs

Small to Medium Enterprises that conduct or intend to conduct experimental development activities may recover part of the costs of secondments of highly qualified personnel as tax credits. This incentive is meant to encourage small R&D companies to loan professionals from bigger corporations or organisations like universities, institutes, think tanks, etc, and to use them for R&D purposes.

Highly qualified staff are defined as persons with tertiary education degree and certain minimum years of experience in the field.

The qualifying undertakings may benefit from tax credits in amount of a maximum of 50% of the costs incurred for the secondment of these highly qualified staff.

Investment Aid Tax Credits

This is a comprehensive tax credit incentive regime which aims to help establish, expand and develop businesses.

Small to medium enterprises and (in certain circumstance) large enterprises, may benefit from tax credits as the percentage of qualified expenditures in qualified economic activities. Qualified economic activities, to name just a few, include manufacturing, repair, maintenance, software, R&D, pharmaceuticals, provision of education, healthcare, hotel services and cultural activities.

Qualifying expenditure covers both tangible assets (expenditures on land, buildings, plant, machinery and equipment) and intangible assets (expenditures for patents, know-how, and other types of intellectual property). The percentage of expenditures which the undertakings can benefit from as tax credits depends on the size of the beneficiary undertaking with small undertakings benefiting from up to 30% of qualified expenditures, 20% for medium undertakings, and 10% for large undertakings.

Business Development Tax Credits Scheme

The aim of this scheme is to support businesses that are establishing their base of operations in Malta, or to help existing businesses to expand or to restructure their operations. Tax credits based on the percentage of the qualified costs are the usual aid measure, but at the discretion of the Maltese authorities, direct cash grants may also be available.

Companies which work in manufacturing, R&D, international market services, waste management, industrial solutions or aircraft maintenance may benefit from up to EUR200,000 over any period of three consecutive years.

The eligible costs that are covered by the scheme include: payroll, relocation, rent, services provided to the business, licensing, and utilities.

Malta also operates a separate scheme which helps undertakings with their business consulting expenses. Businesses that are looking to hire consults because they want to expand their activities or cover a new market sectors may apply and benefit from a €500 voucher as well as tax credit of maximum of EUR2,000 depending on the costs.

Patent Box Regime

Malta has a special tax scheme which is a system of tax deductions for qualifying intellectual property expenditures. In essence, a taxpayer is entitled to a tax deduction which is calculated by considering the income which is derived from intel-

lectual property and the expenditures incurred for developing the said intellectual property.

Skills Development Tax Credits
Malta encourages employers to invest into the personal development of their employees using a special tax incentive programme. Companies that invest into their employees training are able to benefit from a set of tax credits which are based on percentage of the costs that the taxpayers have incurred when providing training or education to their employees. The maximum tax credit allowed per undertaking is EUR1 million.

On the other hand, there is also a scheme for individuals called 'Get Qualified' which provides those following educational, vocational or training courses that lead to certification or diploma with a tax credit on their personal income tax. Thus, individuals who are paying out of their pocket can still recoup some of the costs.

Personal Income Tax Incentives for Highly Qualified Employees
One of the goals of Maltese fiscal policy is to bring and retain foreign talent in certain specific industries, ie, Aviation, Financial Services and Assisted Reproductive Technology and Gaming. One of the incentive programmes that Malta operates for this purpose is easement of income tax liability for certain highly sought-after workers that cannot be found other than through hiring from abroad. Non-domiciled persons who are employed by Maltese companies and who have positions in R&D, development, analytics or innovation or who are managers in these sectors are able to enjoy a reduced income tax rate of 15% for up to five consecutive years for EU/EEA individuals and up to four consecutive years for non-EU/EEA individuals, and which can, upon application, be extended.

Product Certification Tax Credits
Companies that are trying to improve existing products or develop new ones may benefit from tax credits computed on part of the expenses associated with product certification or licensing. The maximum tax credit is of EUR25,000 per certification.

Double Taxation Treaties
Malta is well-known for its highly attractive refund system that allows effective utilisation of capital and reduction of tax burden on holding companies. Additionally, Malta has over 70 double taxation treaties with the majority of developed jurisdictions.

Tax Refund System
See **5.2 Taxes Applicable to Business**.

Participation Exemption
Maltese holding companies who have equity holding of 5% or more in either local or foreign companies may benefit from what is known as the participation exemption. This regime allows the Malta holding company to benefit from an exemption on capital gains and income tax liabilities when receiving dividends from the said equity holding, provided that certain conditions are met.

5.4 Tax Consolidation

Malta has recently introduced tax consolidation rules which are applicable as of year of assessment 2020.

Under these rules group of companies can elect to be treated as a single fiscal tax unit with the principal taxpayer being the holding company. Both subsidiaries resident in Malta and outside can form part of the tax unit. Only subsidiaries in which the parent company holds at least 95% of the shares will be eligible to form part of the fiscal unit.

All the entities in the group must have the same financial year dates. Additionally, the holding company must be either incorporated in Malta, be resident in Malta, or perform some activities in Malta. It can also be a Maltese trust or foundation if it has elected to be treated as a company for the purposes of income tax.

The fiscal unit will benefit from a streamlined and simplified income tax determination and will be able to use the refund system. In addition, the reduced income tax rate stemming from the refund system is allowed even if some of the members of the fiscal unit are not distributing profits. The lower effective tax rate will be applicable immediately, hence resulting in better cash flow for the group, as the holding company will not have to wait for tax refunds.

Tax Paying Responsibilities
The principal taxpayer will be the one responsible for income tax and thus all the income and gains of the members of the fiscal unit will be allocated to the principal taxpayer. Consequently, all the deductions, tax credits, refunds, etc, will also be allocated to the principal taxpayer. This also includes any rights claimed under the double taxation treaties for the subsidiaries located outside Malta.

The principal taxpayer will also onboard all the income tax rights and obligations of the other members of the fiscal unit. Hence it will be the only one required to file income tax returns reducing compliance costs.

