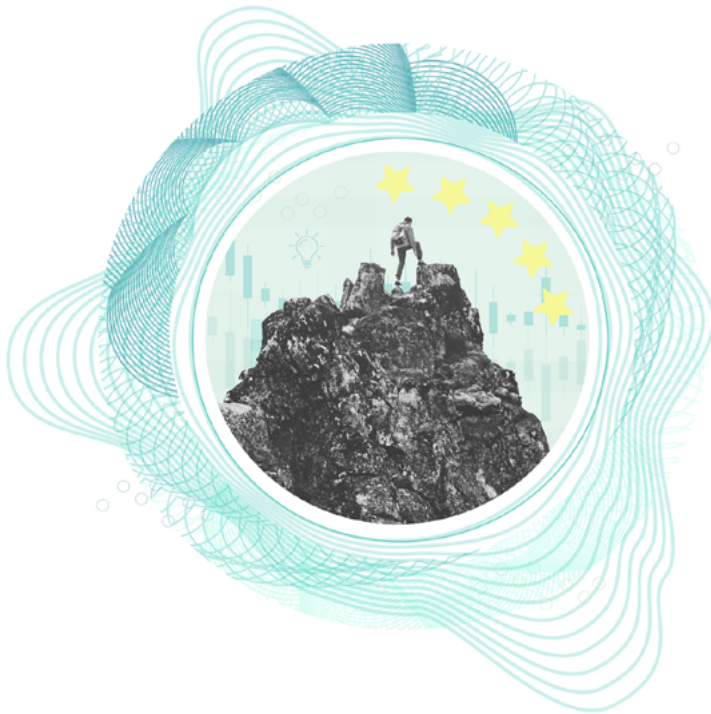


# The funds sector in Malta

## An overview

March 2023

# Introduction



Malta's legislation provides for the establishment of a wide variety of collective investment schemes ('**CISs**') which can be established through a number of corporate vehicles.

The single regulatory body responsible for financial services in Malta is the Malta Financial Services Authority (the '**MFSA**'). The MFSA regulates, licenses and supervises investment services providers and CISs. It also issues on a rolling basis several sets of targeted Investment Services Rules which establish the requirements and conditions applicable to both initial licensing (authorisation) and to license holders' on-going operations (supervision).

According to data published by the MFSA, as at the end of June 2022, there were 483 licensed funds domiciled in Malta, contrary to only five in 1995, whilst the number of funds registered in the list of Notified AIFs ('NAIFs') also continued to rise significantly in recent years. The aggregate net asset value ('NAV') of Malta domiciled funds

reached €21.2 billion in June 2022 with alternative investment funds ('AIFs') having the largest share at 70.5% followed by professional investor funds ('PIFs') at 15.6% and undertakings in collective investment of transferable securities ('UCITS') at 13.9%..

As of June 2022, 83.1% of Malta funds were managed domestically with 48.4% being managed by an external Maltese fund manager and 34.7% being self-managed. With regards to fund administration, in 2022, 90.7% of the investment funds were administered by a domestic fund administrator while the aggregate NAV of both domiciled and non-domiciled funds amounted to €23.9 billion in June 2022.

In December 2022, the MFSA released a consultation document on the proposed establishment of a framework for 'Notified Professional Investor Funds' ('NPIFs') to complement Malta's existing fund frameworks and to contribute towards Malta's attractiveness as a fund jurisdiction..

## CISs' corporate structure

CISs established in Malta may generally take any of the following corporate forms:

- Unit trust;
- Incorporated cell company;
- Limited partnership;
- Contractual fund;
- Investment company with fixed capital (INVCO); and
- Investment company with variable capital (SICAV).

The SICAV is the most commonly used vehicle for CISs in Malta due to its unique corporate features, particularly its flexible share capital structure, which at all times must be equivalent to the NAV of the scheme and in turn, which facilitates the issuance and redemption of fund units without lengthy corporate processes.

