

# **Guidelines in Relation to the NID Rules**

## **Notional Interest Deduction Rules ("the Rules")**

It is hereby clarified that:

### **(i) Determination of the Reference Rate**

The yield to maturity on Malta Government Stocks with a remaining term of approximately 20 years (i.e. "the risk-free rate") referred to in the definition of "the reference rate" contained in Rule 2 of the Rules is published on the website of the Central Bank of Malta on a quarterly basis.

It may be accessed by clicking on <https://www.centralbankmalta.org/malta-government-stocks> and then clicking to open the file "Indicative Rates based on Malta Government Benchmark Stocks". The applicable rate may be found from the Year 20 row.

In this respect, an undertaking is required to determine the reference rate for the purposes of calculating the notional interest deduction ("NID") by reference to the risk-free rate published by the Central Bank of Malta for the end of the quarter falling on the same day as the end of the accounting period of the particular undertaking. For example, the risk-free rate at the end of Q4 2017 is 2.03%. To arrive at the reference rate, this must be added to the 5% premium. Therefore, the reference rate at the end of calendar year 2017 is 7.03% (i.e. 2.03% + 5%).

Should the end of the accounting period of the said undertaking not fall at the end of a quarter, the undertaking shall calculate the NID on the basis of the reference rate applicable as at the end of the quarter immediately preceding the end of the accounting period ending in the year preceding the year of assessment for which the NID is claimed.

### **(ii) Approval for Claiming the NID**

The shareholders or partners in an undertaking, as the case may be, as at the end of the year preceding the year of assessment are required to give their approval for the undertaking to claim a NID by the earlier of the date on which the said undertaking files its income tax return for that particular year of assessment or the date on which any one of the said shareholders or partners ceases to be a shareholder or partner of the undertaking, as the case may be.

### **(iii) Attribution of the Deemed Interest Income**

The interest income that is deemed to accrue to shareholders or partners of an undertaking in terms of Rule 5 of the Rules, should for the purposes of sub-rule (3) of Rule 5 be allocated in its entirety to the undertaking's shareholders or partners, as the case may be.

Unless directed otherwise by the Commissioner in terms of the proviso to the said sub-rule (3), in the case of a company that has claimed the NID, the interest income is to be attributed to each shareholder according to the proportion which the nominal value of the shares that each shareholder holds in the company bears to the total nominal value of the issued share capital of that company as at the end of the undertaking's accounting period.

Unless directed otherwise by the Commissioner in terms of the proviso to the said sub-rule (3), in the case of an undertaking other than a company that has claimed the NID, the interest income is to be attributed to each partner according to the proportion which the value of the capital that each partner holds in the undertaking bears to the total value of that undertaking's capital as at the end of the undertaking's accounting period.

Unless directed otherwise by the Commissioner in terms of the proviso to sub-rule (3) of Rule 5 of the Rules, the interest income that is deemed to accrue to the shareholder or partner of a company or partnership in terms of Rule 5 of the Rules, shall, in case of any person holding the usufruct over any shares or partnership interest, be deemed to accrue to the person holding such usufruct rather than the bare owner of those shares or partnership interest.

### **(iv) Exchange of Information**

When the Commissioner exercises his discretion in terms of the proviso to sub-rule (3) of Rule 5 of the Rules to allocate the deemed interest income on a basis other than the nominal value of the risk capital held by the shareholder or partner, as the case may be, the criteria on which the Commissioner has based his decision in this respect shall be published as part of these Guidelines.

Any decision taken by the Commissioner in terms of the said proviso shall, where applicable, constitute an instance which requires the automatic exchange of information with the competent authorities of all other EU Member States, as well as with the European Commission, pursuant to Regulation 13(3) of the Cooperation With Other Jurisdictions On Tax Matters Regulations [[S.L.123.127](#)].

**(v) “the invested risk capital”**

References to the term “exempt” in paragraphs (a) and (b) of sub-rule (1) of Rule 4 of the Rules are references to exemptions from income tax in terms of article 12 of the Income Tax Act or in terms of any other act.

**(vi) Deducting the NID (Direct and Indirect Attribution)**

The amount deductible in terms of sub-rule (1) of Rule 3 of the Rules shall be deducted against the income of the undertaking in the following manner:

**(a) Direct Attribution**

Where the risk capital of the undertaking represents capital employed in acquiring any specific source of income (including, for the avoidance of doubt such income as is exempt/ not chargeable to tax in terms of any provision of the Income Tax Act or other legislation or income which is subject to a final rate of tax), the NID in respect of that risk capital shall be attributable exclusively against such income. A distinction shall be made between each and every source of income, regardless of the tax account to which such source is to be allocated.

The undertaking may then claim a deduction for NID only against such income that forms part of the chargeable income of the undertaking the profits from which stand to be allocated to the Maltese Taxed Account (hereinafter also referred to as MTA income) and the Foreign Income Account (hereinafter also referred to as FIA income) after all allocations in terms of the Income Tax Acts and their subsidiary legislation have been taken into account. NID that is attributable to a specific source of income may only be deducted against such income.

