



# LEGAL FRAMEWORK ANALYSIS

## NATIONAL REPORT: MALTA

### ICA-EU PARTNERSHIP



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## I. Introduction

Cooperatives benefit from regulations that acknowledge their specificities and ensure a level playing field with other types of business organisations. The research falls within the scope of the knowledge-building activities undertaken within the partnership for international development signed in 2016 between the European Commission and the International Cooperative Alliance (ICA), which aims to strengthen the cooperative movement and its capacity to promote international development worldwide. It demonstrates that the absence of a supportive legal framework for cooperatives, or the presence of a weak or inadequate legal framework, can negatively impact cooperatives and their evolution. In contrast, the existence of supportive regulations can foster cooperatives' creation and strengthening, acting as a driver of sustainable development. For this reason, further knowledge and evaluation of cooperative legislation will become a tool for ICA members, cooperators worldwide, and other key stakeholders such as policymakers and cooperative legal scholars. With greater knowledge and access to a global, country-based legal framework analysis, ICA members can advance their advocacy and recommendations on the creation or improvement of legal frameworks, document the implementation of cooperative legislation and policies, and monitor their evolution.

The main objectives of the legal framework analysis are to:

- provide general knowledge of the national cooperative legislation and of its main characteristics and contents, with particular regard to those aspects of regulation regarding the identity of cooperatives and its distinction from other types of business organizations, notably the for-profit shareholder corporation (the *sociedad anónima lucrativa* in Spanish; the *société anonyme à but lucratif* in French).
- evaluate whether the national legislation in place supports or hampers the development of cooperatives, and is therefore “cooperative friendly” or not, and the degree to which it may be considered so, also in comparison to the legislation in force in other countries of the ICA region (or at the supranational level).
- provide recommendations for eventual renewal of the legal frameworks in place in order to understand what changes in the current legislation would be necessary to improve its degree of “cooperative friendliness”, which is to say, to make the legislation more favourable to cooperatives, also in consideration of their specific identity.

This report was written by Dr. Antoine Naudi, a founding partner of Naudi Mizzi & Associates. He graduated with a Doctor of Laws from the University of Malta and was admitted to the bar in 1995. He possesses a post graduate Masters in Financial Services, a Diploma in Taxation Studies and has successfully completed the MFSA/IFSP First Certificate in Trusts law and Management and the MFSA/IFSP Foundation Certificate in Trusts law and Management – “The International Aspects of Trusts and Companies”.

His practice focuses mainly on civil and commercial matters, company law, taxation and

litigation. He acts for many local and international corporate clients and has been a speaker at various seminars on company legislation and co-operative society legislation. He served as a councillor for the Sliema Local Council between 1993 and 1998. He is also an appointed Arbitrator with the Malta Arbitration Centre for matters concerning cooperative societies and a member of the Administrative Review Tribunal. He is a member of the Corporate Tax Alliance. He also served as a member of the Executive Board of the European Law Firm between 2015-2018.

His involvement with cooperative societies dates back to 1995 and he is currently the legal advisor of Koperattivi Malta – Malta's apex organisation and an ICA member – as well as of several cooperative societies on the island. In preparation of this report, support and coordination was provided by staff from Cooperatives Europe and the ICA.

## II. National cooperative law: Malta

### i. General context

The constitution, registration and control of cooperative<sup>1</sup> societies in Malta, including matters connected therewith or ancillary thereto, is primarily regulated by the Co-operative Societies Act [Chapter 442 of the Laws of Malta]<sup>2</sup> – hereinafter referred to as the “Act” -- together with subsidiary legislation enacted from time to time. There are no specific laws applicable to any particular sector of cooperatives. In fact, apart from the main Act itself, the following regulations have been enacted and are still in force:

**Table 1 “List of regulations”**

<u>Name of the Regulation</u>	<u>Legal notice</u>	<u>Date of entry into force</u>	<u>Last amendment to the Regulations</u>
Co-operative Societies (Rate of Dividend on Share Capital) Regulations	LN 35 of 1990	9 March 1990	N/A
Central Co-operative Fund Regulations	LN 344 of 2016	21 October 2016	LN 81 of 2019

<sup>1</sup> Maltese law refers to “co-operatives” as opposed to “cooperatives”. For the purposes of this paper, the author will however make reference to cooperatives to ensure uniformity with other national reports prepared.

<sup>2</sup> This is also referred to as Act XXX of 2001 which had replaced the Co-Operative Societies Act of 1978.

