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Tax Incentives In Malaysia & The Potential Impact Of The Implementation Of G7 Global Tax Reform

Contact Persons:

Datuk D P Naban
Senior Partner
Tax, SST & Customs Practice
+603 6209 5405
naban@rdslawpartners.com

S Saravana Kumar
Partner
Tax, SST & Customs Practice
+603 6209 5404
sara@rdslawpartners.com

Malaysia presently offers a wide range of tax incentives to promote investments in selected industry sectors with the intention to promote the country's economy. The tax incentives available vary according to the Government's prevailing investment policies and objectives. Tax incentives offered ranges from income tax exemption, in part or in whole, or advantageous income tax rates.

The tax incentives available in Malaysia comes in three main forms, namely Pioneer Status, Investment Tax Allowance and Reinvestment Allowance. These incentives are governed by the Promotions of Investments Act 1986 (PIA 1986) and the Income Tax Act 1967 (ITA 1967). Apart from these main incentives, there are also special incentive schemes available for approved projects which fall within specific priority sectors or located in certain economic regions in the country.

In the past year, the Malaysian Government had introduced various tax incentives to businesses ranging from exemptions, additional deductions and reliefs through economic stimulus packages such as PRIHATIN, PENJANA, PERMAI and PEMERKASA. These incentives were aimed to reduce financial burdens borne by businesses due to the Covid-19 pandemic. Although many businesses were adversely affected by the Covid-19 pandemic, the digital economy had been thriving in an unprecedented manner. This led to the G7 nations (United Kingdom, Canada, France, Germany, Italy, Japan, and the United States) to agree on a global tax reform to tackle tax challenges amidst the current global digital economy.

Types Of Incentives Currently Available In Malaysia

- ***Pioneer Status***

The pioneer status under the PIA 1986 is an incentive which is granted in a form of tax exemption to companies engaging in specific promoted activities, products or operating within a promoted area. Upon approval, the company may enjoy a tax exemption between 70% to 100% of the statutory income for a period of five years. The tax relief period can be extended for an additional five years if the relevant conditions are fulfilled[1].

Eligible companies may make an application in writing to the Malaysian Investment Development Authority (MIDA)[2] by filling up the relevant forms applicable which are available on MIDA's website[3]. Companies with pioneer status may apply for a pioneer certificate within 24 months from the grant of the pioneer status for certification purposes[4].

Unabsorbed capital allowances and accumulated losses incurred during the pioneer period can be carried forward and deducted from the post pioneer income that was signed by its approved company auditor, confirming that the special refund information furnished by the taxpayer was prepared in accordance with the requirements under Sections 190 and 191 of the GST Act 2014.

The determination of promoted activities or products are announced by the Minister of Finance/Minister of International Trade and Industry (MITI) from time-to-time list of promoted activities and products are available on MIDA's website[5]. Examples of categories of companies operating in eligible sectors and industries are as follow:

- Agriculture production
- Manufacture of rubber products
- Manufacture of palm oil products and their derivatives
- Manufacture of chemicals and petrochemicals
- Manufacture of pharmaceutical and related products
- Manufacture of wood-based products

[1] Section 14A, PIA 1986
[2] Section 5, PIA 1986
[3] https://www.mida.gov.my/home/forms-&-guidelines-for-manufacturing-sector/posts/
[4] Section 7, PIA 1986
[5] www.mida.gov.my

- ***Investment Tax Allowance***

The alternative to pioneer status incentive under the PIA 1986 is the investment tax allowance[6]. A company with pioneer shall only be eligible to apply for investment tax allowance for the promoted activity or product if it surrenders the grant of its pioneer status. The investment tax allowance (ITA) is an incentive granted based on the capital expenditure incurred on industrial buildings, plant and machinery used for the purpose of the promoted activities or products. Therefore, the ITA is more suitable for projects which are capital intensive, and which are not expected to generate large profits in a short time. The list of promoted activities or products eligible for investment tax allowance are provided in the PIA 1986[7].

