

an overview of the
**1st Amendment to the
Income Tax Act**



1. Introduction

The legislative intent of the First Amendment to the Income Tax Act has been to address the difficulties faced in implementing the Act and to further strengthen the Maldives Income Tax Regime. Among other things, the most significant additions and changes have been brought to tax exemptions, tax on offshore indirect transfers and the categorically identified payments subject to Non-resident Withholding Tax, specific to the banking, insurance, and telecommunication industry.

This Overview summarises the following key components of the Amendment that are expected to have an impact on taxpayers:

- * Group Entities
- * Income from Illicit Activities
- * Non-resident Shipping or Aircraft Operators
- * Exempt Income
- * Permanent Establishments
- * Capital Gains/Losses
- * Banks
- * Tax Returns & Payments
- * Offshore Indirect Transfers
- * Non-resident Withholding Tax
- * Transfer Pricing
- * Controlled Foreign Entities

1. Income from Illicit Activities

Income received – whether in monetary or non-monetary form – from illicit activities are considered as a taxable income. The Amendment has broadened the definition of such income from illicit activities to include:

1

Money that lacks proof of origin/source – irrespective of whether it is accounted for in the books;

2

Investments and expenses which lacks proof of origin/source;

3

Assets which lack proof of origin/source

2. Group Entities

Prior to the passing of the Amendment, the Act only required group companies to apportion the MVR 500,000 tax free threshold between the companies in the group which were liable to income tax.

The Amendment refines the phrasing of the provision to address group entities and further defines an entity for the purpose of the said provision to include partnerships and any other entity that is not an individual or a bank.

Meaning, not only companies, but even partnerships operating in a group will be required to apportion the MVR 500,000 tax free threshold in accounting for income tax from the date of effect of the Amendment.

3. Non-resident Shipping or Aircraft Operators

With respect to income derived by non-resident shipping or aircraft operators in international transportation, the Amendment clarifies that such income will be taxable in the Maldives, only where the non-resident has a Permanent Establishment (PE) in the Maldives. This aligns the taxation of non-resident shipping or aircraft operators in the Maldives, with the established principles of the OECD and UN Model tax convention which addresses prevention of double taxation.

4. Exempt Income

The Amendment has introduced some noteworthy changes to the following types of income that are exempt from tax.

- * With respect to income derived by partners, the profits distributed by a partnership which is resident in the Maldives to its partners who are resident in the Maldives is considered as an exempt income. The Amendment adds **interest** on the partner's capital also as an exempt income.
- * In addition to the money received as basic pension and retirement pension under the Maldives Pension Act, the Amendment now includes **annuities** received under the Maldives Pension Act as an exempt income.
- * The Act broadly exempted payments received under a life insurance policy. However, with the coming into force of the Amendment, payments received under "**key person insurance schemes**" are excluded from this exemption.
- * The Act specifically exempted tax collected under Goods and Services Tax Act. Now the exemption is extended to cover **all taxes** collected under any Law.

4.1 Special Exemption

Notwithstanding any other provision of the Act, the Amendment also gives the President of the Maldives a discretionary power to grant income tax exemption on income received from specific projects or industries.

The specified project or industries to which the exemption is applicable will be determined by the President of the Maldives, in deliberation with the Cabinet Ministers and the same will be published in the Government Gazette. Such an exemption will only be granted for a specific duration and the following will be considered:

Impact on Government revenue;

Social benefits;

Likelihood of attaining the targeted goal by way of granting the exemption.

The Amendment also details additional conditions and procedures pertinent to the special exemption and provides the Ministry of Finance to publish a Regulation on the procedures to be followed in granting the special exemption to business projects, within three months from the date of effect of the Amendment.

4.2 Return Submission

The Amendment grants the Commissioner General of Taxation the discretion to entail any person subject to tax to submit the details of any exempt income specified under Section 12 of the Act along with their Income Tax Return.

5. Permanent Establishments

5.1 Head Office Expenses

In deducting head office expenses that is attributable to a PE in the Maldives, it is now established that the following types of expenditure cannot be deducted:

- * Royalty payments or fees pertained to patents or rights;
- * Commission paid in relation to management of the PE; or in relation to specific services provided to the PE.

5.2 Interim Payments

In the computation of the taxable income of a PE, Section 27(a) of the Act allows the PE to make an election to deduct the income for which non-resident withholding tax has been suffered (and therefore declare tax on a gross receipt basis). Hence, the Amendment makes it clear that where such an election is made, in the computation of interim payments of the respective PE, the amount of withholding tax suffered on such income cannot be deducted from the PE's interim payments.

5.3 Definition

Noteworthy changes brought to the definition of a Permanent Establishment is summarised below.

A building site, a construction, assembly or installation project or supervisory activities in connection with

Prior to the Amendment, a building site, a construction, assembly or installation project or its related supervisory activities were considered to encompass a PE, if such activities were carried out in the Maldives for a period exceeding **6 months**. The Amendment has reduced the period to **90 days**.

Additionally, to counteract arrangements intended to abuse the 90 days period through the practice of splitting up contracts between closely related enterprises, the definition now captures cases where a particular place of business would be used for very short periods of time by several similar businesses carried on by the same or related persons.

