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Tan Wei Chuan l 11 December 2024

MAKING AN IMPACT THAT MATTERS since 1845

Latest developments

- Foreign-Sourced Income
- Capital Gains Tax
- Hybrid Instruments

Foreign-Sourced Income

Foreign-Sourced Income Received in Malaysia

Qualifying conditions for exemption

	Types of income	Qualifying conditions	Period
Resident company, limited liability partnerships (LLP) and individual partner in relation to partnership business in Malaysia (IIP)	Dividend	**Option A: Participation exemption requirements** a) The dividend income has been subjected to tax in the country of origin; **and** b) The highest tax rate (headline tax) in the country of origin is not less than 15% **Option B: Economic substance requirements** a) An adequate number of employees; and b) An adequate amount of operating expenditure	1 Jan 2022 to 31 Dec 2026
Individual	All types of income other than partnership income.	**Option A:** The foreign income has been subjected to tax in the country of origin; **or** **Option B:** Tax is not imposed in the country of origin due to certain reasons specified within the guidelines	1 Jan 2022 to 31 Dec 2036 ***(Budget 2025)***

Exemption from Tax on Foreign-Sourced Income for Unit Trusts

Income Tax (Unit Trust in relation to Income Received in Malaysia from Outside Malaysia) (Exemption) Order 2024 [P.U.(A) 250/2024]

Chargeable persons

Qualifying unit trust

- Resident in Malaysia and managed by a "management company"

Excludes:

- Unit trust approved by the Securities Commission as REIT or Property Trust Fund listed on Bursa Malaysia
- Unit trust carrying on business of banking, insurance, sea or air transport

Management company

Company licensed by the Securities Commission by which or on whose behalf a unit of a qualifying unit trust —

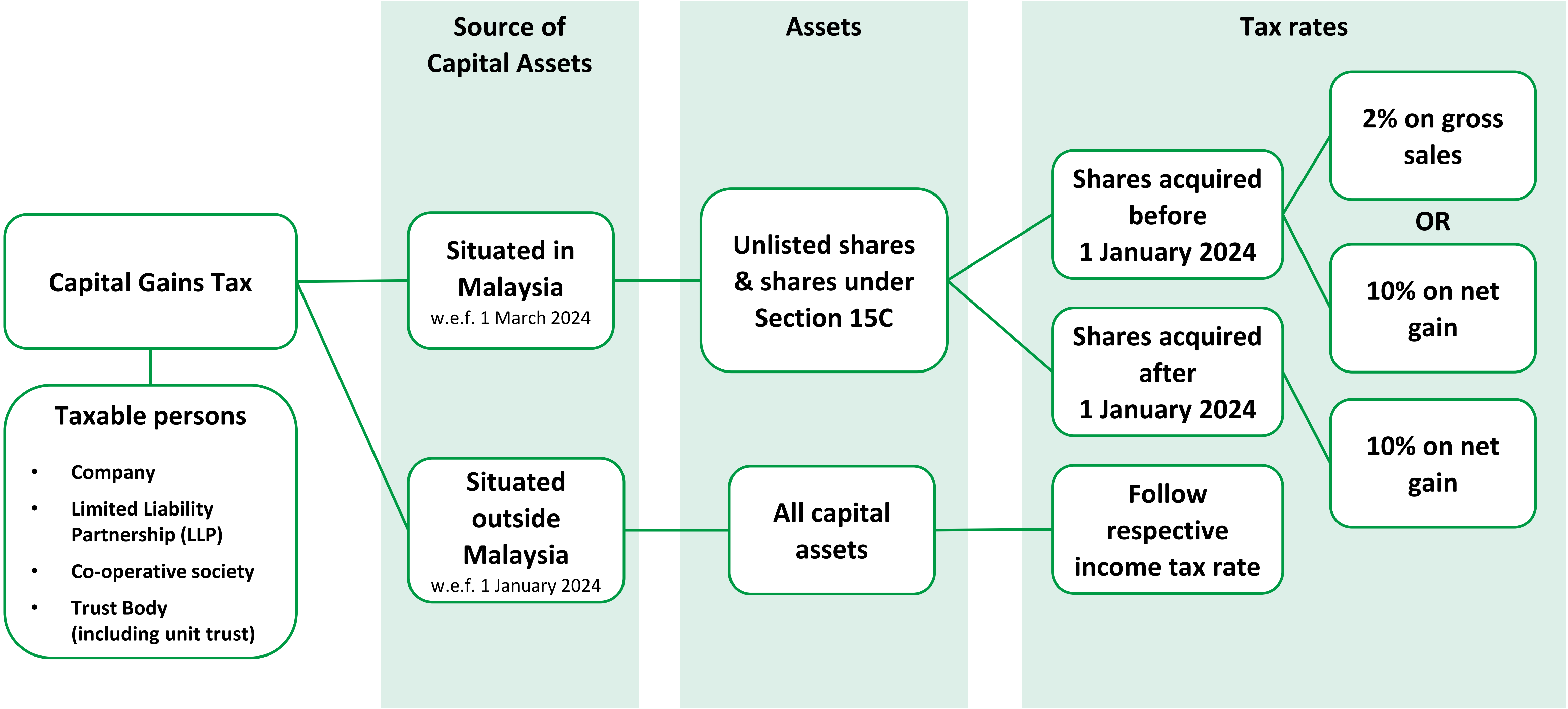
(a) has been or is proposed to be issued, or offered for subscription or purchase; or
(b) in respect of which an invitation to subscribe or purchase has been made