In 2018 Malta also introduced VAT Grouping for Financial Services and Gambling Industries where companies forming

a group of companies may be considered as one fiscal unit for VAT purposes.

5.5 Thin Capitalisation Rules and Other Limitations

The Maltese legislation does not contain provisions regarding Thin Capitalisation rules.

In terms of Income Tax Act, expenses are only allowed as deductions against chargeable income if such expenses are incurred wholly and exclusively in the production of the income. Accordingly, interest paid by a person on any borrowed money may be deducted as an expense against chargeable income as long as the amount borrowed by a person is used in its business activities to generate trading income.

Through the transposition of the EU Anti-Tax Avoidance Directive in 2018, Malta introduced new Interest Limitation rules, which entered into force in January 2019. The new Interest Limitation rules implemented the maximum limitation on the amount of deductions that a company can claim in relation to borrowing costs: either 30% of the taxpayer's earnings before interest, taxes, depreciation, and amortisation (EBITDA) or EUR3 million, whichever is higher.

Exemptions

Exemptions apply to the above-mentioned limitations of 30% where taxpayers are allowed to deduct exceeding borrowing costs up to EUR3 million. Standalone entities may fully deduct exceeding borrowing costs when they are not part of a consolidated group for financial accounting purposes and have no associated enterprises or permanent establishment; as well as members of a consolidated group, when the taxpayer can demonstrate that the ratio of its equity over its total assets is equal to or higher than the equivalent ratio of the group.

Borrowing costs are described as interest expenses on all forms of debt, payments under profit participating loans, imputed interest, finance cost element of finance lease payments and other costs economically equivalent to interests.

Taxpayers may also carry forward exceeding borrowing costs without time limitation; and carry forward unused interests for a maximum period of five years.

5.6 Transfer Pricing

The Maltese legislation does not contain provisions regarding Transfer Pricing rules. However, mentions of the arm's length principle can be found in the Income tax legislation.

Income Tax Act provides that income derived by a Maltese company and attributable to a permanent establishment outside of Malta shall be calculated in accordance with the arm's length principle. The Act also provides that any artificial or fictitious scheme with the purposes to reduce the amount of tax due by the taxpayer shall be cancelled or modified by the Commissioner in order to eliminate the tax advantage obtained.

The provisions present in the Income Tax Management Act refer to the situation where a non-resident person carries on business with a resident person and the transactions are not made in accordance with the arm's length principle, producing a different amount of profit for the non-resident person. In these situations, the Commissioner for Revenue will impose taxation based on the ordinary profits which might be expected to arise from the business.

Patent Box Regime

In 2019 Malta announced a Patent Box regime and references are made to the Transfer Pricing method in order to determine the income or gains, providing that the Transfer Pricing method, in terms of the OECD's Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations are to be used.

Reference to the arm's length principle is also made in many of the Double Tax Treaties entered into by Malta with other countries, which often includes in the provisions on associated enterprises that both countries that are parties to the treaty have the right to adjust the amount of the tax charged in transactions involving related parties, when the profits are different from those which would be made between independent enterprises.

5.7 Anti-evasion Rules

A general anti-abuse provision exists under the Income Tax Act which disregards any artificial or non-genuine schemes which aim is to obtain a tax advantage by avoiding, reducing, or postponing the tax liability of the taxpayer.

The Income Tax Act also provides for anti-tax avoidance provisions with respect to the participation exemption regime, whereby dividends received from a foreign entity, would fall with the exemption only if the foreign entity is resident or incorporated in an EU Member State, if it is subject to foreign tax of at least 15% or if it does not derive more than 50% of its income from passive interest or royalties.

Where none of the conditions mentioned are satisfied, the exemption would apply only if the equity holding in the foreign entity is not a portfolio investment and the foreign entity or its passive interest or royalties are subject to at least 5% foreign tax. Other general anti-abuse provisions are found in the EU ATAD Directive as implemented in Malta.

CFC Rules
Through the EU ATAD Directive, Malta introduced controlled foreign company (CFC) rules, providing that where an entity or a permanent establishment does not have its profits subject to tax or are exempt from tax, it shall be treated as CFC if the taxpayer holds, directly or indirectly, more than 50% of the voting rights, or 50% of capital or is entitled to receive more than 50% of the profits; and the corporate tax paid on its profits by the entity or the permanent establishment is lower than the difference between the tax that would have been charged on the entity or permanent establishment under the Income Tax Act and the tax paid on its profits by the entity or permanent establishment.

An entity or a permanent establishment considered as a CFC shall have its non-distributed income included in the tax base of the Maltese company, when an arrangement or a series of arrangements are considered non-genuine. Some exemptions may be applied.

Exit Taxes
Exit taxes were also introduced in Malta and the taxpayer may be subject to tax on capital gains when assets are transferred:

- from the head office or permanent establishment in Malta to another permanent establishment in the EU Member State or a third country and where Malta no longer has the right to tax capital gains from the transfer of such assets due to be transferred;
- when a taxpayer transfers its tax residence from Malta to another EU Member State or third country and the assets do not remain effectively connected with a permanent establishment in Malta; or
- where the business carried from Malta through a permanent establishment is transferred to another EU Member State or to a third country and Malta has no right to tax capital gains from the transfer of such assets.

Additionally, the Multilateral Convention to Implement Tax Treaty Related to Measures to Prevent BEPS came into force in Malta on April 2019, with the main purpose to modify double tax treaties and establish measures to combat tax avoidance. The changes made by the Multilateral Instrument, to be applied, need to consider when the instrument came into force for both states part in the double tax treaty.

6. Competition Law

6.1 Merger Control Notification

Mergers and acquisitions become subject to notification in Malta when they qualify as a "concentration" and when the two turnover thresholds set out in applicable regulations are met. A concentration encompasses the following transactions:

- mergers between two or more previously independent undertakings;
- the acquisition by one or more undertakings of direct or indirect control of the whole or part of one or more other undertakings;
- full-function joint ventures.