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Including fishing, extraction of natural resources or gaining monetary benefits from such resources

With the Amendment, extraction of natural resources or gaining monetary benefits from such resources, including fishing in the Maldives is considered to constitute a PE, if such activities continue within the Maldives for a period or periods aggregating more than 90 days in any 12 month period commencing or ending in the tax year concerned.

Under a Contract or an Agreement, the usage or installation of mechanical or scientific equipment

The Amendment clarifies that the usage or installation of mechanical or scientific equipment will be deemed to form a PE, if such activities are carried out for more than 90 days.

Agency PE [Dependent Agents]

If an agent on behalf of an enterprise habitually concludes contracts in the Maldives or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, such activities carried on behalf of the enterprise will trigger a PE of the enterprise in the Maldives

Where the contract is:

- * in the name of the enterprise, or
- * for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use, or
- * for the provision of services by that enterprise

In contrast, an 'independent agent' does not satisfy the PE definition. The ITA now acknowledges that where there is no special relationship between the two (such as a common ownership structure), the actions of the agent would not constitute a PE. For an agent to be independent for the purposes of the ITA, that person must:

- * have an independent status; and
- * act on behalf of other persons in the ordinary course of his business.



Example

TradesCo, a resident in Germany, is in the business of buying and selling equipment. SalesCo, a commonly owned company, resident in the Maldives, performs marketing and sales activities on behalf of TradesCo in the Maldives as a commissionaire. This means that SalesCo sells the equipment to buyers in Maldives and relies on TradesCo under a commissionaire agreement to satisfy the obligation to deliver the equipment to the buyers in the Maldives. SalesCo does not own the equipment at any point, nor does it have any entitlement to the amounts paid by the buyers for the equipment. However, on behalf of TradesCo, it concluded the sale of equipment in the Maldives.

In such cases, although TradesCo has no operations of its own in Maldives and makes no sales to customers in Maldives other than those made by SalesCo on its behalf, TradesCo will be deemed to have a PE in the Maldives. This is because SalesCo habitually concluded contracts in the Maldives on behalf of TradesCo for the sale of goods and SalesCo does not do so as an independent agent.

6. Capital Gains/Losses

The Amendment clarifies that no gains or losses can be taken into account in the computation of an individual's taxable income with respect to the types of income listed under subsection 30(e) of the Act, except as business income of that individual. Meaning, although capital gains or losses will not arise from any proceeds derived from the circumstances listed under subsection 30(e) of the Act, the individual may still have to include it in the computation of his total taxable income, where the proceeds constitute business income.

7. Banks

As practiced under the Bank Profit Tax regime which was abolished with enactment of the Income Tax Act, the Amendment now makes it clear that in the computation of a Bank's total taxable income, all amounts recovered out of the amounts previously deducted with respect to specific provisions for doubtful debts is required to be treated as income for the period in which such amounts were recovered

8. Tax Returns & Payments

8.1 Amending Tax Return

Previously, the Act broadly stated that where the Commissioner General believes that the self-assessed amount of the tax payable in a taxpayers return or amended return contains an error, the Commissioner General may correct the error and notify the person of the same. The Amendment revises the provision to denote that the Commissioner General may only correct **'arithmetic errors'** or **'typographic errors'** and inform the taxpayer of the same in writing along with reasons for correction.

8.2 Interim Return & Interim Payment

Prior to the enactment of the Amendment, the Act exempted taxpayers from filing the interim return and making the interim payments if the total amount of the interim payment payable was not more than MVR 20,000 OR the amount of tax payable for the previous year was not more than MVR 20,000.

With the Amendment, for taxpayers to be eligible for the said exemption, both conditions must be satisfied. Meaning, the exemption will be applicable if the total amount of the interim payment payable was not more than MVR 20,000 AND also the amount of tax payable for the previous year was not more than MVR 20,000.

In addition to the above, the Amendment also exempts taxpayers from the interim return filing and payment obligations if the taxpayer is exempt from filing the Income Tax Return for the tax year. This removes the previously put unnecessary administrative burden on employees who derived income solely

from one employer - although such employees were not required to submit an annual income tax return previously, an interim return had to be furnished twice a year declaring the same.

The Amendment ensures that for tax year 2021, anyone who is not required to submit an Income Tax Return will not be required to submit Interim Returns either. This includes employees deriving their only income from a single employer.

9. Offshore Indirect Transfers

The Amendment introduces a new withholding mechanism to tax offshore indirect transfers, with the purpose of safeguarding source taxation of specific transactions which often takes place outside of the Maldives. It captures income derived from the disposal of immovable properties situated in the Maldives and income derived from disposal of intellectual or intangible properties used or registered in the Maldives.

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9.1 The Withholding Mechanism

In relation to the transactions listed in the below table, the new provision stipulates that where a person makes a payment to a non-resident or to a party who is not evidently a resident in the Maldives for tax purposes (the recipient), the person making such payments (the withholding-agent), must deduct tax at the rate of 10% from the total amount of payment and pay such amounts to the MIRA.

Transactions covered under the new withholding mechanism:

1

Disposal of an immovable property situated in the Maldives.