A SICAV may also be set up as an 'umbrella' or multi-fund company whereby the share capital may be divided into different classes of shares and where one class or group of classes of shares constitute a distinct sub-fund of the company. In this way, the scheme may operate a number of separate sub-funds having different investment objectives.

A SICAV may also be established as a cell company, enabling each sub-fund to be set up as a separate incorporated cell (IC) having separate legal and judicial personality from the other subfunds.

# Regulatory rulesets

The following is an overview of the regulatory rulesets applicable to CISs targeting non-retail investors.



## Alternative Investment Funds (AIFs)

More precisely, this ruleset refers to so-called 'full-scope AIFs', that is, those AIFs which are effectively, through their manager (hereinafter the '**AIFM**'), governed by the Alternative Investment Fund Managers Directive<sup>1</sup> ('**AIFMD**'), which seeks to create a harmonised framework for the management and marketing of non-UCITS funds throughout Europe. The transposition of the AIFMD in Malta was largely effected in 2013 by way of amendments to the Investment Services Act, Chapter 370 of the Laws of Malta (hereinafter the '**Investment Services Act**') and the various Subsidiary Legislation and Investment Services Rules issued thereunder.

In terms of the Investment Services Act, AIFs are generally defined as collective investment undertakings (including subfunds thereof) which:

- raise capital from a number of investors with a view to investing it in accordance with a defined investment strategy for the benefit of those investors; and
- do not require authorisation under the UCITS Directive<sup>2</sup>.

### AIFs' management structure

The AIFMD framework stipulates that AIFs may be managed either externally by an entity that is distinct from the AIF or internally by the governing body or internal resource within the AIF. In general, the main functions to be performed by the management of AIFs are portfolio management and risk management. In either case, the AIF must abide by the investment objectives, policies and restrictions outlined in its offering document.

The governing body of the AIF must (except in certain cases) be composed of no less than three members, with at least one being resident in Malta and all of whom must satisfy the MFSA's 'fit and proper' test on a rolling basis and must be independent from any custodian and other service providers of the AIF.

### Externally managed AIFs

An external AIFM of a Malta AIF may either have an established place of business in Malta or be a qualifying European AIFM. If established in Malta, it must be in possession of an Investment Services License and authorised by the MFSA as an AIFM in terms of the AIFMD.

The AIFM may manage more than one fund and may be authorised to carry out discretionary portfolio management services and non-core services involving investment advice, safe-keeping and administration in relation to the shares/units of CISs and the reception and transmission of orders with respect to financial instruments.

The initial capital requirement is set at a minimum €125,000 for AIFMs acting purely as such. Should the value of the portfolios of the AIFs under its management exceed €250m, the AIFM must provide an additional amount of own funds equal to

0.02% of the amount by which the value of the portfolios of the AIFM surpass the €250m threshold. In general terms, in order to be eligible for authorisation as an AIFM by the MFSA:

1. The MFSA must be satisfied that the AIFM will continue to meet its legal obligations;
2. The AIFM must demonstrate that it has sufficient capital and own funds to cover the possibility of surpassing the €250m threshold and to cover professional liability risk;
3. The AIFM's business must be carried out by persons of sufficient experience and good repute;
4. The qualifying shareholders must be suitable towards ensuring sound and prudent management of the AIFM; and
5. The AIFM's head office must be located in Malta.

<sup>1</sup>Directive 2011/61/EU as amended.

<sup>2</sup>Directive 2009/65/EC as amended.

