



Recent Tax Developments Malaysia

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TAX



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Advanced Pricing Arrangement (APA)

- **Key Features**

- Mechanism to reach agreement with tax authority(ies) on prices of goods and services to be transacted in future between taxpayer and related companies for a specified period
- Enhance certainty on pricing issues for international dealings with related parties
- Types of APA: Unilateral, Bilateral and Multilateral APAs
- New Section 138C in Income Tax Act, 1967

- **Effective: From 1 January 2009**

Arm's Length Principle

- **Key Features**

- Specific provision established to empower DGIR to make adjustments on transactions of goods, services or financial assistance by:

- Substituting price of goods and services; and

- Disallowing interest on excessive financial assistance provided to related parties

which do not conform to the arm's length principle

- New Section 140A in the Act

- **Effective: From 1 January 2009**

Arm's Length Principle (Cont'd)

- The Act does not define what is the arm's length principle
- Para 1, Article 9 of OECD Model Tax Convention on Income and Capital definition:
“Where...conditions are made or imposed between...2 (associated) enterprises which differ from those which would be made between independent enterprises, then any profits which would have accrued to one of the enterprises, but, by reason of those conditions have not so accrued, may be included in the profits of that enterprise and taxed accordingly.”

Thin Capitalisation

- A new Section 140A(4) will be introduced which empowers the DGIR to disallow deduction on interest or finance charges which relates to the amount of financial assistance deemed excessive by reference to the fixed capital of such persons
- At this stage, it is unclear how the arm's length ratio will be determined - benchmarking?
- For example, if the arm's length debt to equity ratio is 3:1, then any interest on debt in excess of this ratio will not be deductible
- Also there is no definition of "Financial Assistance" and "Fixed Capital" proposed

Thin Capitalisation (Cont'd)

Tax consideration	Australia	Korea	Japan
Tax rate	30%	27.5%	Approx. 42%
Thin capitalisation	Safe harbour debt amount equal to 75% of net Australian assets but have arms length test as fall back. Special rules for financial institutions (20:1)	Yes, debt to equity ratio of 3:1 (6:1 in case of financial business) on loans from overseas controlling shareholders (generally over 50% ownership)	Debt to equity ratio of 3:1 on loans from overseas controlling shareholders (generally over 50% ownership)
Transfer pricing	Arm's length	Arm's length	Arm's length
Interest withholding taxes	10% or treaty rate	27.5% or treaty rate	20% or treaty rate

Thin Capitalisation (Cont'd)

- **Considerations:**

- How is equity measured
- How is debt measured
- What is the acceptable ratio
- When is compliance with ratio measured
- What is the effect of non-compliance
- Applicable only for cross border transactions or to all transactions
- Any grandfather provisions

Reinvestment Allowance

◆ Tightening of eligibility for RA

Present	Proposed
RA is eligible for a qualifying project	Change in definition of qualifying project by excluding the word "Processing"
Manufacturing activity is not defined	Manufacturing activity is defined and specific
Operation for at least 12 months	Operation for at least 36 months
RA claimed based on TWDV for CT assets	No RA claimable on CT assets
Claw back RA for assets disposed off within 2 years	Claw back RA for assets disposed off within 5 years

Reinvestment Allowance (Cont'd)

- **New definition of “Manufacturing” in the Act**

- (a) conversion by *manual* or *mechanical* means of organic or inorganic materials into a new product by changing the **size, shape, composition, nature** or **quality** of such materials;
- (b) assembly of parts into a piece of machinery or products; or
- (c) mixing of materials by a chemical reaction process including biochemical process that changes the structure of a molecule by the breaking of the intra molecular bonds or by altering the spatial arrangement of atom in the molecule,

but excludes

- Simple packaging, fixing, mixing, assembly (amongst others)
- **Definition of qualifying project now excludes the word “Processing”**
- **Effective: From YA 2009**

Reinvestment Allowance (Cont'd)

◆ Controlled Transfer (CT)

	Disposer	Acquirer
Capital Allowance (CA)	No claw back	CA claimed based on TWDV
RA (Present)	Claw back if < 2 years	RA claimed based on TWDV
RA (Proposed)	Claw back if < 5 years	No RA claimable

Claw back of RA still applicable even though acquirer not eligible to RA claim at all?

Withholding Tax Under Section 109F

- **Withholding tax under Section 4(f) of the Income Tax Act, 1967**
 - Section 4(f) income is defined as gains or profits not falling under Section 4(a) to Section 4(e) of the Act
 - New Section 109F & Section 15B – WHT rate 10%
- **Effective: From 1 January 2009**

Withholding Tax Under Section 109F (Cont'd)

- **Issues:**

- Business income or non-business income of a non-resident?
 - Example of income provided in Budget Speech such as commissions, guarantee fees, and introducer's fees could be business income for certain non-resident service providers – Section 4(a) or Section 4(f) income?
 - Interaction with DTAs
 - Business Income Article
 - Other Income Article

Withholding Tax Under Section 109F (Cont'd)

- **Issues (Cont'd):**

- Services performed outside Malaysia – withholding tax under Section 109F still applicable!
- Services rendered outside Malaysia – no withholding tax if Section 4A income

Group Relief

- **Increasing rate of current year losses allowed to be set-off in group relief from 50% to 70%**
- **Conditions under Section 44A of the Income Tax Act, 1967 still applies**
- **Effective: From YA 2009**

Group Relief (Cont'd)

- **Section 44A conditions – group relief applicable to resident companies subject to conditions:**
 - Paid-up capital exceeding RM2.5 million
 - Same accounting period
 - Shareholding (direct or indirect) in the group must not be less than 70%
 - 70% shareholding continuous in preceding & relevant year
 - Not applicable if either company enjoys Pioneer Status, ITA, Section 127 exemption, RA claims, etc



Thank You



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