and includes any person for the time being, who is exercising the functions of the management company.

Capital Gains Tax

Capital Gains Tax ("CGT")

Summary



Exemption from Capital Gains Tax (CGT) for Unit Trust

Income Tax (Unit Trust) (Exemption) Order 2024 [P.U.(A) 249/2024]

Exemption

- Qualifying unit trust resident in Malaysia
  (***Exclude***: unit trust which is approved by the Securities Commission as a Real Estate Investment Trust (REIT) or Property Trust Fund listed on Bursa Malaysia)

- Gains or profit from disposal of:
  a) Unlisted shares; or
  b) Section 15C shares

- Loss on disposal of shares – allowed as deduction [Subsections 65E(5) and (6)]

Effective

Disposal of shares made from
1 January 2024 to 31 December 2028

Non-application

Disposal of shares where gains or profits is chargeable to tax as business income under Section 4(a) of the Act

CGT Exemption in relation to Restructuring of Companies Scheme

Income Tax (Restructuring of Companies Scheme) (Exemption) Order 2024 [P.U.(A) 289/2024]

Non-application

- Disposal of unlisted shares where gains or profits from the disposal of shares is chargeable to tax as business income under Section 4(a)
- Disposal of shares in respect of restructuring of any companies for the purposes of an IPO and the application for the IPO has been made
- Tax exemption has been granted under Sections 127(3)(b) or 127(3A) of the ITA, in respect of the same disposal of shares

Conditions and application procedures

a) Disposal of unlisted shares to an acquirer company (resident in Malaysia) under scheme of restructuring of companies in the same group to increase efficiency

b) Consideration for disposal should consist of:
- Shares in acquirer company; or
- Not less than 75% of shares in the acquirer company and the balance of a money payment

c) Apply in writing to the Director General after the period of 3 years from the date of the disposal of shares

c) Comply with the conditions imposed by the Minister as specified in the guidelines issued by the Director General under Section 134A

Effective

Disposal of shares made between **1 March 2024 to 31 December 2028**

CGT Exemption in relation to Initial Public Offering (IPO)

Income Tax (Initial Public Offering) (Exemption) Order 2024 [P.U.(A) 290/2024]

Non-application

- Disposal of unlisted shares where gains or profits from the disposal of shares is chargeable to tax as business income under Section 4(a)
- Application made for exemption under the Income Tax (Restructuring of Companies Scheme) (Exemption) Order 2024 [P.U.(A) 289/2024] in respect of the same disposal
- Tax exemption has been granted under Sections 127(3)(b) or 127(3A) of the ITA, in respect of the same disposal

Conditions and application procedures

a) Disposal of unlisted shares in relation to restructuring of any company for an IPO

b) Apply for the IPO under the Capital Market and Services Act 2007 [Act 671] within 1 year from the date of the disposal of shares –
- to the Securities Commission for the purpose of listing on the Main Market; or
- to Bursa Malaysia Securities Berhad for the purpose of listing on the ACE Market and LEAP Market.

c) Obtain the approval for the application of the IPO, either on or before 31 December 2028

d) Apply in writing to the Director General within the period of 1 year from the date of approval for the application of the IPO