Co-operative Societies (Establishment of Administrative Penalties and Sanctions) Regulations	LN 115 of 2003	1 December 2003	LN 215 of 2020
Co-operative Societies (Levying of Fees) Regulations	LN 198 of 2003	1 October 2003	LN 426 of 2007
Employee Involvement (European Co- operative Society) Regulations	LN 48 of 2007	9 March 2007	LN 427 of 2007

The Constitution of Malta mentions cooperative societies very briefly in Article 20 wherein it is stated:

*“The State recognises the social function of co-operatives and shall encourage their development”.*

Other enactments also refer to cooperative societies.

The Income Tax Act [Chapter 123 of the Laws of Malta] makes reference to cooperative societies in a somewhat odd manner. Section 2 of the Income Tax Act – the definition section – includes a cooperative society under the umbrella definition of a company for the purposes of tax legislation when it states:

*“any co-operative society duly registered as such under the appropriate law for the time being in Malta”*

and further defines a “dividend” as:

*“any distribution made by a co-operative society to its members and any amount credited to them as members, including any patronage refund, bonus certificate or bonus share, made, paid or allotted in accordance with the law regulating such societies for the time being in force in Malta”*

Section 12 (1)(q) of the Income Tax Act exempts the income of a cooperative society from the payment of income tax.

The Income Tax Management Act [Chapter 372 of the Laws of Malta] refers to cooperative societies in Section 19 (4)(b) when it indicates the documents which the Commissioner for Revenue expects every cooperative society to prepare and maintain.

The Maltese Civil Code [Chapter 16 of the Laws of Malta] also mentions cooperative societies once in Section 48 (1)(e) of the Second Schedule, Title III Subtitle III which deals with associations established as private benefit organisations.

It is interesting to note that the Maltese Commercial Code [Chapter 13 of the Laws of Malta] and the Maltese Criminal Code [Chapter 9 of the Laws of Malta] make no mention of cooperative societies.

## ICA Principles in the law

The ICA Principles of cooperative identity are explicitly spelt out in Section 21 (2) of the Act. They are therefore part and parcel of our law, but the legislator included a further subsection (3) which states that these principles are **not** directly enforceable in any court or tribunal but shall be adhered to in the interpretation and of the Act and any regulations made thereunder.

## ii. Specific elements of the cooperative law

### a) Definition and objectives of cooperatives

Although there is no definition of the term “cooperative society”, the Act defines a “society” as a cooperative society registered or provisionally registered under the Act which includes a primary society, a secondary society and a tertiary society. However, Section 21 (1) of the Act states:

*“A society is an autonomous association of persons united voluntarily to meet their economic, social and cultural needs and aspirations, including employment, through a jointly-owned and democratically-controlled enterprise, in accordance with co-operative principles, and which, subject to the provisions of this Act, may be registered by the Board as a co-operative society under this Act.”*

This is the closest one gets to a definition of a cooperative society in Malta.

It is rather difficult to define the main legal characteristics which distinguish cooperatives in Malta from other legal types of business organisations in the country as this would require an entire thesis on the subject matter. Suffice it to say that if one compares cooperative societies to a limited liability company (which is the most common type of entity used in Malta to carry out business), some of the main distinguishing non-exhaustive characteristics can be categorised as:

- Regulated by the Act as opposed to companies which are regulated by the Companies Act, 1995;
- One vote per member as opposed to voting according to the number of shares held in a company;
- Fair distribution of revenue, usually based in proportion to transactions, as opposed to a distribution based according to dividend policies in companies;

- Based on the ICA principles as opposed to companies which are set up to maximise their profits;
- Restrictions on the setting up of subsidiary companies as opposed to companies which do not have similar restrictions;
- Provisional registration is possible unlike the situation with companies;
- Cooperatives are exempt from the payment of tax unlike companies.

Ultimately, however, it is the adherence to the seven ICA cooperative principles which makes cooperatives different from other forms of business.

Whilst there is no ad hoc provision in the law which assigns to cooperatives the purpose of promoting their members, Section 21 (1)<sup>3</sup> of the Act seems to point in this direction and even the margin note in the law is entitled “Promotion of economic and other interests”. Whilst this “promotion” would at first glance seem to be the promotion of cooperative societies in general, there can be no doubt that the ultimate beneficiaries of any such promotion are the members themselves. It is indeed very common to find a clause in the statutes of cooperative societies registered in Malta which actually spells out the obligation of the cooperatives to promote the interests of their own members.

