

# Newsalert \*

## Tax and Legal Services



Malta

31 October 2005

The measures announced tonight by the Prime Minister and Minister of Finance in the budget speech for 2006 include:

- A major reform to the taxation of gains on transfers of immovable property: introduction of a final withholding tax of 12% on property value (with no allowable deductions) instead of the current rates reaching up to 35% on the gains realised from the transfer
- Presentation of final report of Pensions Working Group
- Continuation of the Government's privatisation programme
- Introduction of a number of schemes to incentivise alternative energy generation equipment
- Setting up of an Aviation Register to attract foreign-owned airlines and other companies in the aviation industry and introduction of a Yachts Register
- More sustained drive against fiscal evasion and abuse of social services
- A cost of living increase of Lm2.25 per week; Lm1.67 for pensioners.

**This newsletter sets out a summary of these and of the other main budget measures. More details on the changes to tax legislation will be given as soon as the relative laws are published.**

## Overview Budget 2006

### CONSOLIDATED FUND 2005/2006

	2006	2005 (Revised)
	Lm (millions)	Lm (millions)
<b>Recurrent Revenue</b>		
Tax revenue	785	739
Non Tax revenue	166	174
<b>Total</b>	<b>951</b>	<b>913</b>
<b>Recurrent Expenditure</b>		
Personal emoluments	205	204
Programmes & initiatives	470	454
Contributions to Public entities	73	77
Maintenance expenditure	33	34
Interest on public debt	76	75
<b>Total</b>	<b>857</b>	<b>844</b>
<b>Recurrent Surplus</b>	<b>94</b>	<b>69</b>
Capital Expenditure	(149)	(145)
<b>STRUCTURAL DEFICIT</b>	<b>(55)</b>	<b>(76)</b>
<b>Consolidated Fund Balance - 1 January</b>	<b>(51)</b>	<b>(92)</b>
	<b>(106)</b>	<b>(168)</b>
<b>Financing</b>		
Local – Direct Loan Repayments	0	(3)
– Assets' Sales Proceeds	136	18
Net Contributions to Sinking Funds - local/foreign	(1)	(8)
Local Loans	0	110
	<b>135</b>	<b>117</b>
<b>Consolidated Fund Balance - 31 December</b>	<b>29</b>	<b>(51)</b>

### DOMESTIC ECONOMIC PERFORMANCE

#### Convergence programme

The programme targeted a deficit of 2.3% in 2006 equivalent to Lm50 million. This is now expected to reach Lm55 million representing 2.8% of GDP. Government is targeting a deficit of Lm50 million in 2007 and Lm34 million in 2008.

\* **connectedthinking**

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## Inflation

- For the year to September 2005 the inflation rate was 2.8%, up from 2.6% at the end of September 2004. The increase is mainly attributed to the increase in the price of oil. The annual inflation rate related to water, electricity, gas and fuels reached 18%. The inflation rate for 2006 is expected to reach 3.1%.

## GDP

- The forecasted economic growth for 2006 is expected to be 1.1% in real terms and 3.9% in nominal terms.

## Foreign Trade and Balance of Payments

- During the year imports of products and services amounted to Lm1,095.9 million while exports amounted to Lm1,088 million.

## The Labour Market

- At 30 September, the number of people registering for work amounted to 7,210 representing 5% of the labour force (the 30 September 2004 figure was 7,382 representing 5.1% of the labour force)
- The number of gainfully employed women increased by 1% over 2004 to 40,983
- The number of persons with a part-time employment as their main job was 23,138, an increase of 10.5%.

## Tourism

- Tourist arrivals for the period January to September 2005 reached 931,213, an increase of 1.2%
- Cruise passenger arrivals amounted to 217,281 representing an increase of 10.7%
- Gross income from tourism amounted to Lm204.7 million, representing an increase of 1.3%.

## Services

- Revenue generated from services, excluding tourism, increased from Lm449.6 million to Lm461.7 million

## Investment

- Investment in nominal terms increased by 7% - from Lm278.7 million to Lm298.4 million.

## Currency & Foreign Reserves

- Foreign reserves increased from Lm870.3 million to Lm911.7 million
- Continued Government preparations for introduction of the Euro as from 1 January 2008.

## Cost of living allowance

- The weekly cost of living increase for 2006 is Lm2.25
- For pensioners, the increase is Lm1.67 per week

- The above increases include 50 cents per week to compensate for the impact of the increase in energy costs.