A concentration must meet the "control" criterion. This is met where the concentration leads to a lasting change of control, or where rights or contracts confer decisive influence on composition, voting or decisions of the organs of an undertaking.

Once the presence of a concentration is established, this is notifiable to the competition authorities where, in the preceding financial year, the aggregate turnover in Malta of the undertakings concerned exceeded EUR2.3 million, and each of the undertakings concerned had a turnover in Malta equivalent to at least 10% of the combined aggregate turnover.

6.2 Merger Control Procedure

The Office for Competition in Malta, being the competent body for competition law in Malta, invites parties who believe a transaction might be subject to notification to pre-notification meetings at the outset. Such meetings are not mandatory, but usually helpful to determine the nature and quality of data available and required. The notification process is mandatory, and must be notified within 15 working days of conclusion of the agreement, announcement of the public bid or acquisition of a controlling interest.

The notification form largely corresponds to European Commission Form CO. Its form is annexed to the relevant regulations. Unless a notification qualifies for the simplified, shorter procedure, a Phase I decision must be issued within six weeks, unless the authority has made a request for information or for submission of remedies. If, following the end of the Phase I period, a decision is taken to launch Phase II proceedings, such a decision must be reached within four months of the initiation of the investigation.

6.3 Cartels

There are rules to govern anti-competitive agreements and practices under the Competition Act (Chapter 379 of the laws of Malta). To a large extent, these reproduce the rules found in Articles 101 and 102 of the Treaty on the Functioning of the European Union (TFEU), with applicability to anti-competitive agreements and practices which have an effect on Maltese markets. Such agreements and practices are prohibited where they

have the object or effect of preventing, restricting or distorting competition within Malta or any part of Malta.

In broad terms, the prohibition covers the most serious infringements, such as cartels, as well as other forms of horizontal co-operation, such as joint production, R&D, purchasing or commercialisation agreements. The framework allows for the applicability of block exemptions, where these have been prescribed by the Minister responsible for Competition or by the European Commission. Both public and private enforcement of cartel infringements is possible in Malta.

6.4 Abuse of Dominant Position

The Competition Act prohibits the abuse by one or more undertakings of a dominant position, which includes price exploitation and price discrimination. The rules apply to conduct which has an effect in Malta. A relevant product or geographic market share in excess of 40% is usually indicative of dominance, although the assessment depends on a range of factors of competitive conditions, in addition to market shares.

Where the activity concerns trade between Malta and any one or more EU Member States, then that activity is also subject to the provisions of Article 102 of the TFEU.

7. Intellectual Property

7.1 Patents

As provided in the Patents and Designs Act (Chapter 417 of the Laws of Malta), inventions are patentable in Malta if they are novel which does not form part of prior art (everything which is already available to the public), involve an inventive step, and are susceptible to industrial applications (the invention can be made or used in any kind of industry).

Biological inventions may also be patentable, subject to certain ethical and moral exceptions. Discoveries, scientific theories, mathematical methods, aesthetic creations, programs for computers and presentations of information re not regarded as patentable inventions.

A patent becomes protected once it is registered at a patent registry. An application for registration of a patent must be filed at the Office of the Comptroller of Industrial Property and shall be accompanied by the prescribed documents.

The term of a patent is 20 years from the filing date. The right to a patent belongs to the inventor or their successor in title. Where the application for a patent is made by two or more persons jointly, a patent may be granted to them jointly and they will have equal rights unless otherwise agreed between them.

Any right-holder shall have the right to prevent third parties from performing without authorising the following acts:

- The making of a product or the use of a process incorporating the subject-matter of the patent.
- The offering or the putting on the market of a product incorporating the subject-matter of the patent, the use of such product, or the importation or stocking of such product for such offering or putting on the market or for such use.
- The inducing of third parties to perform any of the above acts.

Applications for Damages

Any application to sue for damages shall be made within five years from the date when the injured party has obtained knowledge of the infringement and the application shall be filed before the Patents Tribunal which has the power to order the infringing party to deliver to the right-holder articles and apparatus which are deemed to be in contravention of the patent.

As per Cap.488 Enforcement of Intellectual Property Rights (Regulation) Act, the First Hall of Civil Court (FHCC) of Malta may, on an application filed by the injured right-holder, order the infringer to pay the rights holder damages commensurate with the actual prejudice suffered as a result of the infringement. Such damages are inclusive of lost profits, damages relating to unfair profits made by the infringer as well as damages based on moral prejudice caused to the right holder. Alternatively, the FHCC may award a lump sum of damages which would include at least the amount of royalties and fees which would have been due had the infringer requested authorisation to use the intellectual property in question.

In addition to such damages the Court may upon the plaintiff's application issue an injunction against the infringer aimed at prohibiting the continuation of the infringement. Where the infringer unknowingly engaged in infringing activities, the FHCC shall order the recovery of profits or the payment of damages. Furthermore, the FHCC may order the taking of the following corrective measures:

- recall and remove from circulation within commercial channels; or
- order the destruction of items/materials (where applicable) that are found to be infringing or were used for the creation of infringing items/materials.

7.2 Trade Marks

Trade marks under the Malta Trademarks Act ("TM act") are defined as marks which consist of any signs, in particular words, including personal names, or designs, letters, numerals, colours, the shape of goods or of the packaging of goods, or sounds,

provided that any such signs are capable of distinguishing the goods or services of one undertaking from those of other undertakings. As well as being represented on the register in a manner which enables the competent authorities and the public to determine the clear and precise subject matter of the protection afforded to its proprietor.

Registered trade marks are protected for a period of ten years from the date of filing. Once submitted the application shall be examined by the Maltese Industrial Property Office (IPO) In case the mark and the application meet the requirements of the TM Act the mark is registered.