Save as explained hereunder, the issue as to whether members of a cooperative society have an obligation to make use of the services of the same cooperative finds no response in the law. One would typically expect members to make use of the services or acquire products from the same cooperative society of which they form part as they would normally benefit from lower prices being charged. There is however no direct provision in the law which imposes such an obligation on members. Having premised this, in terms of Section 40 (1) of the Act, a cooperative society whose principal activity consists in the sale or purchase or the provision of any goods and, or, services, may provide in its statute, or may otherwise contract with its members, that:

- every such member who produces such goods or provides such services shall dispose of, or otherwise arrange for the disposal of, the whole or any specified amount or proportion, of such goods or services to or through the society in conformity with any agreement entered into or arrangement made between the society and any third party;
- every such member shall purchase from the society the material required by the member for the purpose or in connection with the production of such goods or the provision of such services, in whole or in any specified amount or proportion thereof, from the society.

Any such rules and obligations, if included in the statute, shall be directly related, necessary and proportionate to the formation and proper functioning of the society and compatible with the provisions of the Competition Act [Chapter 379 of the Laws of Malta].

It is not uncommon for cooperatives to carry out transactions with non-members or to employ persons who are non-members as this generally has the effect of enhancing and increasing the volume of business of the cooperative, thereby promoting the financial

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<sup>3</sup> supra

wellbeing of the cooperatives' members. There are no limitations imposed by law. The statute of a cooperative society could of course always impose certain limitations agreed upon by the members at a general meeting. The law does not prohibit cooperatives from acting in the interest of non-members or the community at large. Likewise, the law does not forbid a cooperative from carrying out any economic activity provided that such activity is not in contravention of any legislation.

## b) Establishment, cooperative membership and governance

The Co-operatives Board [hereunder referred to as the "Board"], set up in terms of Section 3 of the Act, is the statutory body having a distinct legal personality which, among other things, is responsible for the registration, monitoring and supervision of cooperatives societies in Malta. It has an obligation to 'keep or cause to be kept at its office a Register of C-operative Societies', together with 'other registers, statistics or documentation on societies as it may deem appropriate from time to time.'<sup>4</sup> Such a register is open to inspection by the public following payment of any applicable fees. It is interesting to note that cooperative societies which are set up in accordance with cooperative schemes developed by Government for public employees are actually registered in a separate register clearly identified for this purpose.

There can be three types of cooperative societies registered under the Act. Primary societies - in which the majority of the members are individual persons; secondary societies - in which the majority of the members are themselves primary societies; and tertiary societies - in which the majority of member are themselves primary and, or, secondary societies. The national expert highlights this distinction as the minimum number of members seeking to register a cooperative varies according to the type of cooperative society. In the case of primary societies, one needs to have at least five founding members. Secondary societies require at least two primary societies as members, whilst tertiary societies require at least two societies of which one is a secondary society.

It is important to note that if the number of members falls below the statutory minimum, the Board may, of its own motion, make a dissolution order in respect of a cooperative society. There is no time frame stipulated which allows the Board ample discretion as to when it may invoke this measure.

All cooperative societies need to be registered in order to exist. Registration can take two forms – a provisional registration or a full registration. The Board may consider that a proposed cooperative society should not be registered at the time of its application for registration but may also be of the opinion that steps can and will be taken by the founding members to comply with the conditions for registration. In such instances, the Board may provisionally register the cooperative for a period not exceeding 18 months. During this period, the Board can either cancel the provisional registration or grant the cooperative a full registration status.<sup>5</sup> If the Board is satisfied that at application stage,

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<sup>4</sup> Section 10 of the Act.

<sup>5</sup> Provisional registration provisions are found in Article 28 of the Act.



the founding members are compliant with the provisions of the Act, the Board will grant full registration status to the cooperative society.

In either case, the Board issues a certificate of registration which is conclusive evidence that the society is duly registered either provisionally or permanently.

The main requirements to apply for registration include an application set out in the Act which needs to be signed by all the founding members and is to be accompanied with a copy of the statute signed by all prospective members and a copy of a feasibility study into the economic and practical aspects of the activities to be carried out by the proposed society.