Effective

Disposal of shares made between **1 March 2024 to 31 December 2028**

Hybrid Instruments

Introduction and general features

Guidelines on Tax Treatment of Hybrid Instrument

Equity Holding	Debt Holding
Entitled to partake in **share of distributions or profits** of the entity, namely dividend, distribution from Real Estate Investment Trust (REIT) and return, interest or premium arising from profit	The right on distributions or profits is **fixed**
Entitled to **residual assets** of the company after the repayment to debt holders upon liquidation	Entitled to **reimbursement of the principal amount** of debt during liquidation
No maturity date	Has maturity date
The right to vote	No right to vote
Management of the entity has **discretion to make payment** of distributions or profits	Instrument holder has a legal right to **demand payment** of distributions or profits

Conventional Hybrid Instrument

Guidelines on Tax Treatment of Hybrid Instrument

Factors	Features	
	Equity	**Debt**
Source of repayment for the principal and payment of distributions or profits	Retained earnings or restrictive reserve	Not subjected to issuer's profit and liability to pay is accumulative
Priority of principal repayment in the event of liquidation or dissolution	**Lower** than creditor or debt holders Holder assumes responsibility for potential losses	**Higher** than equity holders Payment is mandatory and / or cumulative
Right of holder to **enforce payment**	Holder has **no right** to enforce payment	Holder has **absolute authority** to demand payment
Right to **recover** in the event of default	Holder has **no right** to recover	Holder has the **right to recover** normally under the step-up feature found in perpetual instruments
Maturity date of instrument	**No fixed** repayment date or step-up feature	**Fixed** repayment date and has step-up feature

Conventional Hybrid Instrument – Continued

Guidelines on Tax Treatment of Hybrid Instrument

Factors	Features	
	Equity	Debt
Ability of issuer to obtain a loan and make payment on an **arm's length transaction**	The terms and conditions of the loan are **unreasonable**, and no independent creditor will provide similar loan with such terms. This usually involves a transaction between either **controlled companies** or **related companies**	Issuer has the **capability to secure** a loan to fulfil payment obligations through arm's length transactions
Involvement in the **management**	Holder **has voting rights** *If the holder has no voting rights, it could still be an equity instrument. It should be further evaluated based on other factors*	Holder has **no voting rights**
Benefit to the holder	Holder may expect **profits** and a long-term **capital appreciation** of the investment	Holder may expect a **return on investment**, which is a steady stream of **recurring income** instead of capital appreciation

Tax Treatment of Equity Instrument

Guidelines on Tax Treatment of Hybrid Instrument

Instrument holder

a) **Dividends** received from a company resident in Malaysia **is tax-exempt** under paragraph 12B, Schedule 6 of the Income Tax Act 1967 (ITA).

b) **Foreign dividend income** received in Malaysia from 1 January 2022 until 31 December 2026 may qualify for **tax exemption** under the Income Tax (Exemption) Order (No. 6) 2022 [P.U.(A) 235/2022] and Guidelines on Tax Treatment in Relation to Income Received from Abroad (amendment) issued on 29 December 2022. [Income Tax (Exemption) Order (No. 6) 2022 (Amendment) order 2024 [P.U.(A) 157/2024] and Guidelines on Tax Treatment in Relation to Income Received from Abroad (Amendment) dated 20 June 2024 were recently issued.]

c) Distributions on instrument issued by **REIT** are **taxable** depending on unit holders' activities.

d) In all other cases, financial instruments are **assessable to tax** in accordance with the relevant current tax treatment in Malaysia and provided not specifically exempt.

Instrument issuer

a) Any payment made by the issuer in relation to the instrument is **not an allowable deduction** under Section 33(1) of the ITA or other similar provision of any tax laws in Malaysia.

Tax Treatment of Debt Instrument

Guidelines on Tax Treatment of Hybrid Instrument

Instrument holder

Receipt of **interest** arising from the instrument is **taxable** in the hands of the instrument holder in accordance with the relevant current tax treatment in Malaysia unless tax exemption granted, includes but not limited to:

a) Non-resident companies for ringgit-denominated sukuk (other than convertible loan stock) approved by the Securities Commission Malaysia (paragraph 33A, Schedule 6 of the ITA).

b) Any person for non-ringgit sukuk originating in Malaysia (other than convertible loan stock) and approved by the Securities Commission Malaysia or Labuan Financial Services Authority (paragraph 33B, Schedule 6 of the ITA).

c) Any individual, unit trust and listed close-end fund in respect of debentures or sukuk, other than convertible loan stock approved by the Securities Commission Malaysia (paragraph 35, Schedule 6 of the ITA).