An infringement of a trade mark is actionable by the proprietor of the trade mark. Remedies claimable by injured rights holders shall be those as stated in Cap 488, and as briefly elaborated in **7.1 Patents**. The proprietor of an existing trade mark is entitled to exercise their rights arising out of the registered trade mark by filing a notice of opposition to the registration of any trade marks on the basis of a similarity of part or the totality of the mark itself as well as the similarity of part or the totality of goods or services. Oppositions can be lodged within a five-year period following the date of completion of the registration procedure.

7.3 Industrial Design

Design means the appearance of the whole or a part of a product resulting from the features of, in particular, lines, contours, colours, shape, texture and/or materials of the product itself, and/or its ornamentation. Designs are classified for registration according to the Locarno Agreement (1968) which establishes an international classification for industrial designs used for the purposes of the registration of industrial designs.

A registered design is a property right obtained by the registration of the design under the Patents and Designs Act (Chapter 417 of the Laws of Malta). A design is protected by a design right if the design in question is novel (no identical design has been made available to the public prior to the filing date) and has individual character (the overall impression it produces on the user differs from any overall impression of a design which has already been made available to the public). An application for registration of a design must be filed with the Comptroller of Industrial Property with the required documents.

A design right is protected for a period of five years from the date of filing of the application, and is renewable for one or more periods of five years, up to a total term of 25 years. Any right holder who feels aggrieved by an action in contravention of the exclusive rights conferred by the design right may initiate civil proceedings within five years from the date when the right holder obtained knowledge of the infringement and the identity of the alleged infringer. Remedies claimable by injured rights holders shall be those as stated in Cap 488, and as briefly elaborated in **7.1 Patents**.

7.4 Copyright

As provided in the Copyright Act (Chapter 415 of the Laws of Malta), copyright protects artistic, audiovisual, databases, literary and musical works, and is granted automatically to a work which has an original character and which has been written down, recorded, fixed or otherwise reduced to material form. Therefore, there is no need for registration, as protection is granted upon the creation of the work. Ideas, procedures, methods of operation or mathematical concepts cannot be granted copyright protection. Except in the case of computer programs and databases, copyright protection shall always vest in the author or joint author as the case may be.

The author of a work eligible for copyright (or beneficiary where copyright has been transmitted by assignment or by testamentary disposition) enjoys, until the expiry of copyright, in addition to copyright, the moral right:

- to claim authorship of their work, in particular, the right that their name as far as practicable be indicated in a prominent way on the copies and in connection with any public use of that work; and
- that their name be not indicated on the copies or in connection with any public use of their work, or that their pseudonym be used.

It is not possible to transmit any of these moral rights during the lifetime of the author.

Protection of Copyrights is granted under Maltese law for the following periods:

- Literary, musical or artistic works and database: 70 years after the end of the year in which the author has died, with no regards when was the work lawfully made available to the public.
- Audiovisual works: 70 years after the end of the year in which the last person out of the following has died: Principal director, the author of the screenplay as well as the author of the dialogue and the composer of music which was specifically created for its use in the audiovisual work.
- With regards to Publishers of previously unpublished works for which the copyright protection has expired: 25 years from the time when the work was first lawfully published or lawfully communicated to the public.
- Neighbouring rights (performer rights): 50 years from the end of the year in which the fixation of the performance was first lawfully published or lawfully communicated to the public.

- Neighbouring rights (producer's rights): 50 years from the end of the year in which, the earlier of, sound recording or the first fixation of the audiovisual work was first lawfully published or lawfully communicated to the public; or in the absence of publication or communication to the public, from the end of the year in which the first fixation was made.
- Neighbouring rights (broadcaster's rights): 50 years from the end of the year in which the broadcast was first transmitted whether by wire or over the air. Regardless whether such broadcasting was made by cable or satellite.
- Sui Generis rights of Databases: 15 years as of the first of January of the year following the date of completion of the making of the database; or if made available to the public the right shall be protected for a period of 15 years from the first of January of the year following the date when the database was first made available to the public.
- Sui generis rights in respect of semiconductors: ten years from the end of the year in which the semiconductor product topography was first commercially exploited at any point in the world or alternatively for 15 years from the first fixation or encoding of the semiconductor product topography in case it has not been commercially exploited.

The FHCC shall have jurisdiction to decide on enforcement measures in actions filed by the right-holder for infringement of copyright, neighbouring rights or sui generis rights. Damages claimable by injured rights holders shall be those as stated in Cap 488, and as briefly elaborated in **7.1 Patents**.

Subsidiary Legislation 460.36, which transposed Directive (EU) 2017/1564 is another important piece of legislation which aims to establish rules on the use of certain work subject to copyright protection for the benefit of persons who are blind, visually impaired or otherwise print-disabled without the need to request authorisation from the right-holder.

7.5 Others

The Copyright Act considers databases and software as work eligible for copyright. However, the content of the database is excluded from copyright protection. Software is included within a wider term "computer program" which in turn forms part of the literary works described in **7.4 Copyright**. As a general rule, the intellectual property rights pertaining to literary works apply also with respect to software.

The Copyright Act also contains the concept of sui generis rights granted to the maker of the database. This exclusive right protects against the unauthorised extraction and re-utilisation of the whole or substantial content of the database provided that there has been a qualitatively or quantitatively substantial investment in either the obtaining, verification or presentation of the contents of the database. However, this exclusive right shall not apply to the extraction and re-utilisation of non-substantial parts of the content of a database provided that a licensed user does not perform acts which conflict the normal exploitation of the database or in any manner prejudices the legitimate interests of the maker of the database.

Furthermore, a database will only be eligible for copyright if it constitutes the author's intellectual creation.

In the case of computer programs and databases, where work is carried out during the course of the author's employment, the economic rights granted by way of copyright protection shall be deemed to be transferred to the author's employer unless there is an agreement to the contrary limiting or otherwise excluding such transfer.