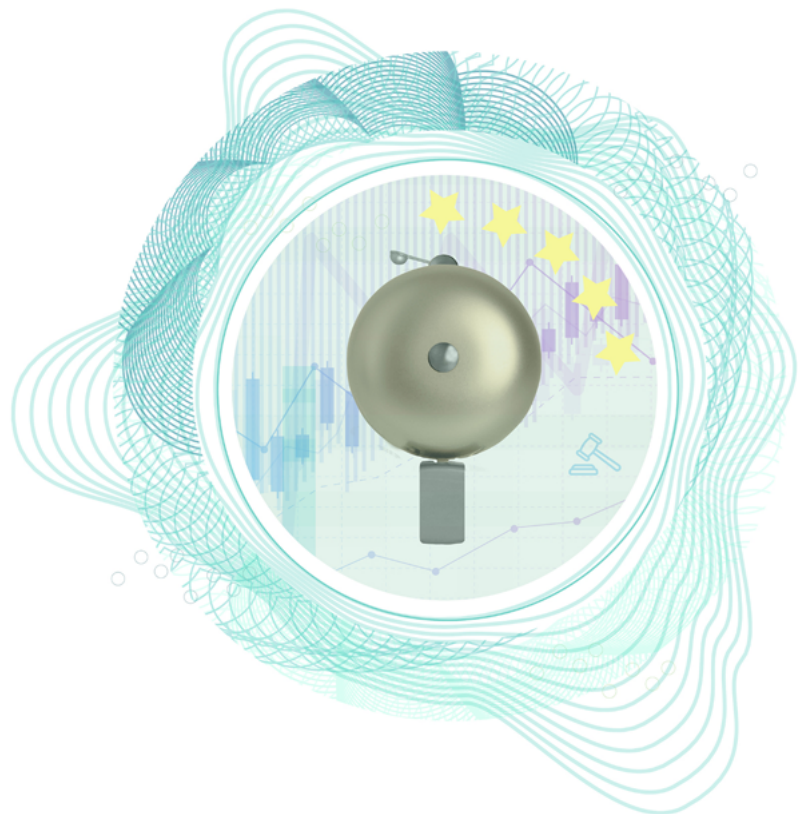
When applying for authorisation, an AIFM will also generally be required to submit certain information on both the AIFM itself and on the AIF/s it manages or intends to manage. This may include, inter alia, information concerning the AIFs' investment strategies, the rules or instrument of incorporation of the AIF/s, information on the persons conducting the business of the AIFM as well as the organisational structure of the AIFM.

Generally speaking, within three months of the submission of a complete application, the MFSA is required to inform an applicant for an AIFM license whether or not such authorisation has been granted. In certain cases, the MFSA may extend such time by another three months.

The AIF must appoint certain external service providers:

1. **A depositary**, who has an established place of business in Malta and is under duty to perform a) cash monitoring; b) oversight; and c) safe keeping.
2. Unless self-managed, an **AIFM** being a legal person duly authorised in terms of the AIFMD responsible for managing the AIF.
3. **An auditor**, who is independent, approved and subject to reporting requirements to the MFSA.
4. **A compliance officer**, who is responsible for the compliance function and for preparing a Compliance Report every six months.
5. **A money laundering reporting officer (MLRO)**, who is responsible for ensuring the AIF's compliance with its Prevention of Money Laundering obligations.

Furthermore, the AIF may choose to appoint certain other service providers as necessary.



### Self-managed AIFs

Self-managed AIFs are generally only permitted to engage in activities specifically related to the internal management (including administration and marketing) of that particular AIF and its assets, and in this respect must set up clearly segregated (functionally and hierarchically) portfolio and risk management functions.