Companies that qualify for ITA will be able to enjoy tax allowances between 60% to 100% on qualifying capital expenditure for a period of 5 years. This allowance can be offset up to 70% of the statutory income of the company. Further, companies can carry forward any unused allowances in a year to subsequent years until it is fully utilised. This incentive can be claimed in addition to capital allowance under Schedule 3 of the ITA 1967.

Applications for ITA are to be made to MIDA. Upon obtaining approval to claim the ITA, companies may within 24 months from the date of the approval, request for a determination of the effective date of the allowance granted[8]. Similar to the grant of pioneer status, the period in which companies can enjoy the allowance can be extended to a total of 10 years.

- ***Reinvestment Allowance***

Reinvestment allowance is an incentive provided under Schedule 7A of the ITA 1967 for companies carrying out projects for purposes of expansion of existing production capacity, modernization or automation of existing production facilities or diversification into related products within the same industry. Other qualifying projects include agricultural projects undertaken for expanding, modernising, or diversifying its cultivation and farming business or one that is recognised by

[6] Section 26, PIA 1986
[7] Sections 26 and 29, PIA 1986
[8] Section 27P, PIA 1986

the minister as responsible for agriculture and ago-based industry[9].

This allowance is available to a Malaysian company which has been in operation for not less than 36 months and has incurred capital expenditure on a factory, plant or machinery used in Malaysia for the purposes of a qualifying project[10]. It is imperative to note that companies which have been granted pioneer status or approved to claim ITA are not eligible for this incentive[11]. Companies intending to reinvest before the expiry of its tax relief period, can surrender their pioneer status or pioneer certificate to be eligible for reinvestment allowance.

Moreover, it allows a company to claim 60% of the capital expenditure incurred for the qualifying project and is restricted up to 70% of the statutory income in a year of assessment. A company may also offset the reinvestment allowance against 100% of its statutory income provided that the qualifying project has achieved the level of productivity determined by the Minister of Finance[12]. Any unutilised allowance can be carried forward up to a maximum of 7 consecutive years of assessment.

The reinvestment allowance will be given for a period of 15 consecutive years beginning from the year the first reinvestment claim is made[13]. However, no allowance will be given to assets acquired for reinvestment and are disposed of within five years from the time of acquisition. If a company had purchased an asset from a related company within the same group and reinvestment allowance had been claimed on that asset, the purchasing company is not allowed to claim any reinvestment allowance on the same asset[14]. Applications for reinvestment allowance should be submitted to the Inland Revenue Board of Malaysia.

[9] Paragraph 8, Schedule 7A, ITA 1967
[10] Paragraph 1, Schedule 7A, ITA 1967
[11] Paragraph 7, Schedule 7A, ITA 1967
[12] Paragraph 3, Schedule 7A, ITA 1967
[13] Paragraph 2, Schedule 7A, ITA 1967
[14] Paragraph 1B, Schedule 7A, ITA 1967

- ***Other incentive regimes available***

Apart from the three standard incentives discussed above, special incentive schemes are also available for projects that the Malaysian Government considers to be of national and strategic importance. Some of the schemes that will be discussed here are the Principal Hub Incentive, Green Technology Incentive, Economic Corridors Incentive and Multimedia Super Corridor Incentive.

Principal Hub Incentive

A principal hub is defined as a locally incorporated company that uses Malaysia as a base for conducting its regional and global businesses and operations through management, control, and support of key functions, such as management of risk, strategic decisions, finance, and human resources[15]. The three main types of qualifying services are strategic services, business services and shared services. This incentive was introduced to attract local and multinational companies to establish their hubs in Malaysia. Application for this incentive is to be made to MIDA not later than 31 December 2022.