Instrument issuer

Any sum payable in relation to the instrument is **allowed as deduction** under:

a) Section 33(1) of the ITA and subject to restriction under Section 33(2) of ITA and other provisions under the ITA; or

b) Similar provisions as stated in paragraph 6.2.3(a) involving any tax laws in Malaysia.

Transfer Pricing – Key development and updates

Transfer Pricing

Key developments and updates

Contemporaneous TPD

- ✓ Schedule 1
- ✓ Schedule 2
- ✓ Schedule 3

Threshold

- Gross business income > RM25mil + Total controlled transactions > RM15mil
  OR
- Provision or received controlled financial assistance > RM50mil (*EXCLUDED financial institutions)*

Timeline

- Preparation of CTPD: Prior to tax return filing deadline
- Furnishing of CTPD: Within 14 days of a request by IRBM

Arm's length principle

When market forces drive the terms and conditions agreed upon in an independent party transaction, the pricing should accurately reflect the true economic value of the contributions made by each party.

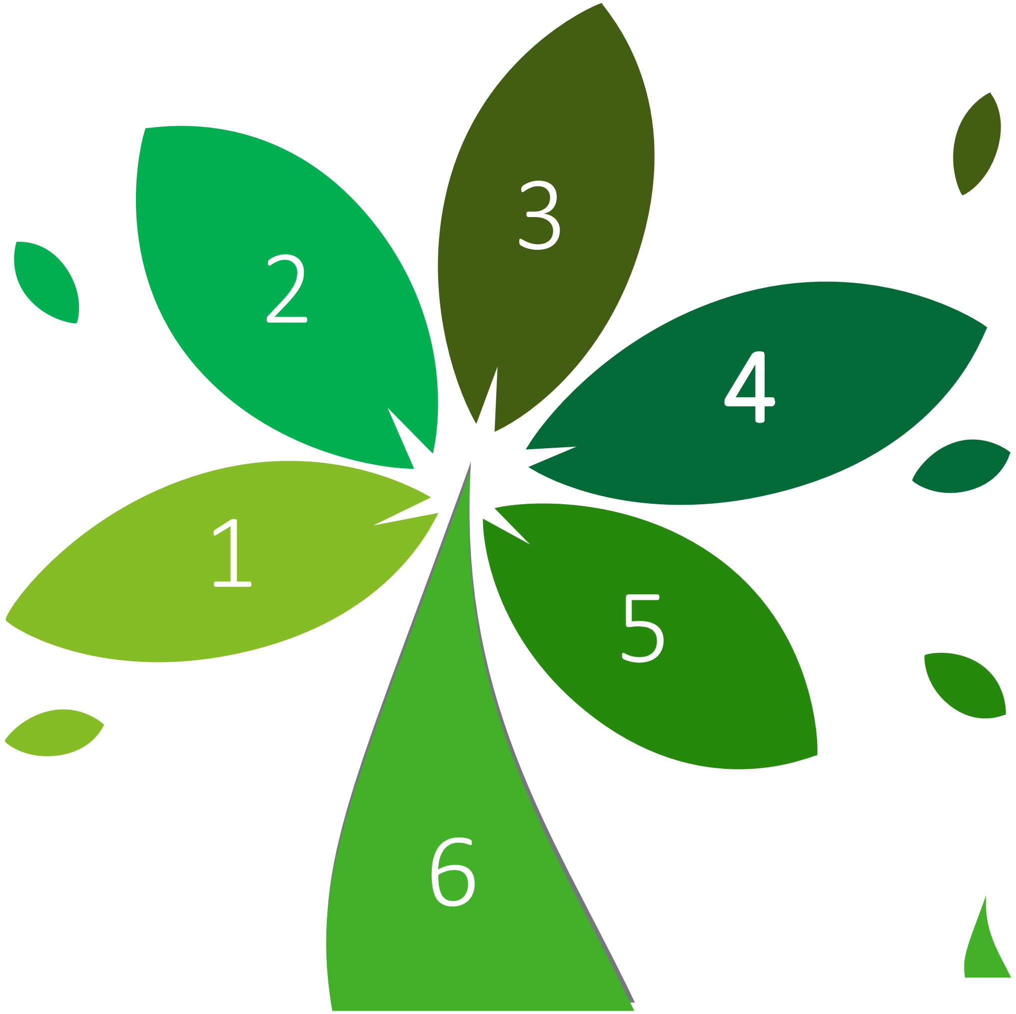
- Arm's length range
- TP method
- Separate/combined transactions
- Selection of tested party
- Comparable period
- Use of multiple year data

Transfer Pricing

Key developments and updates

2
The penalty of Section 113B(1) shall apply if taxpayer missed the tax return deadline. The amount of penalty would depend on how late taxpayers prepare the TPD.