Trade Secrets

Trade Secrets have also become a recognised intellectual property within the Maltese jurisdiction, following the introduction of the Trade Secrets Act (Chapter 589 of the Laws of Malta). This act, which came into force on 13 July 2018, is a transposition of Directive 2016/943/EU on the protection of undisclosed know-how and business information (trade secrets) against their unlawful acquisition, use and disclosure.

For a trade secret to obtain a legally protectable status, it would have to satisfy the definition established by the Trade Secrets Act.

According to this Act, a "trade secret" means information which meets all the following requirements:

- it is secret in the sense that it is not, as a body or in the precise configuration and assembly of its components, generally known among or readily accessible to persons within the circles that normally deal with the kind of information in question;
- it has commercial value because it is secret; and
- it has been subject to reasonable steps under the circumstances, by the person lawfully in control of information, to keep it secret.

Trade secrets under the Trade Secrets Act are protected from:

- unauthorised access, appropriation, copying of documents object materials substances or electronic files which are lawfully under the control of the secret holder and which contain either the trade secret or information from which the trade secret can be deduced; and
- any conduct not contained in the above point which can be considered as contrary to honest commercial practices.

Furthermore, unlawful use or disclosure of a trade secret is considered to arise in situations in which a person, without the consent of the trade secret holder, is found to have met any of the following conditions:

- having acquired the trade secret unlawfully;
- being in breach of a confidentiality agreement or any other duty not to disclose the trade secret;
- being in breach of a contractual or any other duty to limit the use of the trade secret; or
- knowledge that the trade secret has been obtained directly or indirectly from another person who was using or disclosing the trade secret unlawfully.

According to Article 9 of this Act, any party has the ability to protect a trade secret against its unlawful acquisition, use or disclosure. During the course of legal proceedings, a trade secret's confidentiality may also be preserved.

Damages claimable by injured rights holders shall be those as stated in Cap 488, and as briefly elaborated in **7.1 Patents**.

8. Data Protection

8.1 Applicable Regulations

The primary legislative instrument regulating personal data protection in Malta is the Data Protection Act (Chapter 586 Laws of Malta). Furthermore, given Malta's status as an EU Member state, the EU General Data Protection Regulation (EU) 2016/679 ("GDPR") is directly applicable to the territory of Malta.

The Data Protection Act aims to implement and further specify the relevant provisions of the GDPR. Accordingly, the Data Protection Act together with the subsidiary legislation issued thereunder essentially regulate areas which are either not addressed by the GDPR or where the GDPR allows Member States to implement their own rules. This includes the setting up and composition of the data protection supervisory authority in Malta.

Therefore, while the GDPR provides the substantive data protection rules, the Data Protection Act essentially establishes the local enforcement and procedural rules. In particular, the latter establishes the Office of the Information and Data Protection Commissioner (IDPC) which is the regulatory authority overseeing all aspects of data protection in Malta, as well as the Information and Data Protection Appeals Tribunal, which hears appeals from parties that feel aggrieved by any decision taken by the Information and Data Protection Commissioner.

8.2 Geographical Scope

Given that the GDPR is directly applicable in Malta, any processing of personal data relating to Maltese data subjects is primarily governed by the GDPR. As such, the territorial scope set out in Article 3 of the GDPR includes all personal data processing activities which are:

- carried out by establishments from within the territory of the EU, including Malta; and/or
- targeting the EU territory (including the Maltese territory) by way of offering goods and services aimed at the EU territory or monitoring the behaviour of data subjects within the EU.

Accordingly, any foreign company undertaking personal data processing activities of customers located in Malta should comply with the rules established by the GDPR. Furthermore, the specific provisions of the Data Protection Act shall apply in cases where:

- the processing of personal data is done in the context of activities of an establishment of a controller or a processor located in Malta or in a Maltese Embassy or High Commission abroad;
- the processing of personal data is done in relation to data subjects who are located in Malta, by a controller or processor not established in the EU: this applies where the processing activities are related to the offering of goods or services to data subjects in Malta or the monitoring of their behaviour in so far as their behaviour takes place within Malta; and
- the processing of personal data is done by a controller not established in the EU but in a place where the laws of Malta apply by virtue of public international law.

8.3 Role and Authority of the Data Protection Agency

The authority in charge of supervision and enforcement of data protection legislation in Malta is the Office of the Information and Data Protection Commissioner (IDPC).

Pursuant to Data Protection Act, the IDPC is granted authority to monitor and enforce the application of the provisions of the Data Protection Act and the GDPR, with a special focus on:

- protecting the fundamental rights and freedoms of natural persons relating to the processing of their personal data; and
- facilitating the free flow of personal data between Malta and any other Member States.

Furthermore, the role of the IDPC includes the facilitation of the right to access information held by public authorities and to promote transparency and accountability within government.

Under the Data Protection Act, the IDPC is given authority to exercise its tasks and powers with complete independence and free from any external influence, whether direct or indirect. The person appointed to hold office as Commissioner is appointed by the Prime Minister of Malta, following consultation with the opposition leader.

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WH Partners is a Malta-based leading law firm with a business focus and expertise in fintech, technology, gaming and gambling, tax, M&A and corporate finance. The firm also advises clients on intellectual property, data protection, capital markets, commercial contracts, real estate, employment law, trusts and foundations and citizenship, residence and immigration. WH Partners is the exclusive member for Malta of Ally Law.

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Trends and Developments

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The Rise of Fintech

Introduction- Fintech

The financial services industry has seen drastic technology-led innovation over the past years. Undoubtedly, the accelerating pace of technological change has become the driving force in the financial services ecosystem. Fintech disruptors have been striving to get in the traditional ecosystem. These so-called disruptors are fast-moving companies, often start-ups, focused on particular innovative technologies.

As an industry traditionally comprising banks, insurers and asset managers, Malta's finance sector has recently seen new operators entering the market. New challenges in the post-crisis financial landscape, pressure on banks to cut costs and changing market dynamics driven by technology-savvy consumers have created a fertile environment for fintech.