The admission of new members into a cooperative is partly regulated by law but is often regulated in the cooperative society's statute. The general rule set out in Section 53 of the Act is that any person may qualify for membership in a primary society if they are an individual who:

- a) has attained the age of 18 years and is of sound mind; and
- (b) satisfies such other requirements with regard to residence, employment, profession or other matter as may be prescribed by the statute; and
- (c) is not an undischarged bankrupt

Where the statute of a cooperative so permits, a commercial partnership may also qualify for membership provided that:

- a) the operations of the commercial partnership are wholly or mainly similar or equivalent to the operations of the society;
- (b) the commercial partnership shall be represented by a duly authorised individual at the general meetings of the society; and that such an individual shall be a director, partner or the majority shareholder of the said partnership;
- (c) a commercial partnership may not be a member of a committee of management or of a supervisory board, if any; and
- (d) the Board is informed immediately, by the society, whenever a commercial partnership is accepted as a member of that society

Apart from the criteria set out in the quoted section of the Act, it is very common to find ad hoc clauses in the statutes of cooperative societies imposing specific conditions for a person to be eligible to become a member of a cooperative. By way of example, if one is dealing with a farmer's cooperative, one would typically find a clause in the statute stating that in addition to the criteria set out at law, a member must possess a licence to act as a farmer, amongst others that may be imposed.

Cooperatives are therefore not obliged to accept third parties as members although such third parties are offered some form of protection under the Act by virtue of the proviso to Section 52 (2) which states that if a person's application is refused by the committee of management, such person may appeal to the general meeting of members and in any such case they may be admitted by a resolution passed by not less than two-thirds of the members present and voting at such a meeting.

The general rule is that a member may resign and hence transfer their share to a third party. This rule is however subject to Section 58 of the Act which states that no member may transfer any share held by them or their interest in the capital of the society or any part thereof, unless they have held such share or other interest for not less than one year. The transfer must also be made in favour of the society, a member of the society or a person whose application for membership has been accepted by the committee of management of the society.

The liability of a member, present or past, of a society, is limited to the amount, if any, unpaid of the shares held by them. The liability of a past member for the debts of a society in terms of the aforesaid shall be limited to those which existed on the date on which they ceased to be a member and ceases on the expiration of two years commencing on that date. The liability of the estate of a deceased member is limited to the debts of the society, as they existed on the date of the death of the member and ceases on the expiration of two years commencing on that date.

The “one member one vote” principle is applied in the majority of decisions taken by cooperative societies. Hence each member of a Primary society shall only have one vote in the affairs of the society, including general meetings, irrespective of the number of shares they hold and the right to vote shall be exercised in person and not by proxy. Having said this, Section 56 of the Act allows a society to derogate from this principle in its statute when it states: “*Unless the statute of a society provides otherwise ...*”

In the case of secondary or tertiary societies, each society which is a member shall have as many votes as may be provided in the statute of the respective societies.

The internal structure of administration or governance of a cooperative society comprises the general meeting of members, the committee of management, the supervisory board (if appointed) and, to a certain extent, the manager of the cooperative society if so appointed.

The supreme authority of any cooperative society vests in the general meeting of the members forming part of the cooperative.<sup>6</sup> General meetings can be of two types – the annual general meeting and the extraordinary general meeting. An annual general meeting is to be called by not later than six months from the end of the cooperative’s financial year, with a notice to be given to all members at least 15 days prior to the meeting indicating the agenda and any resolutions to be proposed.

The functions of an annual general meeting are spelt out in Section 66 of the Act and include the approval of previous minutes, approval of the financial statements, considering reports by the auditor, by the committee of management or the supervisory board, amendments to the statute, election of members to the committee of management, appointment of the auditors, deciding appeals of persons whose application for membership would have been rejected by the committee of management, approval of honoraria, allowances or fees and decisions to be taken on the maximum amount the cooperative society may borrow.

By default, any meeting of the members which is not the annual general meeting is referred to as an extraordinary general meeting which may be convened at any time by

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<sup>6</sup> Section 62 (1) of the Act.

the committee of management and which shall be convened by the committee of management on receipt of a request for such a meeting signed by at least one-fourth of members or 15 members of the society, whichever is lower, stating the objects of the meeting OR on receipt of a request by the Supervisory Board or the Board also stating the objects of the meeting. Should the committee of management fail to summon a meeting within one month from when they are specifically requested to do so, the Supervisory Board or the Board have the power to convene a meeting themselves.

Business is only transacted at general meetings provided a quorum of 15 members or one-fourth of the members qualified to vote, whichever is the lower, are present at the meeting. Voting at general meetings is decided by a majority of votes unless otherwise specified in the Act or in the cooperative society's statute. Resolutions put to the vote are to be decided by a show of hands unless voting by call of names or by ballot is demanded by at least two members, where the number of members present is less than 20, or by at least five of the members present in any other case.