3

Disposal of a share or any interest in a company or partnership or trust which is resident in the Maldives.

2

Disposal of a share or any interest in a company, partnership or trust, where at the time of disposal of such share or interest, during any time of the past 365 days, more than 50% of the value of company, partnership or trust is directly or indirectly related to an immovable property situated in the Maldives.

4

Disposal of an intellectual or intangible property used or registered in the Maldives or income derived under an agreement made in the Maldives for the disposal of such property.

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The withholding agent or the payer must pay the amount to the MIRA on the earlier of the following dates:

- * As a result of any of the listed transactions, the date on which the ownership of the specified asset is transferred to the withholding agent; or
- * The date on which the payment is made to the recipient.

The new provision also makes it very clear that, regardless of whether the withholding agent deducts tax from the total payment made to the recipient, it is the withholding agents' responsibility to pay the tax amount to the MIRA. Where the withholding agent fails to pay the tax amount to the MIRA as stipulated under the new provision, both parties (i.e. the withholding agent and the recipient of the payment) will be jointly held responsible for the amount of tax that should have been withheld from the total payment.

Also, in the case no tax is withheld by either the withholding agent or recipient of the payment by the income tax return filing deadline, the owner(s) of the immovable property that is being disposed of, will be required to pay tax at the same rate for the transaction in question.

10. Non-resident Withholding Tax

Under the Income Tax Regime, payments made to non-resident contractors have been subject to NWHT under Section 55(a) of the Act, at the rate of 10%. When the economic reality of the situation is considered, such non-resident contractors end up in a refund position with a presence of a PE in the Maldives - as they are allowed to submit a final income tax return and pay taxes on their net taxable income.

Hence, to address the challenges faced by such non-resident contractors doing business in the Maldives, the Amendment has **lowered the NWHT rate for payments made to non-resident contractors from 10% to 5%**.

In addition to the above, the Amendment also removes the NWHT previously imposed on reinsurance premiums at the rate of 3% and clarifies that the following payments will not fall within the categorically identified payment subject to NWHT under Section 55(a) of the Act:

- * Interconnection charges payable by telecommunication service providers; and
- * Bank commissions/charges in relation to deposits, transfers and card transactions.

Overall Changes to NWHT

Category	Prior to Amendment	Now
Reinsurance premium	Subject to NWHT at the rate of 3%	No longer taxed
Payments made to Non-resident Contractors	Subject to NWHT at the rate of 10%	Subject to NWHT at the rate of 5%
Interconnection Charges	Within the scope of Royalties	Clarified and removed from definition. No longer taxed.
Bank Commissions	Within the scope of Commissions paid in respect of services supplied in the Maldives	Clarified and removed from definition. No longer taxed.

10.1 Non-resident Withholding Tax Certificate

The Act states that where a person requests for a NWHT Certificate, the same must be provided to the person by the MIRA within 7 days from the date such a request was put forward.

The Amendment makes it clear that it is the responsibility of the payer of the payment (i.e., the person responsible to deduct NWHT), to ensure that the Certificate is provided. It is also stipulated that in the case the payer refuses to provide the Certificate to the person, the person may directly request the MIRA along with proof that such a request has been made.

11. Transfer Pricing

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Section 67 of the Act specifies circumstances under which taxpayers are required to compute their taxable income in accordance with the 'arm's length terms', irrespective of the actual arrangement or transactions.

In addition to the already established circumstances, for the purpose of the said provision, the Amendment specifies that in cases where an arrangement or transaction results in a one of the persons being afforded a higher tax credit compared to had the arrangement or transaction been carried out in arm's length terms, Section 67 of the Act will be applicable and such transactions will be brought to arm's length terms.

12. Controlled Foreign Entities (CFE)

To be considered as a CFE in the Maldives, 5 or fewer tax residents of the Maldives must have a controlling interest in the foreign entity. Prior to the Amendment, under the CFE rules, each shareholding resident of the Maldives was required to include the undistributed income of the CFE in its taxable income utilising the formula provided in the Act.

However, with the coming into force of the Amendment, not all shareholding residents of the Maldives are required to include the undistributed income of the CFE in its taxable income – only shareholding residents of the Maldives with a shareholding of 10% or more in the foreign entity is required to account for such income in its taxable income.

Contact us

If you have any specific questions relating to the guide, feel free to contact one of the following members of our team:



Zaina Zahir

Senior Associate

Zaina's practice covers a broad range of Maldives and cross-border tax matters, with a particular focus on the tax aspects of corporate acquisitions, transfer pricing, and resolution of disputes on related matters.

■ zaina@ctlstrategies.com



Madeeh Ahmed

Partner & Senior Tax Advisor

Madeeh is a chartered accountant and specialises in the tax aspects of the corporate undertakings and transactions that usually involve large and complex transactions that constitute the firm's major practice areas. Madeeh leads the firm's tax advisory practice.

■ madeeh@ctlstrategies.com

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ctlstrategies.com

8th Floor, H. Thuniya
Boduthakurufaanu Magu
Male' 20066, Maldives

ask@ctlstrategies.com

+960 795 6996



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