The NID in respect of capital that does not produce any income shall not be allowed as a deduction.

NID that is attributed directly to MTA or FIA income and which exceeds the 90% limitation in terms of Rule 4(2)(a), as explained further in (vi)(c) below, shall be carried forward on a source-by-source basis. NID that is directly attributable to any tax account other than the Maltese Taxed Account or the Foreign Income Account shall be forfeited;

**(b) Indirect Attribution**

Where, after carrying out the direct attribution of NID in (vi)(a) above, it transpires that the remaining risk capital of the undertaking represents capital that is employed in acquiring two or more sources of income of the undertaking in a general manner without being specifically attributable to any particular source of income, the NID in respect of such risk capital (“the remaining NID”) shall be attributable to such sources of income of the

undertaking (including, for the avoidance of doubt, such income as is exempt/ not chargeable to tax in terms of any provision of the Income Tax Act or other legislation or income which is subject to a final rate of tax) on a pro-rata basis in proportion to the chargeable income from each source of income net of any NID that has been directly attributed (irrespective of whether such directly attributed NID is deductible or not).

The undertaking may then claim a deduction for part or all of the remaining NID only against such income that forms part of the chargeable income of the undertaking the profits from which stand to be allocated to the Maltese Taxed Account and the Foreign Income Account after all allocations in terms of the Income Tax Acts and their subsidiary legislation have been taken into account. NID that has been attributed to a specific source of income on such pro-rata basis may only be deducted against such income.

NID that is attributed indirectly to MTA or FIA income and which exceeds the 90% limitation in terms of Rule 4(2)(a), and NID that is attributed indirectly to any other income the profits from which stand to be allocated to any tax account other than the Maltese Taxed Account or the Foreign Income Account and which exceeds such income, shall be carried forward in a general pool of indirectly attributable NID.

(c) The 90% limitation set out in Rule 4(2)(a) shall be calculated by reference to the total chargeable MTA and FIA income. However, the NID directly attributable to a particular source of MTA or FIA income that may be claimed in any year shall not exceed the income from that same source for that year.

#### **(vii) NID first deducted against Deemed Interest Income**

Where an undertaking (“A”) holds an interest in another undertaking (“B”) and B claims a deduction for sums that are deemed to be payable by way of interest on its risk capital in terms of Rule 3(1) of the Rules, A is deemed to have received an amount equal to the interest on risk capital claimed by B (the deemed interest income) in terms of Rule 5.

Where, besides such deemed interest income, A has other sources of income in respect of the risk capital that it has employed in B (such as, for example, dividend income from B) A may deduct its own NID attributable to the risk capital employed in B first against such deemed interest income.

#### **(viii) Deduction and Carry Forward of NID**

Where risk capital of an undertaking is not employed in a trade or business, and such risk capital does not result in any income (which, for the avoidance of doubt, is to be construed as referring to income before taking account of any expenses or other items that are deductible for income tax purposes) being produced in the year preceding the relevant year of assessment,

the NID available on such risk capital shall not be allowable as a deduction for income tax purposes, and therefore no excess thereof shall be carried forward to subsequent years of assessment.

The previous paragraph shall, however, not affect an undertaking's ability to carry forward unutilised NID that has been brought forward from prior years of assessment to subsequent years of assessment.

#### **(ix) Partial Deduction of NID with Carry Forward**

In terms of Rule 3(2) of the Rules, an undertaking may determine whether or not to claim a deduction of NID which it is deemed to have incurred on its risk capital.

Where an undertaking chooses not to claim a deduction for NID that it would have otherwise been entitled to claim, such NID cannot be claimed in future periods.

Any NID available to the undertaking for which it is not able to claim a deduction on the basis that the said NID exceeds 90% of the undertaking's MTA and FIA income can be carried forward in line with the provisions of Rule 4(2)(a) of the NID rules.

#### **(x) Certain Scenarios involving Multiple Funding Sources**

Where an undertaking has multiple funding sources such that it is not possible to determine whether any capital employed in another undertaking constitutes risk capital or other funding sources, the amount of risk capital that shall be taken into account in determining the NID shall be equal to a fraction of the capital employed in that other undertaking that is equal to the fraction arrived at by taking the risk capital of the undertaking and dividing it by the total of the risk capital of the undertaking and its other funding sources.

#### **(xi) Accounting Periods other than 12 Months**

To further approximate the neutrality between debt and equity financing, an adjustment shall be applied to the NID to remove distortive and disproportionate deductions in respect of accounting periods that are longer or shorter than 12 months. The NID in respect of the years of assessment to which such accounting periods refer shall be inflated or reduced by multiplying the deduction contemplated by Rule 4(1) of the Rules by the number of days in the accounting period and dividing the result by 365. This paragraph (xi) shall be applicable to the year of assessment 2020 and subsequent years of assessment.