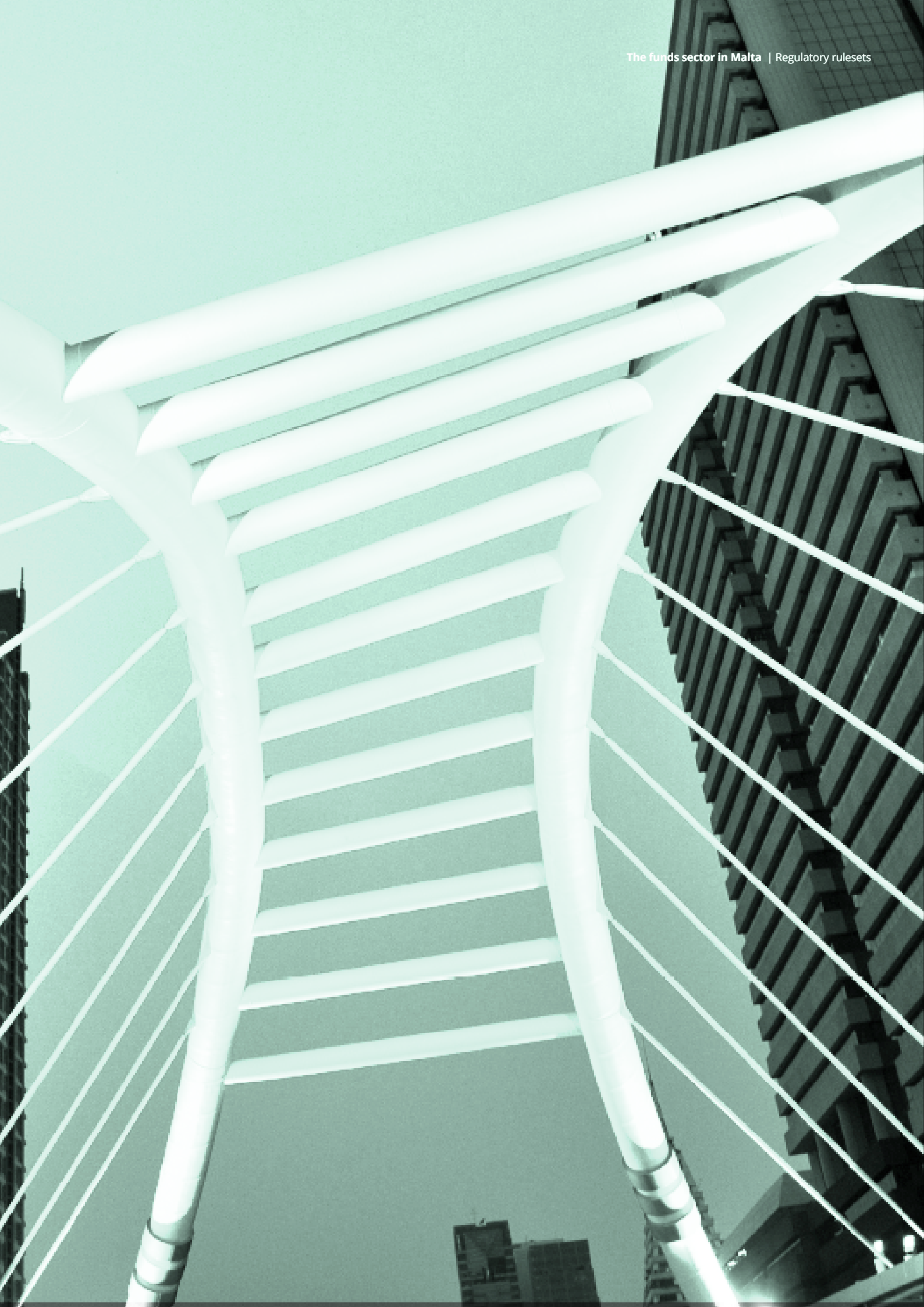
A self-managed AIF must have sufficient substance in Malta to be able to perform at least one of the aforementioned functions (i.e. either portfolio management or risk management) and must have initial capital of at least €300,000.

Beyond appointing certain mandatory external service providers, a self-managed AIF should appoint an **in-house investment committee** under the

responsibility of the board of directors, which must be composed of at least three members, one independent director and one Malta resident director. The investment committee is responsible for: a) the monitoring and review of the investment policy; b) establishing and reviewing investment guidelines; c) issuing rules for stock selection; d) setting up the portfolio structure and asset allocation; and e) making recommendations to the AIF's governing body.

In principle, for a self-managed AIF, the decision to grant or reject a license application should be issued by the MFSA within a period of three months (with the possibility of a three month extension) from the submission of a complete.







