



Malta introduces VAT Grouping

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Introduction

Effective from 1st June 2018, new VAT Grouping provisions were introduced in the VAT legislation through Legal Notice 162 entitled '*Value Added Tax (Registration as a Single Taxable Person) Regulations, 2018*', published on 22nd May. Although VAT Grouping has been opted for by the majority of the EU Member States, it is a novel concept within the Maltese VAT Legislation.

Background

In essence, VAT Grouping allows multiple persons established within an EU Member State who, while legally independent, are closely bound by financial, economic and organisational links, to be regarded as one single taxable person for VAT purposes.

The EU VAT Directive gives discretion to Member States to implement VAT Grouping into their domestic VAT legislation after consulting with the VAT Committee. Indeed Malta has consulted with the VAT Committee and in the process, last month, the European Commission published a working paper, numbered 942 with its observations on the Maltese VAT Grouping regime as originally proposed. Since then, tweaks were made to the proposed VAT Grouping Regulations. Legal Notice 162 is the result. Such development followed from the last budget speech of the Minister of Finance, in October 2017, in which the introduction of VAT Grouping in Malta was announced.

The VAT Grouping regulations

Eligible persons

VAT Grouping is open to legal (not physical) persons established in Malta when at least one of such persons is a taxable person licensed or recognised in the financial or gaming sectors in terms of the Banking Act, the Financial Institutions Act, the Gaming Act, the Insurance Business Act, the Insurance Intermediaries Act, the Investment Services Act, the Lotteries and Other Games Act, the Retirement Pensions Act and the Securitisation Act. VAT Grouping is not mandatory but optional to eligible persons.

The required links between the VAT Group members

In order to be able to form a VAT Group, the members must all be bound to each other by Financial, Economic and Organisational (FEO) links.

Members are linked **financially** where any two of the following are, directly or indirectly, held as to more than 90% by the same person or persons - (i) voting rights or equivalent interests, (ii) entitlement to profits available for distribution; and (iii) entitlement to surplus assets available for distribution upon winding up or an equivalent event.

The **economic** links would be satisfied where (i) the activity of each member is of the same nature, is complementary, is interdependent or falls within the same industry of the other members; or (ii) where one member of the group carries out activities which are wholly or substantially for the benefit of one or more of the other members.

The **organisational** links are present where the members have a shared management structure, wholly or in part.