1
Domestic RPTs are still required to comply with section 140A, even if both parties are chargeable and assessable to tax in Malaysia and any adjustment would not alter tax payable by both parties.



3
IRB has its own internal mechanism to identify whether TPD is contemporaneous.

4
Even if penalty is imposed on taxpayer for not preparing CTPD, TPD would still be required to be prepared by taxpayer.

5
Ultimate responsibility is on taxpayer to prove that TPD is contemporaneous.

6
Amendment of TPD after the completion date of report is not allowed, unless it is to attach the updated benchmarking result or Master File

Transfer Pricing – Audits

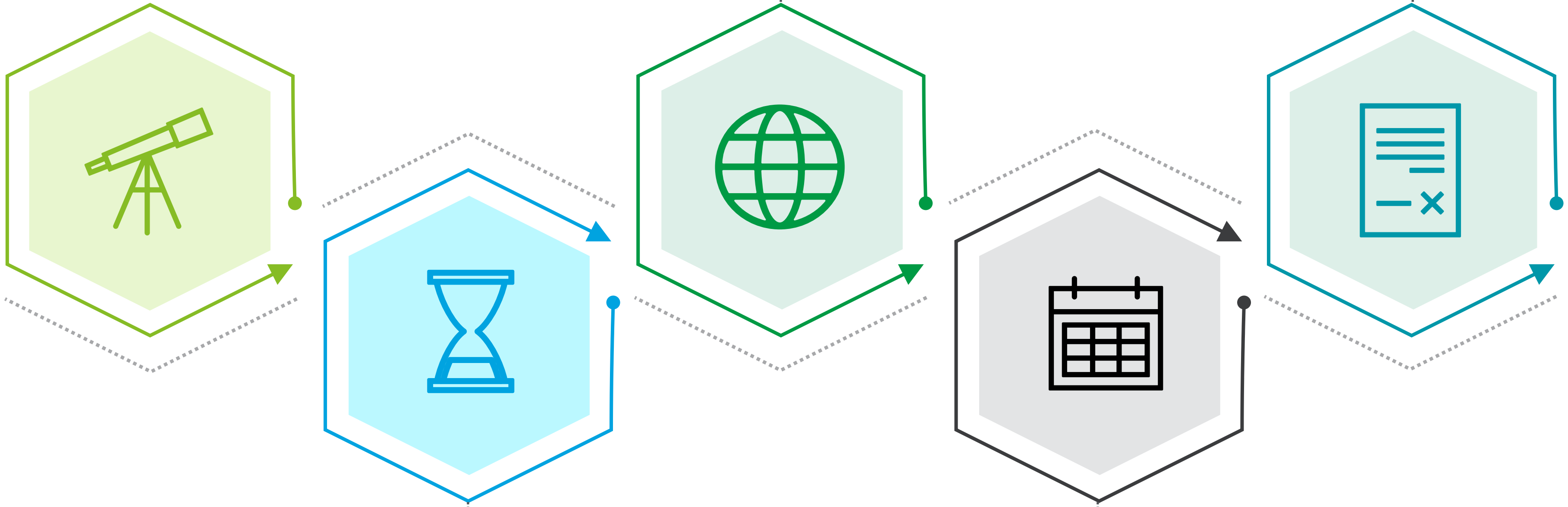
Transfer Pricing Audits

Key developments and issues identified during audit review in recent years

Audits can be conducted by different special branches of IRB

Joint audit for same group can be carried out by multiple branches simultaneously

If audit period covers YA 2023 and earlier years, both set of rules (TPR 2023 & TPR 2012) will apply respectively



