Income Tax Act

Overview & Impact

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Introduction

The Income Tax Act ("ITA") ratified into law by the President on 17 December 2019 introduces personal income tax for the first time in the Maldives . It also abolishes the existing Business Profit Tax and Bank Profit Tax regime and brings these taxes within the scope of income tax regime. The Income Tax Act will come into force on 1 January 2020, although tax on income from employment will commence from 1 April 2020.

Abolition of certain taxes

The ITA abolishes the following taxes from 1 January 2020.

1. Remittance Tax - a 3% tax imposed on money transferred out of the Maldives by foreigners employed in the Maldives which was in effect from 1 October 2016.
2. Land Sales Tax - a 15% tax imposed on the sales price of dwelling or land which was in effect since 2002.
3. Petroleum Tax - a tax which was intended to impose on the activities of petroleum companies.

What happens to the Business Profit Tax regime?

Since 18 July 2011, the Maldives has been imposing income tax on business profits. As ITA intends to bring personal income and business income within its scope, the taxes imposed under the Business Profit Tax Act would be abolished on 31 December 2019, and continued under the ITA from 1 January 2020 onwards.

The tax rates under ITA will remain the same (as BPT regime) for corporates (15% as business income and 10% as non-resident WHT) and banks (25%) although the individuals will have different tax rates.

Who is subject to tax under the ITA?

Under the ITA, the following persons, among others, are subject to tax if their taxable income falls within the marginal tax brackets provided in the Act:

1. an individual
2. a company incorporated in Maldives or elsewhere
3. a partnership
4. a trust
5. an association

What incomes are taxable under the Income Tax Act?

The income that is taxable under Section 3 includes:

1. employment income
2. income from trade, business or profession
3. income derived from the rental of movable or immovable property
4. dividend and interest
5. annuity, pension and retirement benefits
6. technical service fee
7. royalty and commission
8. capital gains
9. any other gains or profits of an income in nature.

A person is taxed on his total taxable income which is derived from all the sources of income mentioned in Section 3 of the ITA. Taxable income is the income that is left after deducting all the allowable deductions under the ITA (see below).

Tax on employment income will take effect from 1 April 2020, while tax on all other types of income are applicable on all persons effective from 1 January 2020. Income from employment (remuneration) includes salary, allowances, bonuses and benefits in kind paid to employees by an employer for their services. Remuneration paid to directors or partners for their services are also charged to tax under the head 'remuneration'.

What is taxable income?

Income tax is payable on total 'taxable income' in a given year. Taxable income is the gross income from all the sources mentioned above, less any deductions allowable under the ITA. The deductions available vary depending on the type of income. For example, deductions in relation to employment income are very much limited under the ITA, while a person will be able to claim a deduction for most of his/her expenses in relation to business income.

General rule for deductions

In relation to employment income

Expenses must be wholly, exclusively and necessarily incurred during the period in the production of employment income (that is, in the performance of employment duties) (Section 17(a), Section 32(b)(6). Although the said conditions are not satisfied, the following specific deductions may be claimed in relation to employment income:

1. Zakat-al mal paid to the relevant government institution (Section 18);
2. The amount that a person contributes to the Maldives Retirement Pension Scheme (Section 19);
3. Donations made to a MIRA approved charitable organizations (up to a maximum of 5% of taxable income before deducting donation expense) (Section 21).

Domestic or private nature expenses are not deductible. Since limited deductions are available in relation to employment income, in most cases, employment income less pension payable to Maldives Pension Administration Office will be the person's final taxable income.

In relation to business income

Expenses must be wholly and exclusively incurred during that period, in the production of business income, subject to the restrictions provided in the ITA. Most of the business expenses when claimed in accordance with internationally accepted accounting standards such as International Financial Reporting Standards (IFRS) are allowable as deductions in relation to business income, although certain expenses may be restricted.

Certain deductions specified in the ITA are allowed even for businesses (such as Zakat, pension, donations) despite restrictions under the general rule.

Capital expenses are allowed capital allowance at the following rates, which are stated in the Income Tax Regulation:

Category	*Rate*
Building	4%
Aircraft	7%
Wooden marine vessels	7%
Other marine vessels	5%
Furniture and fittings	10%
Motor vehicles	20%
Earth moving vehicles	5%
Plant and equipment (excluding office equipment)	10%
Office equipment	20%
Computer software	$33^1/_3$%
Crockery, cutlery, utensils, linen, loose tools	$33^1/_3$%

Basics

The ITA adopts a ‘residence-based’ tax system. A tax resident of Maldives is taxable on world-wide income, be it an individual or an entity (Section 10(a)). A non-resident is taxable only on Maldives-sourced income (Section 10(b)).