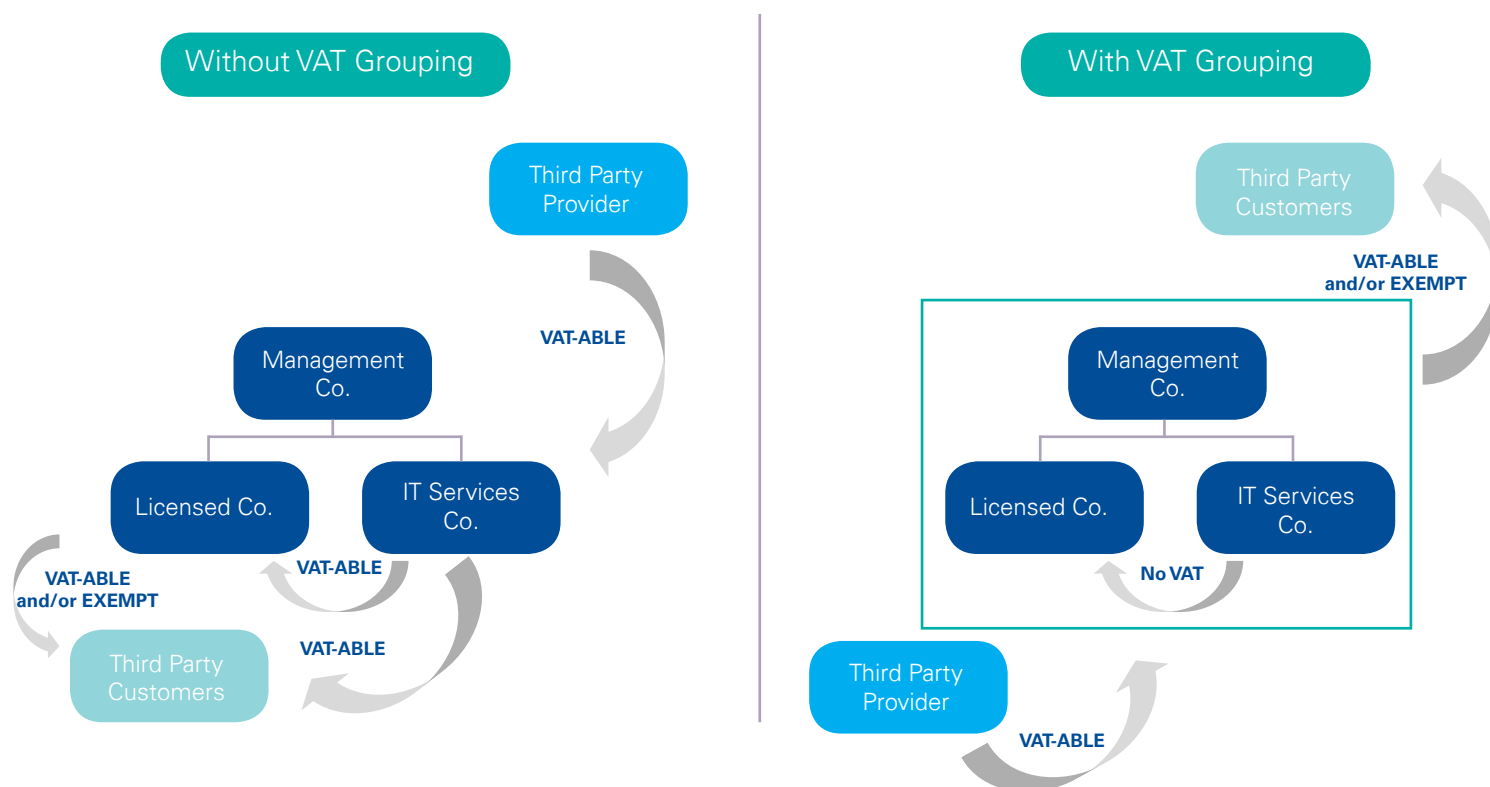
Persons bound to each other by the FEO links may only form part of one and the same VAT Group.

The implications of forming/joining a VAT Group

Upon forming a VAT Group, any supplies of goods and services between the VAT Group members are treated as out of scope of VAT. In turn, any supplies made **by** the group members to third parties or non-members of the VAT Group are to be treated as supplies made **by** the VAT Group. Similarly, any supplies made **to** the group members by third parties or non-members of the VAT Group are to be treated as supplies made **to** the VAT Group. More precisely, such supplies are deemed to be made **by / to** a Group Reporting Entity (GRE) that needs to be nominated by the members from amongst themselves to represent the VAT Group in terms of exercising the rights and discharging the obligations of the VAT Group. An apparent advantage of such treatment for entities engaged solely or partly in exempt without credit supplies, as is typically the case with financial and gaming operators, is that no self-induced VAT would be created on supplies (sometimes being recharges of pure costs such as HR costs, IT costs, etc.) made by group members to such operators. Supplying members need not charge VAT to recipient members while recipient members would not pay VAT, and potentially suffer it in part or in full, on such intra-group supplies. Such an advantage cannot be undermined, particularly in the financial and gaming sectors where the balance between in-housing of certain functions and outsourcing them can be challenging.

Another major implication is that all members of a VAT Group are jointly and severally liable for the payment of the Group's VAT liabilities, including interest and penalties. Even if a member leaves the VAT group, its liability for the period of membership remains with it. Conversely, by joining a VAT Group, a person is not relieved from any VAT obligations existing prior to the time of joining.