Malta's small size makes it the ideal test environment for new technologies and ventures. Currently, financial institutions are being witnessed taking a secondary intermediary role rather than managing transactions from end to end they are just one node in a network. This evolution is driven by P2P transactions, enabled by a new breed of fintech companies. This is already witnessed with P2P lending platforms, often in partnership with traditional banks.

In spite of regulation and other potential barriers to entry, the industry has seen exceptional demand for fintech-related services in areas such as consumer banking and wealth management. For instance, the rise of "robo-investing platforms" offered by both online-only and traditional wealth management companies is being repeated across virtually every sector within financial services. Disruptors in retail banking are using this online-only model to grow market share by offering a highly customised user experience combined with lower fixed costs. The industry is seeing new high-tech companies with potential to drive down costs and offer better customer experience in the marketplace lending arena.

Future of money – the raise of digital currencies and payments

Digital currencies, cryptocurrencies, online payment systems, cashless society movements are rapidly changing the world of money by shifting it towards dematerialisation.

Cash, the most common means of payment, is becoming less popular in today's fast, technology driven lifestyles. Massive environmental impacts of its production and costs associated with its storage and transportation, the fact that it enables tax evasion and fuels criminal activity are the strongest and most common arguments against it nowadays.

The last decade has seen the rise of electronic money, which is slowly but surely replacing cash payments. However, also being witnessed is the rise of cryptocurrencies such as Bitcoin and Ethereum, which, due to their high volatility, unpredictable transaction costs and AML/CFT risks, have until now failed to gain widespread adoption. However, these deficiencies seem to be unravelled by newly emerging stablecoins, Libra being the most well-known one.

The Libra Project

Facebook's Libra project was formally announced in June 2019 with its main goal being "to enable a simple global payment system and financial infrastructure that empowers billions of people". The initial idea was for Libra coin to be pegged to a basket of traditional fiat currencies (50% USD, 18% EUR, 14% JPY, 11% GBP, 7% SGD) and its value would depend on the evolution of the whole basket. As a result of the accusations made by the governments and regulators, Libra's whitepaper was changed in April 2020 to reflect the new strategy of issuing several stablecoins, referred to as Libracoins, which would be pegged to single currencies such as LibraUSD, LibraEUR, LibraGBP and LibraSGD. This approach will "allow people and businesses in the regions whose local currencies have single-currency stablecoins on the Libra network to directly access a stablecoin in their currency".

Taking into consideration that Facebook has over 2.4 billion users, who would be given an alternative to the current banking system, it is only understandable that the governments and regulators fear the impact Libra could have on the monetary sovereignty.

In his speech given at the ECB Legal Conference in September 2019, Yves Mersch, member of the Executive Board of the European Central Bank, stated that because money is a public good, money and state sovereignty are inexorably linked. He further warns of the risk related to the digital currencies issued by the private companies:

"When it comes to money, centralisation is only a virtue in the right institutional environment, which is that of a sovereign entity and a central issuance authority. Conglomerates of corporate entities, on the other hand, are only accountable to their shareholders and members. They have privileged access to private data that they can abusively monetise. And they have complete control over the currency distribution network. They can hardly be seen as repositories of public trust or legitimate issuers of instruments with the attributes of money".

Central bank digital currencies

As a response to this new reality, the central banks started looking into creating their own digital currencies (CBDC). Bank of England, defined CBDC in its discussion paper "Central Bank Digital Currency – opportunities, challenges and design" as "an electronic form of central bank money that could be more widely used by households and businesses to make payments and store value". CBDC will be issued and regulated by the central banks and supported by the monetary reserves of the issuing central bank.

The Bank for International Settlement (BIS) defines three types of CBDCs:

- Retail CBDC, general purpose based on central bank accounts;
- Retail CBDC, general purpose based on digital tokens; and
- Wholesale CBDC, based on tokens or accounts and used for interbank payments or securities settlement.

Aside from countering the aforementioned challenges presented by Libra, the following are some of the other reason to launch CBDC: increase of the payment system efficiency and maintenance of competitive systems, cross-border payments, higher seigniorage, prevention and tracing of illegal transactions, money laundering and funding of terrorism, crime and tax evasion, financial inclusion, development of cashless society, countering competition from foreign CBDCs, etc.

BIS recently conducted a survey among 66 central banks which shows that more than 80% are working on developing their own CBDC, European Central Bank being one of them. The People's Bank of China (PBOC) is already conducting trials of its digital yuan in in Shenzhen, Suzhou, Chengdu and Xiongan. On 21 January 2020 the Bank of Canada, the Bank of England, the Bank of Japan, the European Central Bank, the Sveriges Riksbank and the Swiss National Bank, together with the Bank for International Settlements (BIS), announced that they have created a group to share experience as they assess the potential cases for central bank digital currency (CBDC) in their home jurisdictions.

There is no doubt that the digitalisation of money is on a fast track with private companies leading the way by issuing their own stablecoins. The Central banks are left with no choice but to follow the trend and work on issuing CBDC which will be supported by a strong framework providing for inter alia consumer protection and efficient payment systems.

Tokenisation of Assets

The evolution being experienced is not just about the money. Tokenisation of assets promises to completely revolutionise the concept of ownership. Anything from ideas to paintings to buildings can be represented in tokens and freely traded on blockchain systems. Asset tokenisation has become one of the most prominent use-cases of distributed ledger technologies (DLTs) in financial markets, for assets including securities (eg, stocks and bonds), commodities (eg, gold) and other non-financial assets (eg, real estate).

Tokenisation is the process of issusing a token that digitally represents a real tradeable asset. A security token can be used to create a digital representation – a security token – of an asset, meaning that a security token could represent a share in a company, ownership of a piece of real estate, or participation of an investment fund. These security tokens can be traded on the secondary market.