Except as otherwise provided for by the Act and the powers reserved for the general meeting, the general rule is that the committee of management is vested with the conduct and management of the affairs and business of the cooperative. Every cooperative society needs to have a committee of management composed of not less than three and not more than nine individuals acting in their own name, which committee members are elected, suspended, removed or re-elected by the general meeting of the cooperative society.<sup>7</sup>

In order for an individual to be eligible for membership of or remain a member of the committee of management, they need to satisfy the following criteria.<sup>8</sup>

They:

- (a) are a member of the society;
- (b) are an individual appointed in writing by a commercial partnership which is a member of the society;
- (c) do not engage in an activity which gives rise to a conflict of interest, subject to the general meeting deciding that such a person may still be eligible;
- (d) do not take part, on a permanent or occasional basis, in any activity which is directly or indirectly in competition with that of the society;
- (e) are not an undischarged bankrupt;
- (f) have not been convicted of any crime punishable by more than one year's imprisonment;
- (g) do not have any outstanding debt owing to the society at the end of the society's financial year other than in respect of a loan made under the relevant rules of the society statute;

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<sup>7</sup> Section 71 of the Act.

<sup>8</sup> Section 72 of the Act.

(h) in the case of a primary society, they are not already a member of a committee of management of another primary society having the same or similar objects or activities;

(i) they do not receive any remuneration, salary or other payments, allowances and honoraria notwithstanding, except in those societies where the members of the society are also the employees.

Whilst all members of the committee of management serve until the next annual general meeting, it is quite common for cooperative societies to adopt a rotation system in their statute such that at every general meeting only one-third of the committee members retire from office – this in order to allow continuity and add new blood to experienced committee members in the collective interest of the members.

The committee members are to elect from amongst themselves a president, vice-president, secretary and treasurer with all these offices having specific functions set out in the Act. Committee meetings are held at least once a month with all decisions taken by majority vote without the chairman having a casting vote.

The committee of management may also appoint a manager with duties to be specified either in the statute of the cooperative or in his letter of appointment. If appointed, his duties will be conducted under the general supervision and policy directions of the committee of management, and they may be invited to attend meetings of the same committee of management from time to time.

Apart from the general meeting of the members, the committee of management and the manager, if appointed, good governance within a cooperative society is further strengthened if the cooperative society allows in its statute the possibility of establishing a supervisory board.<sup>9</sup> This board, made up of not less than three and not more than five members or as otherwise prescribed by the cooperative's statute, consists of persons who are neither members of the society nor the its committee of management and are usually individuals who have knowledge of cooperative legislation, accounting, auditing and financial procedures.

The supervisory board regulates its own procedure and is responsible to the general meeting of the cooperative society for assisting the committee of management in the efficiently running the cooperative society by ensuring that decisions taken at committee level are in accordance with the law and the statute of the society. It serves as a watchdog on the decisions which the committee of management takes from time to time and can bring to the attention of the same committee any matters concerning the affairs of the society. It is also bound to present to the annual general meeting of the members a specific report on the management and financial position of the society in those cases in which the committee of management fails to act in accordance with the requirements of the statute and can also, as stated earlier in this paper, summon extraordinary general meetings in specific circumstances.

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<sup>9</sup> A simple majority of members present and voting at a general meeting may likewise appoint a supervisory board.

### c) Cooperative financial structure and taxation

The capital of a cooperative society may be raised, subject to the provisions of the Act, in any one of the following manners:

- (a) admission fees;
- (b) subscription and payment of shares;
- (c) savings deposits made by its members;
- (d) deposits or loans from non-members; and
- (e) surplus carried to reserve funds.

The following rules shall have effect with respect to the manner of raising capital specified above:

- a) no admission fee shall be refundable except in respect of an application for membership that has been rejected;
- (b) no share may be redeemed except in accordance with the statute of the society and no rule in the statute allowing such redemption shall have effect unless such rule also specifies the minimum number of shares a member shall hold while they are a member;
- (c) savings deposits may be either obligatory and regular or voluntary. Regular and obligatory deposits shall be made in accordance with the statute of the society and may not be withdrawn except for purposes and in accordance with conditions specified in the statute, or on termination of membership; such deposits may serve to secure loans taken by or guarantees given by a member. Voluntary deposits may be withdrawn, subject to any conditions or restrictions specified in the statute;
- (d) deposits or loans from non-members shall be subject to the provisions of the Act and of the statute of the society; and
- (e) a reserve fund shall be kept and used in accordance with the provisions of the Act and of the statute of the society.