The companies must fulfil the following criteria to be eligible:

- Incorporated under the Companies Act 2016 and is a resident in Malaysia
- Have a paid-up capital of more than two million five hundred thousand ringgit (RM 2,500,000.00)
- Provide at least three qualifying services to its network companies located in three countries outside Malaysia in a year
- Have an annual value of sales of at least five hundred million ringgit (RM 500,000,000.00)

New companies are entitled to enjoy concessionary corporate income tax rate of 0% or 5% for a period of 5 years (another 5 years extension is available if additional conditions are

[15] Guideline for Principal Hub Incentive, revised as at 31.12.2018, MIDA

fulfilled). The effective tax rate for existing principal hub companies is 10% for a period of 5 years[16].

Green Technology Incentive

The available tax reliefs[17] in relation to the green technology industry are summarised in the table below:

Categories	Qualifying activities	Tax Reliefs
Green Technology Projects	Companies undertaking green technology projects related to renewable energy, energy efficiency, green building, green data centre, and waste management	• Investment Tax Allowance of 100% qualifying capital expenditure incurred from 25 October 2013 to year of assessment 2023 • The ITA can be utilised to offset against 70% of statutory income • Unutilised allowances can be carried forward until they are fully absorbed
Green Technology Assets	Companies that purchase green technology assets listed on the MyHijau Directory at www.greendirectory.my.	
Green Technology Services	Companies undertaking services related to renewable energy efficiency, electric vehicle, green building, green data centre, green certification and verification, and green township	• Income tax exemption (ITE) of 100% of statutory income from the year of assessment 2013 until the year of assessment 2023

Multimedia Super Corridor (MSC) Incentive

The MSC incentive is one of the Malaysian Government's initiatives in transforming the country into a global hub for multimedia technology. The goal is to develop an area equipped with high-capacity global telecommunications and logistics networks. This scheme is managed by the Multimedia Development Corporation (MDeC).

[16] Income Tax (Exemption)(No.6) Order 2018, Income Tax (Exemption)(No.7) Order 2018 and Income Tax (Exemption)(No.8) Order 2018

[17] Income Tax (Exemption)(No.9) Order 2018

The MSC Malaysia status is awarded to both local and foreign companies that develop or use multimedia technologies to produce or enhance their products and services as well as for process development. The three categories of business entities eligible for this scheme are private limited companies, institutions of higher learning and incubators. The main fiscal tax reliefs[18] available for a MSC status company are as follow:

Location of Company	Tier	Tax relief
In designated premises within MSC Malaysia or Cybercities or Cybercentres	1	100% income tax exemption on statutory income derived from services related to promoted activities for a period of five years (extendable for another five years if conditions are fulfilled)
In other commercial premises within MSC Malaysia or Cybercities or Cybercentres	2	
Not subject to any location requirement	3	70% income tax exemption on statutory income for a period of 5 years. Able to apply for extension of exemption period if conditions are met.

Other privileges include unrestricted employment of local and foreign knowledge workers, freedom to source funds globally for investments, protection of intellectual property and cyber laws, no censorship of the Internet and globally competitive telecommunication tariffs. However, any statutory income a MSC status company derive from royalty and other intellectual property rights are excluded from this incentive scheme and remain subject to tax under the ITA.

Economic Corridors Incentive

The main five economic corridors introduced to bridge development imbalances in Malaysia are the Northern Corridor Economic Region (NCER), Iskandar Malaysia in Southern Johor (IRDA), East Cost Economic Region (ECER), Sabah Development Corridor (SDC) and Sarawak Corridor of

[18] Income Tax (Exemption) (No. 10) Order 2018

Renewable Energy (SCORE). Special incentives, on top of the existing incentives given by the Malaysian government as listed above, had been customised for the purpose of each economic region. However, some maybe mutually exclusive in which a taxpayer may only be eligible to claim either incentive but not both.