This method of converting rights to a real-world asset into digital tokens that can be moved, traded, recorded or stored on a blockchain system. Blockchains offer a way to revolutionise traditional paper markets, dramatically reducing costs and paperwork. There are key benefits that tokenisation offers to both investors and sellers: faster and cheaper transactions. Transactions are completed by means of smart contracts so certain parts of an exchange are automated. Fewer intermediaries are needed, leading to not only faster execution, but also lower transaction fees.

Another advantage is accessibility as tokenisation opens up investment in assets to a much wider audience. There is also more transparency. A security tokencan have the token-holder's rights and legal responsibilities embedded directly onto the token, along with the immutable record of ownership. These characteristics promise to add transparency to transactions, allowing users to know with whom they are dealing with, their rights and who has previously owned the token.

Applying DLTs and smart contracts

The application of DLTs and smart contracts in asset tokenisation has the potential to deliver a number of benefits including efficiency gains driven by automation and disintermediation; transparency; improved liquidity potential and tradability of assets with near-absent liquidity; faster and potentially more

efficient clearing and settlement. It allows for fractional ownership of assets which, in turn, could lower barriers to investment and promote more inclusive access of retail investors to previously unaffordable or insufficiently divisive asset classes (eg, real estate) allowing global pools of capital to reach parts of the financial markets previously reserved to large investors.

At the same time, the adoption of asset tokenisation at a large scale would face a number of challenges related to technology (scalability; settlement finality; interoperability; network stability; cyber-risks); governance; risks related to AML/CFT; issues around digital identity; issues around data protection and privacy; as well as around the legal status of smart contracts.

Another point to consider is governance. If ownership of an asset (such as a building) is split among thousands of people, there is little incentive for owners to bear the costs associated with that asset such as maintenance.

Tokenisation of Securities

With regard to financial assets, tokenisation of securities (equity and/or debt) is seen by the market as the sector with the most imminent potential for growth as it would involve the mere replacement of one technology with another.

Security token are nothing more than a digital representation of real tradeable assets that are found on blockchain-based platforms. As a step forward in this direction, in July 2019, the Malta Financial Services Authority (MFSA) issued a consultation document to establish the legal framework for security token offerings (STOs).

According to consultation document, in order to determine whether a DLT asset is in fact a financial instrument or not, one would need to apply the Financial Instruments Test to determine whether it qualifies as electronic money, financial instrument, virtual financial asset or a virtual token. If it qualifies as a financial instrument, one will need to analyse whether it is equivalent to a transferable security as defined by MiFID II and whether they are negotiable on the capital market. The MFSA issued its feedback however no legislative framework has been developed and the MFSA is expected to issue a dedicated rulebook to STOs in the next months.

In essence, tokenised securities could be seen as a form of cryptography-enabled dematerialised securities that are based and recorded on a decentralised ledger powered by DLTs, instead of electronic book-entries in securities registries of central securities depositories. The use of DLT expediates trade clearing and settlement to nearly real-time, reducing counterparty risks and freeing up collateral, producing capital efficiencies for participants in the trade. The post-trade process is simplified, and the back-office administrative burden is lowered significantly. The use of a uniform and equivalent central securities depositary system for securities based and powered by DLTs will need to be addressed at a European level as the DLT will need to be structured to work around the EU Central Securities Depositary Regulation.

Other key benefits with security token offerings is that anti-money laundering and know-your-customer checks are quicker because they are automated and the fact that tokens can be traded globally, the investor as long as he or she has a wallet, will be able to trade wherever he or she wishes.

Clear guidance from regulators is fundamental since there is usually uncertainty as to how a security token should be considered within the law. It is crucial to provide a safe legal framework in which the technology can thrive. Having said this, as with any technology, some questions need addressing.

Malta DLT Framework

The Maltese Government and the Malta Financial Services Authority have together made a huge leap forward in their fintech journey. The first step in the right direction was the creation of a Distributed Ledger Technology (DLT) legal regime which consists of the: Malta Digital Innovation Authority (MDIA) Act (Chapter 591 of the Laws of Malta); Innovative Technology Arrangements and Services (ITAS) Act (Chapter 593 of the Laws of Malta); and the Virtual Financial Assets (VFA) Act. The three acts work together to regulate: DLT; investment services activities concerning VFA's; and issuers offering VFA's to the public or wishing to admit VFAs on a DLT exchange, in or from within Malta.

Under the DLT framework, specifically the VFA Act, the MFSA has been given the power to introduce a Financial Instrument Test. The objective of the FI Test is to determine whether a DLT asset, based on its specific features, is encompassed under: the existing EU legislation and the corresponding national legislation; the VFA Act; or is otherwise unregulated.

The FI Test sequentially assesses the features of the DLT Asset against a set of predetermined criteria to determine whether a DLT Asset qualifies as:

- a Virtual Token (as defined under the VFA Act to mean any form of digital medium recordation whose utility, value or application is restricted solely to the acquisition of goods or services, either solely within the DLT platform (excluding DLT exchanges) or in relation to which it was issued or within a limited network of DLT platforms); or
- a Financial Instrument (as defined under section C of annex I to MiFID II); or

- Electronic Money (as defined under the Electronic Money Directive 2009/110/EC); or
- a VFA (as defined under the VFA Act to mean any form of digital medium recordation that is used as a digital medium of exchange, unit of account, or store of value and that is not - (a) electronic money; (b) a financial instrument; or (c) a virtual token).

Malta fintech strategy

in January 2019, the MFSA embarked on a wider, cross-sectorial "fintech strategy' (Strategy) supported by six pillars, namely: regulations (to adopt regulatory and supervisory initiatives to support innovation and improve regulatory efficiency), ecosystem (to foster community, demand and collaboration and enhance access to finance), architecture (to encourage collaboration through the adoption of Open APIs and shared platforms), international links (to build international links across jurisdictions to foster collaboration and trust), knowledge (to cultivate deep talent pools and stimulate research and collaborative ideation. and security (to establish an environment that is resilient to cybersecurity threats).