A society may not issue bonds or debentures without the authority of the Board and shall, in any such issue, comply with any conditions prescribed by the Board.<sup>10</sup>

Members need not contribute equally to the capital of the cooperative society. There is however a restriction found in Section 57 of the Act which states that notwithstanding anything that may be contained in the statute of a society, no member shall hold more than 40% of the share capital of any society. This is provided that, in the case of

<sup>10</sup> All the detailed rules concerning capital are referred to in Section 87 of the Act.

secondary or tertiary societies, a member which is itself a cooperative society may hold more than 40% of such share capital.

Shares are acquired voluntarily but, as stated earlier in this national report,<sup>11</sup> a member can only transfer them or any interest therein if they held such share or interest for at least one year and if the transfer is made in favour of the cooperative society, a society member or a person whose application for membership has been approved by the committee of management. A member can of course withdraw from a cooperative subject to any conditions prescribed in the statute and in such the amount to be paid to the withdrawing member for the redemption of his share or interest shall be the nominal value thereof. There is no provision in the Act which specifies that contributions be linked or made proportional to the volume of transactions.

A society may receive deposits and loans from members and from persons who are not members only if so authorised by its statute and only to such extent and under such conditions as may be determined or prescribed by its statute or in terms of law. A cooperative which under its statute has the power to borrow money shall determine at a general meeting the maximum liability which it may incur within the limits prescribed by its statute, in respect of loans or deposits from members and non-members including bank overdrafts.<sup>12</sup> A cooperative may also invest or deposit its funds in accordance with the provisions of its statute or in any other manner which the committee of management may consider appropriate subject to any general or specific directions determined by the general meeting of the members.

Section 90 of the Act imposes an obligation on all cooperatives to maintain a reserve fund in the form of liquid assets, to be used exclusively to cover losses incurred by the cooperatives. Every cooperative is to transfer at least 20% of its surplus at the end of each accounting period into this Reserve Fund. However, this requirement does not apply in the event that at the end of any accounting period, the Reserve Fund is equal to the total of the paid-up share capital and equal to 20% of the borrowed capital of the society, as shown in the audited and approved balance sheet of the preceding financial period.

Apart from this allocation to the Reserve Fund, every society is to contribute 5% of its surplus resulting from its activities, operations, investments and any other sources at the end of each accounting period to what is known as the Central Cooperative Fund (hereinafter referred to as "CCF"). The CCF is deemed to have a distinct legal personality and is capable of doing all such things and entering into all such transactions as are incidental or conducive to fulfil its objectives. Essentially the CCF serves to promote cooperative education, training, research and the general development of the cooperative movement in Malta.<sup>13</sup>

The net surplus of a society which remains at the end of each accounting period after transfers are effected to the Reserve Fund and the CCF may be divided amongst the

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<sup>11</sup> Page 8 supra.

<sup>12</sup> Section 88 of the Act.

<sup>13</sup> There are several regulations issued under our law relating to the CCF which the author will not delve into for the purposes of this national report.



members by way of dividend<sup>14</sup> or in any manner authorised by the Act or by the statute of a society and may also be allocated to any other funds of the society. A society may apply any amount of its net surplus for any charitable, educational or other public purpose.

Apart from dividends which are pegged to the proportion of subscribed capital, a society may distribute any part of the remainder of its net surplus by way of patronage refund – a distribution paid to members in proportion to the volume of business or other transactions done by the said members with the society. This is indeed the most common method of distribution amongst members of cooperative societies in Malta.

It is worth mentioning too that there are yet another two ways of distributing any part of a cooperative's net surplus which are generally used to alleviate cash flow problems for the cooperative society. Firstly, a society may issue a bonus certificate which entitles the holder to claim payment of the sum for which the certificate is issued out of the society's funds on a date specified in the certificate, not earlier than five years from when the bonus certificate was issued. No interest or dividend shall be paid on such certificates. Secondly, a society may issue a bonus share which may not be withdrawn or transferred before the elapse of 10 years from the date of its issue unless the holder of the bonus share has ceased to be a member, in which case the sum claimed by a former member may be claimed by the same person or their heirs up to 12 months after the date when the person had ceased to be a member.