The below diagram gives a simplified pictorial explanation of how VAT Grouping may affect the taxability of transactions among members and non-members of a VAT Group.





Procedure

An application to form/join a VAT Group will need to be made electronically to the VAT Department together with the submission of evidence supporting the FEO links. The applicants must be compliant with both their income tax and VAT compliance obligations in order to successfully set-up/join a VAT Group.

The VAT Group will be allocated a single VAT number in terms of Article 10 or 12 of the VAT Act as the case may be. Any previous individual VAT numbers of the members will be cancelled. Consequently, the change in the VAT number of a member would require notification to the suppliers of such member.

Once a VAT Group is formed, 24 months must pass before it can be dissolved. Once dissolved, another 24 months must pass before the VAT Group can be formed again.

Membership of a member shall be terminated where the FEO links cease to exist.

All members are to keep full and proper records of all transactions entered into with both members and third parties. In addition, the GRE is required to keep consolidated records of all transactions which are deemed to be treated as carried out by the GRE.

The territorial scope of VAT Grouping

The VAT Grouping Regulations provide that if a legal person has establishments (branches/head office) outside Malta, such establishments would collectively be deemed as one single legal person for Maltese VAT Grouping purposes. In its aforementioned working paper, the EU Commission had queried the extension of the territorial scope of VAT Grouping beyond Malta arguing that such extension seems to be inconsistent with earlier guidelines set by the VAT Committee and with the case of the Court of Justice of the EU, *Skandia America*¹. Following consultation on this point, the VAT Grouping Regulations now include a rule to the effect that, if an establishment in Malta provides or receives services to/from a foreign establishment of the same entity and that foreign establishment is a member of a VAT Group in a Member State that operates a system of VAT Grouping in terms of which the foreign establishment alone forms part of a VAT Group, such services are no longer treated as out of scope of VAT.

The anti-abuse provisions

The VAT Grouping Regulations include an anti-abuse provision giving power to the Commissioner to regard intra-group supplies as third party supplies in order to avoid abuse. Naturally, one still has to see how such provision will be applied in practice once VAT Grouping picks up.

¹ Judgement of 17 September 2014, *Skandia America Corp. (USA) v. Skatteverket*, C-7/13



KPMG Observations

There are several benefits of VAT Grouping. Eliminating self-induced VAT on internally-generated supplies is one major benefit. Another benefit is aimed at administrative simplification – the VAT Group would file one consolidated VAT return (and recapitulative statement, where applicable) rather than separate VAT returns (and separate recapitulative statements) for every member of the group.

In addition VAT grouping unblocks cash that could otherwise be temporarily stuck if one member of the group is in a VAT payable position whilst another member is in a refundable position as shown in the above diagram. Such consolidation of the VAT position of members would simultaneously be beneficial for the tax authorities which need to process less VAT documentation and payments.

Nonetheless thorough consideration still has to be made before persons decide to join or form VAT group. For instance, the decision as to whether the VAT group should be registered under Articles 10 or 12 should be made on a group-wide basis, i.e. depending on the input and output supplies of the whole group. For those members whose type of registration would change if they join a VAT Group, they have to assess, amongst others, the VAT implications on any lease of office premises, bearing in mind that letting of premises for business purposes is only VAT-taxable if the lessee is registered under Article 10 of the VAT Act.

Similarly, when the VAT group includes members providing supplies which do not carry with them a full right of input VAT recovery, as is typical within the gaming and financial services sector, one has to assess the impact on the recovery of VAT on costs of the VAT Group as a whole, including the rights to recover VAT incurred on capital goods.

Any thresholds promulgated by the VAT Act, such as the 5% limit of input/output tax for the correction of mistakes in a subsequent VAT return will apply on a group-wide basis.

In conclusion, VAT Grouping is a new reality which would be worth for the financial and gaming industries to explore. The good thing is that the VAT Grouping regime is optional; which gives leeway to groups of companies to decide if and to what extent its entities should be grouped after a thorough analysis of their VAT positions.

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