The term “residency”in the context of Income Tax differs from its ordinary usage or meaning. An individual is generally a resident if the person’s permanent place of abode is in the Maldives or has been present in the Maldives for a period of 183 days or more in a 12-month period commencing or ending in a tax year. Further, an employee or official of the Government of the Maldives who is posted overseas during a tax year is also considered as a resident.

A company is considered resident if it:

1. is incorporated in the Maldives, or
2. has its head office in the Maldives, or
3. has its central management and control in the Maldives.

The ITA also introduces a “temporary residency” concept in relation to individuals, where temporary residents will declare and pay income tax on Maldives sourced income only.

A temporary resident is an individual who would otherwise fall under the definition of a resident (that is, present in the Maldives for more than 183 days, or has a permanent place of abode in the Maldives, etc) but also, is staying in the Maldives with a permit granted under the Maldives Immigration Act. Such individuals will not be considered as a temporary resident if he/ she is married to a Maldivian.

In practice, what this means is that foreign nationals working in the Maldives (under a work visa) who are not married to Maldivians, will declare their income only on Maldives-sourced income.

Tax Year

A tax year is from January to December. A person is generally required to declare tax for an accounting period of 12 months ending in a tax year. Accounting period of a person should also be from January to December.

Exempt Income

Types of income exempt from ITA are included in Section 12. This includes passive interest income (up to MVR 5,000 per year) and gifts (subject to *de minimis* rule and certain other conditions) and dividends received from a resident company by a resident.

Tax Rates

Individuals (Section 7):

Annual Taxable Income (MVR)	*Tax Rate*
≤720,000	0%
>720,000 ≤1,200,000	5.5%
>1,200,000 ≤1,800,000	8%
>1,800,000 ≤2,400,000	12%
>2,400,000	15%

Banks (Section 8):

Banks would pay income tax at the rate of 25%. No tax-free threshold is given to banks.

Others (everyone except individuals and banks) (Section 9):

Annual Taxable Income (MVR)	*Tax Rate*
≤500,000	0%
>500,000	15%

Accounting Basis (Section 13)

In relation to employment income

Generally, the declaration has to be based on the accrual basis.

In relation to business income

Accounts must be prepared in accordance with IFRS or any other internationally accepted accounting standards approved by the MIRA.

Pay as You Earn (PAYE) Meachanism

Employers are required to withhold income tax on remuneration paid to employees and pay such amounts to MIRA on a monthly basis (Section 54). The Withholding Tax brackets provided in the ITA are as follows:

Monthly Income (MVR)	*Tax Rate*
≤60,000	0%
>60,000 ≤100,000	5.5%
>100,000 ≤150,000	8%
>150,000 ≤200,000	12%
>200,000	15%

The above PAYE brackets are based on the annual tax brackets for individuals (pro-rated to arrive at monthly brackets).

The employers can only deduct an employee's contribution payable to the Maldives Retirement Pension Scheme for that month, in accounting for the employee's WHT. Employees can make an annual declaration of their income and claim any additional deductions (apart from pension contribution) that they may be eligible for. However, if an employee derives income solely from a single employer, he/she is not required to file an annual tax return (although he may choose to do so if he/she wishes to claim further deductions).

Due to the fact that limited deductions are available from employment income, in most cases, the correct amount of tax would have been paid as PAYE and hence, an employee's PAYE will usually be his/her final tax liability. This means that it will not be necessary to file a return and make a year-end adjustment. However, where an employee is eligible for deductions apart from pension, he/she may claim any such deductions by filing his/her final return which is due on 30 June following the tax year. When the final return is filed, any adjustment for excess or shortfall has to be accounted for.

Non-resident Withholding Tax

Non-resident Withholding Tax will be imposed on the following types of payments to non-residents (the ITA provides that Withholding Tax is payable on the earlier of payment date or accrual date of the payments) (Section 55).

1. Rent in relation to immovable property situated in the Maldives;
2. Royalties;
3. Interests;(except interest payable to bank or financial institutions approved by MIRA)
4. Dividends;
5. Technical Service Fee;
6. Commissions paid in respect of services performed in the Maldives;
7. Payments made in respect of performances by public entertainers;
8. Payments made for carrying out research and development in the Maldives;
9. Payments made to a non-resident contractor;
10. Insurance premiums;
11. Reinsurance premiums.

The Withholding tax rate is 10% on all the payments listed above except reinsurance premium (reinsurance premium attracts a 3% WHT).

Filing and Payment

Businesses and individuals are required to file their tax returns to MIRA no later than 30 June of the following tax year. The payments are generally made on 3 installments.