The Strategy's ultimate goal is to establish a holistic and robust fintech sector, to enable fintech start-ups and scale-ups, technology firms and established financial services providers to develop viable fintech solutions which drive innovation and enhance access to financial products, increase competition whilst promoting market integrity, deliver better customer experiences, and ultimately, contribute to the long-term success of the Maltese financial services sector.

The key elements set-out in the Strategy concern the introduction of a "Fintech Regulatory Sandbox" (to promote innovation and experimentation) and "Fintech Innovation Hub" (to further stimulate collaboration and innovation). The Sandbox would provide a platform where firms may explore and test their business concepts and solutions with proportionate safeguards, in a contained environment for a well-defined duration. This space will allow the MFSA to monitor the innovative business with contained risk. It will also allow the MFSA to build capacity and experience in regulating and supervising this field.

Malta's fintech sandbox

Following the launch of the Strategy, the MFSA, in January 2020, took the position of issuing a Draft Rule ("Rule") which attempts to establish a Sandbox which would not require a standalone framework or any additional changes to the existing legislation.

The below listed criteria would all need to be satisfied for the applicant and its fintech solution (ie, a specific utilisation of fintech) ("Solution") to be eligible for participation in the Sandbox:

- Innovation - the Solution shall be a technology enabled innovation which offers something new to the financial services sector.
- Need - there must exist a genuine need to test the Solution within the Sandbox.
- Benefit – a benefit must be derived, directly or indirectly to the financial services sector and its consumer.
- Readiness – the Applicant (ie, the person submitting to the MFSA a proposal for a Solution to be tested within the Sandbox) must show it has enough resources to operate for the duration of the sandbox and that the Solution functions already.

The Sandbox lifecycle will consist of six stages, namely: proposal, selection, application, testing, evaluation and exit. It is important to note that only where the MFSA determines that the proposed Solution: would not require a licence or authorisation from the MFSA; or is an activity which the Applicant is already licensed or authorized by the MFSA to carry out, may such Applicant proceed to the "Testing Stage".

AML compliance considerations

Malta has transposed the fifth AMLD into the following legislative instruments:

- the Prevention of Money Laundering Act (Chapter 373 of the Laws of Malta) (PMLA); and
- the Prevention of Money Laundering and Funding of Terrorism Regulations (Subsidiary Legislation 373.01). (PMLFTR)

Any fintech business (including VFA Issuers and VFA Licencees) which carries out either a "relevant financial business" or "relevant activity" is defined as a Subject Person under the PMLA and the PMLFTR. Subject Persons are required to take steps, proportionate to the nature and size of its business, to identify and assess the risks of money laundering and funding of terrorism that arise out of its activities or business, taking into account risk factors including those relating to customers, countries or geographical areas, products, services, transactions and delivery channels and shall furthermore take into consideration any national or supranational risk assessments relating to risks of money laundering and the funding of terrorism.

Moreover, Subject Persons must implement any guidance measures issued by Malta's Financial Intelligence and Analysis Unit.

How does Malta's framework compare to the UK's fintech position?

The UK has by far the largest fintech business community in Europe. In the UK there currently exits no regulatory framework specifically for fintech enterprises or DLT for that matter.

However, the UK have moved quicker than Malta in embracing fintech as in 2014 the Financial Conduct Authority (FCA) created "Project Innovate" which established:

- a "Regulatory Sandbox" to support fintech innovation and allow various firms to test their products and services in a controlled environment with real customers;
- an "Innovation Hub" to assist fintech firms understand the regulatory environment and apply for any required authorizations; and
- an "Advice Unit" which provides regulatory feedback to firms developing automated models that seek to deliver low cost advice to consumers.

It is important to note that simply because a firm is offering a fintech solution in the UK it would not necessarily mean that such solution would fall outside traditional financial services regulated activity. A firm which intends to utilise a fintech solution to carry out regulated activities would still be required to apply for a licence with the FCA or Prudential Regulatory Authority (PRA).

Unlike Malta, the UK is yet to create a DLT legal framework. Thus, one would need to assess, on a case-by-case basis, whether a DLT asset's characteristics and activity would fall under traditional financial services legislation.

The FCA, in July 2019, issued a Policy Statement (PS19/22) which serves as a guide in assessing the different characteristics of DLT assets and the rights attached to them. The Policy Statement sets out in categorising DLT assets under a number of classifications, namely: exchange tokens and utility tokens falling outside the regulatory environment; and security tokens and e-money tokens falling within the regulatory environment. Furthermore, the Policy Statement stipulates the various permissions which would be required to: issue security and e-money tokens; or offer services in relation to security and e-money tokens.

Conclusion

With Brexit now a reality, one would need to evaluate the pros and cons of such an exit on the UK fintech environment. UK laws, as a result of Brexit, would eventually divert from EU law. This could be problematic for licensed financial services businesses operating in multiple EU Members states as they might not be able to benefit from the passporting regime which enables firms that are authorised in an EU Member State to provide regulated services, to also provide those same services in any other EU Member State with minimal additional authorisation.

Malta is well positioned to attract UK based fintech firms that wish to target the EU market. It is a jurisdiction that has a robust and innovative framework in place, while offering a very attractive business environment and infrastructure that is crucial for such firms to grow. To do so, Malta will need to find the right balance between reducing bureaucracy and maintaining a high degree of regulatory oversight in order to offer a safe, stable and reputable option for the fintech business community.

WH Partners is a Malta-based leading law firm with a business focus and expertise in fintech, technology, gaming and gambling, tax, M&A and corporate finance. The firm also advises clients on intellectual property, data protection, capital markets, commercial contracts, real estate, employment law, trusts and foundations and citizenship, residence and immigration. WH Partners is the exclusive member for Malta of Ally Law.

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