## FISCAL MEASURES

### Income Tax- taxation of gains on transfers of property

- A final withholding tax of 12% of the value of property being transferred (with no allowances for expenses and other related deductions) is being introduced as from 1 November 2005
- On the basis of the current maximum tax rate of 35%, this final tax translates into a deemed profit margin of just under 35% of the value of the property being transferred
- The new final withholding tax is payable on a contract of sale in the same manner as the current provisional tax on capital gains
- The final withholding tax of 7% introduced in the 2004 budget speech remains applicable for disposals of property inherited prior to 25/11/1992
- No changes to existing exemptions on transfers of own residences, transfers on separations, sales by court orders and intra group transfers
- Persons transferring property until 31 December 2005, where the relative promise of sale has been registered or is in the hands of notaries by 20 November 2005 are entitled to opt to be taxed either under the old or the new rules.

### Other Fiscal Measures

- Review of taxation framework:** A commission is being appointed to carry out a review of the tax framework and to recommend incentives for generating employment and economic growth
- Incentivisation of alternative energy generation equipment:** A number of measures are being introduced in this sector, e.g. introduction of a refund of 25% (maximum of Lm500) on purchase cost of photovoltaic technology, no Enemalta charge on meter installation for operation of photovoltaic technology etc
- Motor vehicle registration tax:** Reduction of registration tax for new commercial vehicles exceeding 5 tonnes from 36% to 24%.

## PENSION REFORM

- The final report on the White Paper on Retirement Pension Reform was presented by the Pensions Working Group. It is being analysed by Government, which intends to take a decision soon.

# Overview Budget 2006

- The following is the key feedback received on the White Paper:
  - Maximum annual pensionable income of Lm6,750 no longer adequate
  - Difficult for a strict pension indexation to reflect corresponding increases in wages over the years
  - Most feedback agrees with raising of retirement age to 65 years subject to disagreement by a number of unions, and widespread concern on applying higher retirement age to some categories of workers, mainly manual
  - No general consensus on the changes proposed in the White Paper to the accumulation and calculation parameters of the two-thirds pension
  - Agreement on voluntary introduction of a second pillar private pension, but no agreement on mandatory introduction of such a second pillar private pension
  - Contributions should be solely directed to the funding of pensions.

## MEASURES AIMED AT CURTAILING ABUSE AND OPTIMISING USE OF PUBLIC RESOURCES

- **Health Services:** Reforms to introduce a pricing policy for pharmaceuticals, and strengthening organisational/audit capacities to prevent abuse
- **Social benefits:** Setting up of an inter-ministerial Working Group to make proposals to consolidate a means test mechanism for social benefits
- **Fiscal evasion:** Legislative changes will allow sharing of information between Tax Compliance Unit and Social Benefit Fraud Directorate so as to reduce tax evasion and abuse of social benefits. New rules will introduce mechanisms to reduce VAT receipt abuse and to subject the availability of loans from banks and financial institutions to the requirement of presentation of the contract of acquisition and fiscal receipts on works carried out
- **Excise Duty:** Introduction of a new tagging system for alcohol bottles in order to reduce the illegal importation of alcohol
- **Labour Market:** Intensification of enforcement of regulations to control employment in the black economy and temporary work.

## INITIATIVES

### Privatisation and Trade Liberalisation

- **Privatisation:** Government intends to continue the privatisation process, with strategic partners being sought for Maltacom, Bank of Valletta, Tug Malta, Maltapost and Kordin Grain Terminal, whilst the privatisation of yacht marinas is also under consideration
- **Trade liberalisation:** Liberalisation of the importation and distribution of energy products (including petrol, diesel and gas and production and distribution of Liquid Petroleum Gas (LPG)).

### Other

- **Information Technology and Communication:** Introduction of new programmes include launching of a set of e-Business road maps and an e-Learning Consortium
- **Environment:** Introduction of various programmes including continued rehabilitation of landfills and bring-in sites, investigation of possibility of land reclamation for property development, construction waste management etc
- **Maritime & Aviation Sector:** Amalgamation of Malta Maritime Authority and Department of Civil Aviation into a new Port Authority, and setting up of an Aviation Register to attract foreign-owned airlines and other companies in the aviation industry and introduction of a Yachts Register
- **Accrual Accounting:** Continuation of work on the introduction of accrual accounting within the public service and issuing of tender for the replacement of the existing Department Accounting System by a new financial management system
- **Industrial support:** Further support for Malta Enterprise, improvement of industrial zones, tax credits for new technology, back office, films etc
- **Golf courses:** Development of two additional golf courses, one in Malta and one in Gozo.

The notes are designed to keep readers abreast with financial and tax developments. They are not intended to be a definitive or comprehensive analysis of the subject and should not be acted upon without prior consultation with the Partners or Senior Consultants of the firm. For further details please do not hesitate to contact:

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