### The de minimis regime

The AIFMD framework allows for the application of a lighter or de minimis regime for 'small' AIFMs. De minimis AIFMs are managers, which directly or indirectly, have under their management fund portfolios whose assets collectively do not exceed the following amounts:

- Less than €100 million; or
- Less than €500 million, where the funds are unleveraged and have no redemption rights exercisable within a period of five years following the date of initial investment in each fund.

De minimis AIFMs having established their place of business in Malta must seek authorization by the MFSA as a de minimis license holder. Once authorised as such, de minimis AIFMs are generally exempt from complying with the provisions of the AIFMD except with regard to certain reporting requirements.

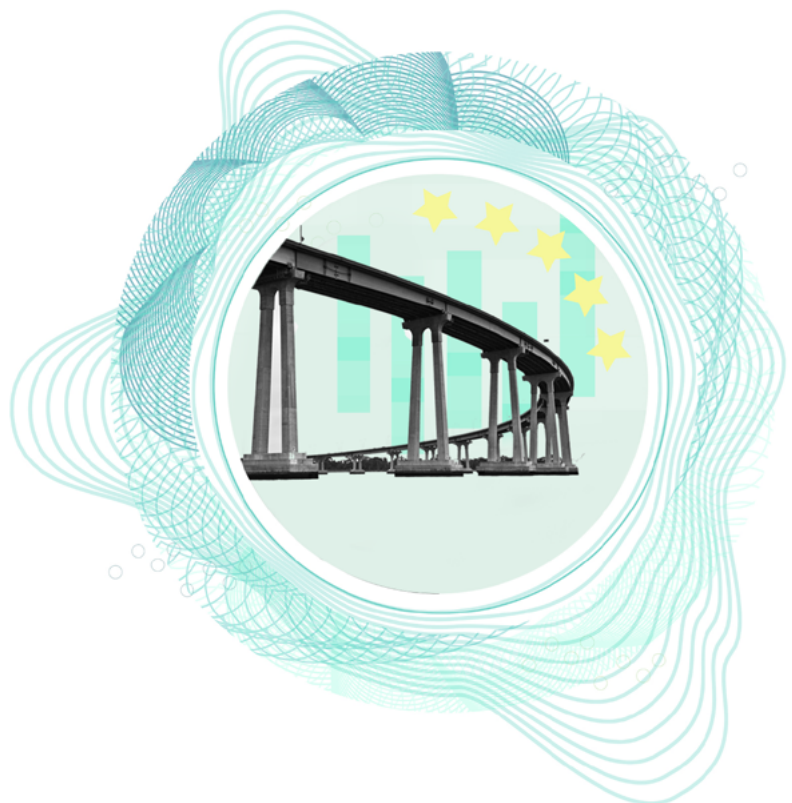
In addition, under this lighter regime, de minimis AIFMs are not eligible to make use of the EU passporting rights under the AIFMD described below. However, in the event that such AIFMs would wish to benefit from such passporting rights, they may choose to opt-in under the AIFMD, and in turn become subject to all the obligations applicable to full-scope AIFMs.

### EU passporting

The AIFMD confers an EU-wide marketing passport to full-scope AIFMs to market any AIFs under their management to professional investors across the EU. Under the EU passporting framework:

- Units or shares of European AIFs may be marketed by a Maltese AIFM in Malta;
- Units or shares of European AIFs may be marketed by a Maltese AIFM in another
- EU or EEA member state other than Malta; and
- Units or shares of European AIFs may be marketed by a European AIFM in Malta.

Maltese AIFMs wishing to obtain a marketing passport must file an application with the MFSA, which must, in turn, transmit the notification to the competent authority of the respective state and provide the AIFM with a response within 20 working days from receipt of the complete notification file.