Currently, special legislations have been enacted only in respect of IRDA, ECER and SDC[19]. Guidance on the incentives available in these regions are also provided by the local authorities. Among others, the various tax incentives available to companies operating within the economic corridors include the following:

- 100% income tax exemption on statutory income for ten years in various sectors
- exemption from real property gains tax
- income tax exemption on rental or disposal of buildings
- withholding tax exemptions on technical fees or royalties paid to non-resident companies
- stamp duty exemption on instruments of transfer in relation to a qualifying activity
- deduction equivalent to value of investment made to a related company carrying out qualifying activity or a special qualifying activity

Further, companies carrying out manufacturing or services activities in less-developed areas are entitled further incentives such as 100% income tax exemption for up to 15 years and import duty exemption on materials and equipment used directly in the manufacturing or services activity.

Proposed G7 Global Tax Reform

The proposed tax reform consists of two pillars. Under Pillar One, the relevant companies would be required to pay tax in all countries they operate (including Malaysia), and not just where their headquarters are based in. Multinational

[19] Income Tax (Exemption) (No. 20) 2007, Income Tax (Exemption) (No.4) 2016, Income Tax (Exemption)(No.11) Order 2018, Income Tax (Exemption)(No.12) Order 2018 and Stamp Duty (Exemption)(No.8) Order 2018

enterprises with at least 10% profit margin would see 20% of their profit (above the margin) reallocated and taxed in the countries they operate in.

Under Pillar Two, a global minimum corporate tax of 15% is to be implemented in participating countries. Other countries will be given the right to impose a top-up tax to 15% on companies' income generated from another country that has a lower tax rate. This reform is aimed to prevent multinationals from shifting profits to low-tax countries.

Inevitably, the proposed global tax reform will have an impact on the operation of multinational companies in Malaysia. The imposition of a global minimum tax at 15% will neutralize tax incentives offered by Malaysia as the multinational will not be able to enjoy the 0% tax rate granted under one of the incentives schemes provided by the government. Additionally, the global minimum tax may put Malaysia in a "worse-off" position if she continues to provide tax incentives. If Malaysia continues to give tax incentives to multinational companies but they are being taxed at the rate of 15% in their parent company's jurisdiction, Malaysia will be left with a loss of tax revenue.

Although the proposed global tax reform aims to discourage multinational companies from shifting profits to tax havens and low tax jurisdictions and Malaysia, with a corporate tax rate of 24% may not be severely affected in that manner, the ability to attract investments through existing tax incentives will still be impacted. The provision of tax incentives may be less effective as companies will then take into account the 15% tax they have to pay in their parent company's jurisdiction regardless.

As such, the Malaysian Government may consider introducing non-tax related incentives such as grants and subsidies when further information regarding the implementation of the proposed global tax reform is available. As of July 2021, over 130 countries had principally agreed to the reform, and it is targeted to be implemented in 2023[20].

[20] https://www.oecd.org/newsroom/130-countries-and-jurisdictions-join-bold-new-framework-for-international-tax-reform.htm

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Senior Partner
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S Saravana Kumar
Partner
Tax, SST & Customs Practice
+603 6209 5404
sara@rdslawpartners.com

Conclusion

All in all, there are various tax incentives that have been introduced by the Malaysian Government as part of the efforts to attract local and foreign investments to stimulate economic growth. Having a good knowledge of the tax incentives available will be highly beneficial for companies to plan their businesses and develop their strategies accordingly.

However, with the proposed global tax reform gaining great support and potentially be implemented in two years' time, it is high time Malaysia puts her priority in highlighting its positive non-tax traits such as strategic location, abundance of natural resources, developed infrastructure and puts her best efforts in improving non-tax factors such as having stable governance, robust economic policies, availability of skilled workforce, strong research and development.

Tax incentives may be a relevant consideration, but it is not the only or main reason multinational companies choose to invest in Malaysia. Hence, it is pertinent that the Malaysian Government continue to strengthen the non-tax advantages and explore potential non-tax related incentives to continue to maintain as a favourable option for foreign investment in years to come.

Authored by Chew Ying, an associate from the firm's Tax, SST and Custom department.