

act



## VAT and income tax treatment of yacht leasing

Photo by Keith Buhagiar

### Value Added Tax Implications

Yachting is an ever-growing industry in Malta. The Maltese VAT Department has issued guidelines, whereby the overall VAT rate incurred on the acquisition of a yacht can be reduced substantially depending on the size and means of propulsion of the yacht.

A leasing agreement has to be entered into by the lessor (the owner of the yacht) whereby he contracts the use of the boat to the lessee for a consideration which should be at arm's length. At the end of the lease agreement, the lessee may opt to purchase the boat at a percentage of the original price. At the end of the lease agreement, the lessee will become the owner of an EU vat paid yacht registered in Malta.

### Conditions

In order to benefit from the yacht leasing guidelines, a number of conditions must be satisfied:

- the owner of the yacht, i.e. the lessor, must be a company incorporated in Malta with a valid Malta VAT identification number.
- the lessee may however be a Maltese or foreign individual or company.
- the lessor and the lessee must enter into a yacht leasing agreement for a period not exceeding 36 months.
- the lease agreement must provide for the first lease installment to amount to 50% of the value of the yacht, and the lessor must effectively make a profit on the lease contract.
- the boat must come to Malta, possibly at the beginning of the lease agreement or alternatively at the time when the purchase-option is exercised; the presence of the yacht in Malta at one of these times is a condition imposed by the VAT Department and cannot be waived.
- prior approval shall be sought in writing from the Director General VAT who is to confirm the rate applicable according to the use in EU territorial waters (depending on the size and propulsion of the yacht), as well as the acceptability of the value of the yacht as declared. For this purpose a valuation certificate of the yacht shall be submitted with the application for approval.
- any purchase value at the end of the lease agreement shall not be less than 1% of the original value of the yacht, and this will be subject to the standard rate of VAT at 18%
- the Malta Company makes at least 10% profit out of the transaction.

### Acquisition of the Yacht

The VAT treatment upon acquisition of the yacht by the Malta Company will depend on whether the yacht is acquired locally, acquired from another EU Member State, or imported into Malta from a third country. In any of these three situations, any VAT due would be refundable on the basis that the yacht is being used for the economic activity of the lessor.

If proof of VAT relating to the vessel is required, a document may be provided upon request by the VAT department as proof that the purchase of the vessel has been declared for VAT purposes in Malta. When the yacht is sold to third parties, Maltese VAT will then be charged which is calculated on the consideration paid for the acquisition of the yacht.

### Lease of the Yacht

The lease of the yacht is considered to be a supply of services taking place in Malta where the yacht is actually put at the disposal of the customer provided the lessor is established in that same place. Thus, where the yacht is put at the disposal of the customer in Malta, i.e. the same place where the supplier is established, the place of supply will be Malta.

### ➤ Calculation of VAT due on leasing

In view of the difficulties in determining the exact period of time which the yacht spends inside and outside EU territorial waters, the yacht leasing guidelines provide that VAT will only be due on a percentage of the lease based on a presumption as to the time that a yacht is to be within EU territorial waters. These percentages are set according to the length of the boat and its means of propulsion (power or sailing). The standard rate of VAT of 18% is applied on the established percentage of the lease, deemed to be related to the use of the boat in EU territorial waters. The table below indicates the established percentage portions according to the type of boat.

Type of boat	% of lease taking place in EU	VAT computation	Effective VAT rate
Sailing boats or motor boats over 24 metres in length	30%	30% of consideration x 18%	5.40%
Sailing boats between 20.01 to 24 metres in length	40%	40% of consideration x 18%	7.20%
Motor boats between 16.01 to 24 metres in length	40%	40% of consideration x 18%	7.20%
Sailing boats between 10.01 to 20 metres in length	50%	50% of consideration x 18%	9.00%
Motor boats between 12.01 to 16 metres in length	50%	50% of consideration x 18%	9.00%
Sailing boats up to 10 metres in length	60%	60% of consideration x 18%	10.80%
Motor boats between 7.51 to 12 metres in length			
(if registered in the commercial register)	60%	60% of consideration x 18%	10.80%
Motor boats up to 7.5 metres in length (if registered in the commercial register)	90%	90% of consideration x 18%	16.20%
Boat permitted to sail in protected waters only	100%	100% of consideration x 18%	18.00%

This means that the standard rate of VAT at 18%, is only charged on the percentage of the lease payments. Thus for example a sailing boat that is over 24 metres in length is deemed to be used for 30% of the time in EU territorial waters and 70% outside such waters. Maltese VAT would be chargeable by the lessor to the lessee on 30% of the value of the monthly lease payments.

The VAT Department will issue a VAT paid certificate in the name of the Lessee, as owner, indicating that VAT has been paid in full. Further conditions may be imposed by the VAT Department.

#### Illustration

Mr. Smith sets up a company in Malta (lessor) to buy a 25 metre pleasure yacht from a UK supplier. The market value of the yacht is €1,000,000. The company enters into a lease agreement with Mr. Smith (the lessee) whereby he agrees to pay 50% of the value of the yacht on the date of the lease agreement. The lessee can also be another Malta company. The duration of the lease agreement is for a 36 month period. The rest (€500,000) plus a 10% profit (€100,000) will be paid in equal monthly installments over the duration of the lease agreement i.e. €16,667.

The lessee has the option to buy the boat at the end of the lease agreement at a price which is 1% of the original value of the yacht i.e. €10,000.

The VAT implications are as follows:

No VAT implications on the purchase of the yacht by the lessor from the UK supplier.

VAT due on payment of 50% deposit =  $50\% \times €1,000,000 \times 30\% \times 18\% = €27,000$

VAT due on the 36 monthly installments =  $€16,667 \times 36 \text{ months} \times 30\% \times 18\% = €32,400$

VAT due on the purchase of the yacht at the end of the lease agreement (optional) =  $€10,000 \times 18\% = €1,800$

Total VAT paid is €61,200 i.e. VAT rate is of 6.12%

#### Income Tax Implications

Where leasing arrangements of yachts is deemed by the Director General (VAT) to be in accordance with guidelines issued by the VAT department, the following tax treatment is to be adopted for each year for the duration of the lease:

- the lessor is charged to tax only on the annual finance charge, namely the difference between the total lease payments less the capital element divided by the number of years of the lease;
- the lessee is allowed a deduction in respect of (i) the finance charge; (ii) maintenance; (iii) repairs; and (iv) insurance;
- the lessee is allowed capital allowances in respect of the yacht and the parties may not opt to shift the burden of wear and tear onto the lessor;
- where the lessee exercises an option to purchase the yacht on the termination of the lease, the purchase price received by the lessor shall be considered to be of a capital nature and no tax thereon shall be payable by the lessor.
- A Malta Company will be subject to tax at the corporate rate of tax of 35%. Upon distribution of a dividend to the shareholders of the Malta Company, a refund of tax will be due. The refund is paid to the shareholders of the company and will amount to 6/7ths of the tax paid by the Malta Company, resulting in a net tax leakage in Malta of 5%.

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