### Professional investor funds (PIFs)

The PIF regime is a local regime governed by the Investment Services Act and the Rules issued thereunder. PIFs are another special class of non-retail collective investment scheme, broadly similar in character to AIFs but which are generally subject to a more light-touch regulatory framework. PIFs are designed to target so-called 'qualifying investors' and are generally more flexible and are not subject to any investment or borrowing (including leverage) restrictions unless when investing in immovable property or through loans. This notwithstanding, PIFs (as well as AIFs) must always abide by the investment objectives, policies and restrictions outlined in their offering document.

The inherent flexibility and limited restrictions applicable to PIFs (compared to AIFs) emanate from the fact that PIFs must, necessarily, fall under the de minimis regime (described above). As such, generally speaking, a PIFs asset value should be either less than EUR 100 million when leveraged or less than EUR 500 million when unleveraged and having a lock-in period of five years.

It should also be noted that, as PIFs fall under the de minimis regime, they are generally not able to benefit from the EU passporting rights provided under the AIFMD.

The Maltese regulatory framework provides for a process whereby a fund registered under the PIF regime may convert into a full-scope AIF. This would generally occur when the assets under management of the fund (or, more precisely, the relevant fund manager) exceed the de minimis thresholds described above.

### The PIFs' management structure

The board of directors as the governing body of a PIF is required to be composed of no less than three directors with at least one being resident in Malta. All directors must satisfy the MFSA's 'fit and proper' test on a rolling basis and any changes in the composition of the board must be communicated to the MFSA.

PIFs can also be either externally managed by a third-party entity or be self-managed by an internal resource. PIFs must appoint certain external service providers (similarly to AIFs), those being:

01. An auditor;
02. A compliance officer; and
03. A money laundering reporting officer (MLRO)

PIFs may choose to appoint certain other service providers such as a Depositary (not being mandatory as in the case of AIFs).

### Self-managed PIFs

In a self-managed scheme, the discretionary management of the PIF's assets is vested in the board of directors, which must prove to the MFSA that the PIF is capable of organising and controlling its affairs in a responsible manner and that it has adequate operational, administrative and financial procedures and controls to ensure compliance with all regulatory requirements.

The board is also required to appoint an investment committee similarly to self-managed AIFs, which must be composed of at least three persons (one being resident in Malta) and will be responsible for the day today investment management of the fund's assets in line with its investment policy.

The initial capital requirement for self-managed PIFs is set at €125,000.

### Externally managed PIFs

Where an external manager is appointed, such manager may or may not have an established place of business in Malta. Should the manager be based in Malta, it must be duly licensed and authorised by the MFSA and must hold an appropriate Investment Services License.

If established outside Malta but falling under the AIFMD framework as an authorised EU de minimis AIFM, the fund manager may provide fund management services without any additional requirements imposed by the MFSA provided it is compliant with AIFMD rules in its home state.

In any other case, the fund's manager must undergo a 'fit and proper' test by the MFSA in order to ascertain whether it possesses the necessary business organisation, systems, and the required experience and expertise to act as manager.

### Licensing process for AIFs & PIFs

The licensing process varies considerably depending on the fund authorisation being sought and the specifics of the contemplated fund, however it is generally divided into three phases:

- Intention phase: This would typically commence with the submission of a statement of intent ('Sol') followed by preliminary meetings with the MFSA and information collection and if successful would culminate with communication by the MFSA of a 'no objection' to submit the application;
- Pre-authorisation phase: This would typically commence with the submission of the application and payment of the relevant application fees. In turn the MFSA will carry out a due-diligence assessment and review the submitted application and accompanying documentation. If successful, this phase would conclude with the issuance of an 'in principle' approval by the MFSA;
- Authorisation phase: Once all preauthorisation requirements have been fulfilled to the satisfaction of the MFSA, authorisation should be granted in the form of the issuance of an authorisation letter and a certificate of authorisation and certain post-authorisation requirements may be specified.



### Notified Alternative Investments Funds (NAIFs)

Malta was amongst the first countries to adopt a notified framework across the EU in late 2016. The Notified AIF framework aimed at providing AIFMs with a quick time-to-market for the establishment of their funds, coupled with the ability to market them within the EU in terms of the AIFMD passporting regime.