- Ø First Interim Payment - 31 July of the ongoing tax year
- Ø Second Interim Payment - 31 January of the following tax year
- Ø Final Payment - 30 June of the following tax year.

The first and second interim payments are generally based on half of the previous year's tax liability. Any excess/ shortfall is adjusted during the final payment.

However, the ITA allows taxpayers to make an estimate of the current year's liability and make interim payments based on that estimate if they expect their current period's liability to be less than that of the previous year (subject to certain conditions).

Further Section 49 removes the obligation of making the interim payments if the person's total interim payment liability is less than MVR 20,000, or his/her previous year's tax liability was less than MVR 20,000. In this case they will only pay a final payment of tax.

Tax avoidance

Transfer pricing (Section 67)
The ITA provides certain measures for tax avoidance schemes and arrangements. Transactions between related parties are required to be made at arm's length. Further Transfer Pricing Documentation requirements are required to be kept for related party transactions.

Thin capitalization (Section 71)
The ITA provides thin capitalisation rules which are in line with the Action 4 of the G20/OECD's Inclusive Framework on Base Erosion and Profit Shifting Project. Under the said rules the maximum amount a taxpayer can deduct as interest expense (except for interest payable to local banks and financial institutions licensed by MMA) is 30% of the tax-EBITDA. Any excess interest not deductible in the current year can be carried forward for a period of 10 years to be deducted against the interest capacity (30% of tax EBITDA) of that year.

Tax EBITDA is taxable profit before deducting Interest, capital allowances and loss relief.

Capital Gains Tax

The ITA has also introduces a more comprehensive capital gains tax regime. Gains on disposal of movable, immovable or intellectual property would generally attract capital gains tax. The capital gains will form part of the taxable income of that person and be subject to the tax brackets given in the ITA.

Certain types of transactions are exempt from Capital Gains Tax under Section 30(e) of the ITA (eg; disposal of household furniture and appliances).

Transitional Provisions

As Business Profit Tax and Bank Profit Tax is rolled over to the income tax regime, certain provisions required for a smooth transition into income tax regime, are provided in Chapter 13 of the ITA.

Companies, partnerships, individuals, trusts and other forms of businesses who are already in business prior to 1 January 2020 must already be fulfilling obligations under the Business Profit Tax regime. As BPT is to be abolished from 31 December 2019, tax on business profits will be imposed under the income tax regime from 1 January 2020 onwards.

The ITA contains special provisions to ensure a smooth transition from BPT to ITA. This includes the following:

- **Registration:** Although businesses are generally required to register under the ITA, no separate registration is required by those who are already in business (Section 87). However, as PAYE mechanism will take into effect from 1 April 2020, businesses will be required to register for PAYE (which is expected to be a basic registration with details of employees- more or less similar to the registration of employees for pension scheme under the Maldives Pension Act).

- **BPT Interim and Final Payments:** Although BPT will be abolished from 31 December 2019, the obligations that remained under the BPT Act for periods prior to 31 December 2019 will continue to apply (Section 88), even after 31 December 2019. This means that the non-resident Withholding Tax return for December 2019 (due on 15 January 2020), second interim payment for tax year 2019 (due on 31 January 2020) and the BPT final return and payment liability for tax year 2019 (due on 30 June 2020) will still be applicable 'as if the BPT Act is not repealed'.

- **Tax Audits:** Although the BPT Act will be abolished from 31 December 2019, Section 88 of the ITA authorizes MIRA to conduct audits and impose enforcement measures against taxpayers under the BPT Act even after that date, as if the Act was not repealed.

- **Losses carried forward:** Any losses that is carried forward under the BPT Act, can be utilised against the profits of businesses even under the Income Tax Act. However, the ITA imposes certain restrictions on businesses to claim loss reliefs, which includes a requirement that in case of companies, such losses can be deducted only if, from the beginning of the accounting period in which the loss is incurred to the end of the accounting period in which the loss (or part of a loss) is offset, the same shareholders continuously own 50% or more of the ordinary share capital of the company.

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ABOUT US

CTL Strategies is a multi-disciplinary law firm registered in the Maldives, specialised in tax advisory services. Over the past 5 years, we have advised international hotel chains, multinational companies, some of the big four audit firms, and a number of the world's largest companies as well as high net-worth individuals on their tax compliance, planning and tax disputes. Some of our team members have been involved in formulating the recent tax policy changes as well as drafting the Income Tax Act, and had headed departments at the tax authority that were responsible for drafting tax rulings and regulations on the Business Profit Tax Act as well as Goods & Services Tax.

We are ranked by the Asia Law Profiles as a Highly Recommended tax disputes firm in the Maldives in addition to be recognised as leading law firm in the Maldives from 2017.

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