IRB targets to close audits at a fast pace

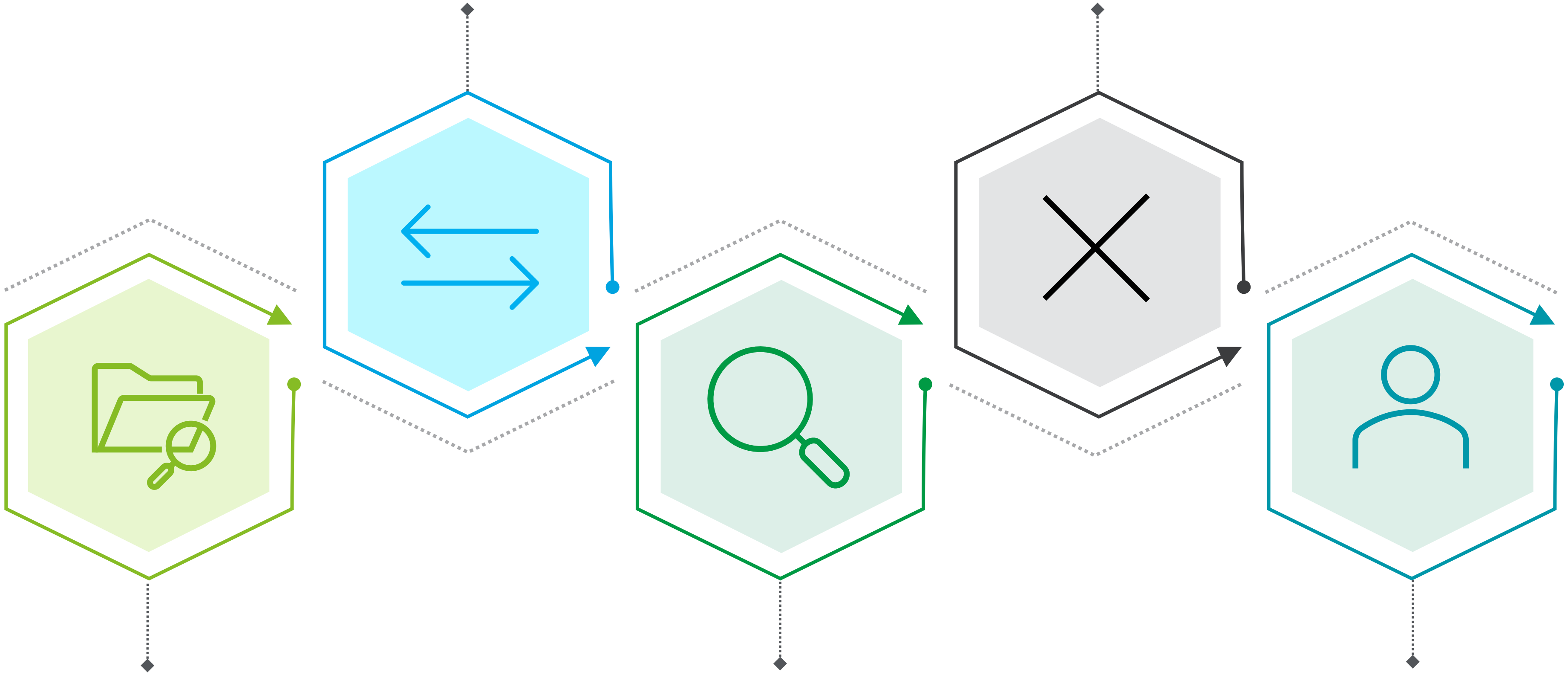
IRB can open up YAs as recent as YA 2023 for audit

Transfer Pricing Audits

Key developments and issues identified during audit review in recent years

Change of TP policy or method / PLI for different years

Inaccurate characterisation



- Ambiguous TP policy documented
- Intra-group services – Lack of intercompany agreements

Substance over form

- Inconsistent application of TP policies
- TP method and PLI selected are not in line with functional analysis / characterisation

Use of foreign tested party and comparables with lack of verifiable information

Transfer Pricing Audits

Triggers for incentivised clients

An incentivised company does not get exempted from the transfer pricing audit. During the course of audit, the tax authority would focus on aspects such as:

- whether the company is satisfying all the incentive approval conditions
- whether the company has submitted progress report/compliance report as required
- whether disposal of IP, compensation for loss of business income is under Section 4(f) income
- whether the non-incentivised activity/product has been duly excluded from the computation of tax exempted income
- whether the intercompany transactions are at arm's length, benefits tests for intercompany services
- withholding tax compliance