In terms of the Investment Services Act and the Rules issued thereunder a fund may generally be eligible for notification as a NAIF if the following conditions are satisfied:

1. the NAIF is promoted to professional / qualifying investors only;
2. the NAIF is managed by a full-scope AIFM authorised and licensed in terms of the Investment Services Act or by an EU AIFM being in possession of a management passport under the AIFMD (and therefore may not be self-managed);
3. the board of directors of a NAIF is to be composed of at least three members, one of whom must be resident in Malta;
4. at least one of the directors of the NAIF is independent from the AIFM, the custodian, the promoter and all other service providers appointed;
5. the AIFM assumes responsibility for that NAIF.

As a result, NAIFs are not subject to the formal three phase licensing process by the MFSA and are generally not subject to restrictions on the types of financial instruments they invest in. Furthermore, as is the case with all licensed AIFs, a NAIF should be eligible to make use of the EU passporting.

The AIFM of a NAIF is responsible for selecting the NAIF's service providers and must ensure that each service provider

is competent, qualified and capable of providing the services for which it was appointed. The NAIF may appoint service providers as it deems necessary. However, it is at least required to appoint an administrator, a depositary, an auditor and an MLRO. The AIFM also has an ongoing obligation to carry out due diligence on the members of the NAIF's governing body and its service providers. This due diligence obligation is to be satisfied prior to the submitting of the notification pack as well as at end of each financial year at a minimum.

#### The notification procedure

The AIFM must submit a notification pack to the MFSA within 30 days of the governing body of the NAIF approving its Prospectus. The same process applies in the case of notification of sub-funds of the NAIF. The notification pack must include:

- The prospectus;
- A Resolution of the NAIF's governing body certifying that the prospectus is drafted in accordance with the pro forma template and includes the minimum required content;
- A self-certification by the AIFM that, having regard to any delegate manager(s) or advisers it has in place, it has the necessary competence and experience to manage the AIF and monitor effectively any delegate;

- A joint declaration by the AIFM and the NAIF's Governing Body, whereby each undertakes responsibility for the NAIF, including, inter alia, the obligations arising under the AIFMD; and
- A declaration by the AIFM confirming that it has carried out the necessary due diligence regarding the service providers of the NAIF and the governing body of the NAIF. This declaration must include a statement that the AIFM is satisfied with the outcome of this due diligence exercise.

Within 10 working days from the date of submitting a duly completed notification pack, the MFSA should proceed to including the AIF in the List of Notified AIFs following which the NAIF is permitted to commence business. In case of any amendments to the NAIF's prospectus, these will need to be communicated to the MFSA within 30 days of the governing body approving the amended prospectus.





### Taxation of CIS

For the purposes of the Income Tax Act (Chapter 123 of the Laws of Malta) ('ITA'), the term 'CIS' is generally defined as "any scheme or arrangement which is licensed under the Investment Services Act".

The income of a CIS licensed in Malta is generally exempt from tax in Malta unless such income derives from immovable property situated in Malta and unless such income qualifies as 'investment income' derived by a 'prescribed fund'.

A prescribed fund is generally defined as a Malta-based scheme that:

- holds at least 85% of the value of its total declared assets in Malta; and
- is classified as prescribed fund by the Commissioner for Revenue ('CfR') by notice in writing.

Therefore, the Malta tax treatment of CISs generally depends on their classification as 'prescribed' and 'non-prescribed' funds in terms of the Income Tax Act as any qualifying

'investment income' derived by a prescribed fund is generally subject to a withholding tax at source, in the amount of 10% or 15% depending on the classification of the income.

All other funds not meeting the above definition should generally qualify as non-prescribed funds and their income should be exempt from tax in Malta to the extent it is not derived from immovable property in Malta. In all cases, income from immovable property situated in Malta is subject to the standard corporate rate of taxation applicable in the circumstances.



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