Any member of an amalgamating society<sup>15</sup> or of a transferor society may, by not later than two months from the date of the resolution passed by such society relating to the amalgamation, declare his intention not to become a member of the new society or of the acquiring society and upon giving notice thereof, they shall cease to be a member and shall be entitled to receive the nominal value of their shares.

The situation relating to remaining funds in a cooperative upon dissolution is somewhat different. Upon the winding up of a society, the assets, including the Reserve Fund, are first applied to the liquidation costs, then to the liabilities of the society, then to the payment of the share or subscription capital. Thereafter, if the statute permits, assets are then distributed to the payment of a dividend or patronage refund at a rate not exceeding that specified in regulations made under the Act or society's statute for any period during which no dividend or patronage refund was paid. Any monies remaining after allocating them as explained above, barring any creditor claims, cannot be divided amongst the members (except in the case of a liquidation of a secondary society) but will instead be deposited into a liquidation account held by the Board, which on the lapse of five years will then be transferred to the CCF.

### **Cooperative taxation**

As stated above,<sup>16</sup> Section 12 (1)(q) of the Income Tax Act exempts the income of a co-operative society from the payment of income tax.

<sup>14</sup> The statute may establish the maximum rate a society may pay to its members by way of dividend, failing which the maximum rate will be established by the Minister responsible for cooperative societies in consultation with the Board.

<sup>15</sup> An amalgamating society may refer to a primary secondary or tertiary society.

<sup>16</sup> Page 2 supra

### iii. Other specific features

#### d) Cooperative internal and external control and cooperation among cooperatives

##### **Cooperative external control**

All cooperative societies are subject to a degree of external or State control the moment they are created as their existence is initially dependent on the acceptance by the Board. Apart from being directly involved in the registration process of a cooperative, the Board also monitors and supervises cooperatives to ensure compliance with the provisions of the Act. It has wide reaching powers including that of holding an inquiry into the affairs of any cooperative society, imposing administrative penalties, suspending or restricting the activities of the society and removing the committee of management of any cooperative society.

As stated earlier in this national report,<sup>17</sup> under Maltese law, the Minister responsible for cooperative societies in Malta sets up the CCF which, in terms of the Central Co-operative Fund Regulations<sup>18</sup> is composed of 11 voting members, six of which are appointed by the Minister responsible for cooperatives. It is once again noted that the use of the funds held within the CCF is dependent on the external control exercised by the Government of Malta through its appointees on this fund.

Apart from external control exercised directly or indirectly by the Minister responsible for cooperatives, there is a certain “positive” control on cooperative societies imposed by law due to the fact that every cooperative society in Malta is duty bound to prepare audited financial statements which are to be submitted to the Board together with the audit report within five months after the close of each financial year.

##### **Cooperation among cooperatives**

The sixth ICA principle on cooperation among cooperatives is included in Maltese legislation in Section 21 (2) of the Act which states:

*“Co-operatives serve their members most effectively and strengthen the co-operative movement by working together through local, national, regional and international structures.”*

It is the only direct reference in national legislation to ensure cooperation amongst cooperative societies and there are no special forms or rules on secondary cooperatives or on representative organisations of the cooperative movement.

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<sup>17</sup> Page 14 supra

<sup>18</sup> Subsidiary Legislation 442.03



### III. Degree of ‘cooperative friendliness’ of the national legislation

Maltese cooperative legislation can be considered to be friendly towards cooperatives to a significant degree. The Act incorporates the ICA principles and in practice, through experience working in this field, the national expert can safely conclude that there are no precise legal obstacles or barriers deriving from specific regulations or other sources of law which hinder the advancement and promotion of the cooperative movement in Malta.

The legislation is rather flexible and allows for a good rapport between the various cooperatives and the Board. Unfortunately, apart from assistance which may be obtained from the limited budget of the CCF, the promotion of cooperative societies is a function left to the societies themselves which, due to limited budgets, more often than not, fail to really promote the cooperative movement in Malta in a significant fashion. To the author’s knowledge, there are hardly any incentives for cooperatives in existing legislation other than the provision of the Income Tax Act exempting a cooperative from the payment of income tax and surely not in the area of public procurement.

### IV. Recommendations for the improvement of the national legal framework

The enactment of any piece of legislation will inevitably, as time goes by, require amendments or innovative ideas to be inserted to cater for situations which would have occurred in the natural course of events. The Act is no exception. Whereas one can safely conclude that the Act adequately caters for the proper functioning of cooperative societies in Malta and guarantees a certain amount of flexibility, the author believes that there are a number of areas which, if amended, would lead to the development of more cooperative societies in the country. A few examples will follow.

One of these areas relates to the definition of who can be a member of the cooperative. Section 53 (2) of the Act referred to previously in this national report.<sup>19</sup>

It is a known fact in Malta that the main commercial vehicle for carrying out business in Malta is the limited liability company – which falls within the definition of a commercial partnership in terms of the Act. Section 53(2)(a) of the Act severely restricts the right of limited liability companies to become members of cooperative societies since the objects of the companies must be “...*wholly or mainly similar or equivalent to the operations of the society*”. Over the years, there have been several instances in which companies coming from different sectors of the economy expressed the desire to set up a cooperative society between themselves but have hit a brick wall when it comes to incorporation precisely due to the fact that their main objectives, as contained in their respective Memoranda of Association are not wholly similar or equivalent to the operations of the cooperative they intend on setting up. The national expert regrets this

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<sup>19</sup> Supra Page 7

and believes that by removing this restriction, one would pave the way for companies to set up or participate in cooperative societies thereby increasing the limited number of cooperative societies registered in Malta and above all allow the cooperative movement to benefit from the wealth of experience and investment which limited liability companies have developed over the years.

Another aspect which could be more adequately regulated is that relating to amendments to the statute. As things stand today, any amendment to a statute of a cooperative society is only effective if approved by the Board.<sup>20</sup> At first glance there might not seem to be anything abnormal with this but in practical terms, this often poses a problem from a timing perspective. In terms of law, any proposed amendment needs to be first circulated to members of a cooperative at least 15 days prior to any extraordinary general meeting. It then needs to attain the required majority at the extraordinary general meeting. Assuming that a majority has been achieved, the resolution is then sent to the Board for approval and eventual publication in the Government Gazette. The problem arises if the Board decides to block the suggested amendment to the statute as the cooperative society would be in a situation where its members would have approved the resolution whilst the Board refused it. Unless an agreement is reached with the Board, the cooperative society would need to once again circulate the amended resolution, call a meeting of its members hoping to achieve a renewed majority vote. The author believes that the above can easily be avoided if the procedure is amended in such a manner wherein any proposed change to the statute is first vetted by the Board and only once this is confirmed would it then be circulated to its members on the notice of the agenda of the extraordinary general meeting.

Another questionable legislative enactment is that contained in Section 17 of the Central Co-operative Fund Regulations which provides that the said regulations and the CCF Committee, which as stated earlier has a majority of Government appointed members, *"shall be subject to the existing rules governing public funds including the Public Administration Act, the Public Services Management Code and the Code of Ethics in accordance with the First Schedule to the Public Administration Act"*. In essence, 5% of the surplus which each cooperative contributes to the CCF from their work during the year and therefore from their private funds, is not only being ultimately administered by a committee made up of a majority of Government nominated individuals but worse still, the said contributions are being transformed into public funds by means of this section of this subsidiary legislation. Prior to the inclusion of this new Section 17 in Legal Notice 344 of 2016, the CCF was administered by a committee with a majority of members coming from the cooperative movement and only a minority from the Government. In the opinion of the national expert, the situation ought to revert back to what it was prior to 2016 for cooperatives, via their appointees on the CCF, to operate the funds which they are contributing to the CCF in the best interest of the cooperative movement in Malta.

Finally, provisions of the Act relating to dissolution and amalgamations of cooperatives require, in the author's opinion, a major overhaul as the provisions are rather concise, as noted above.

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<sup>20</sup> Section 35 (3) of the Act.

## V. Conclusion

This national report is not intended to be an all-encompassing resume of the position of cooperatives in Malta. Although the Act adequately caters for the proper functioning of cooperatives in Malta and provides a certain level of flexibility, a number of areas for potential amendment remain that could encourage the development of cooperatives. However, a detailed study of every other existing legislation in the country would need to be undertaken in a separate exercise, to determine with certainty which legislation, if any, provides or could provide added incentives to cooperative societies in Malta. The national expert has prepared this report to the best of his knowledge in line with the methodological process of the legal framework analysis research.

**December 2020**

*The legal frameworks analysis is a tool developed under the ICA-EU Partnership #coops4dev. It is an overview of the national legal frameworks at the time of writing. The views expressed within this report are not necessarily those of the ICA, nor does a reference to any specific content constitute an explicit endorsement or recommendation by the ICA.*

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