

# MALAYSIA

## TRANSFER PRICING LANDSCAPE

**1967:** Introduced General anti-avoidance through Section 140 of the Malaysian Income Tax Act, 1967

**July 2003:** Transfer pricing guidelines were introduced by the Internal Revenue Board of Malaysia (IRBM) in July 2003.

**January 2009:** Section 140A of the Malaysian Income Tax Act, 1967 with specific transfer pricing provisions was introduced.

**May 2012:** The Income Tax (Transfer Pricing) Rules, 2012 enacted (with retrospective effect from 1 January 2009) provides insight on specific requirements with respective arm's length standard from a Malaysian transfer pricing perspective.

The Income Tax (Advance Pricing Arrangement) Rules, 2012 introduced.

**July 2012:** Revised transfer pricing guidelines issued which replaced the earlier guidelines. Advance Pricing Arrangement Guidelines, 2012 was introduced.

**May 2014:** Form C of the tax return form of 2014 introduced a new checkbox (Box R4) through which taxpayers had to declare whether transfer pricing documentation was prepared.



## Introduction

Section 140 of the Malaysian Income Tax Act, 1967 empowers the Director General to disregard certain transactions which are believed to have a direct or indirect effect of altering the incidence of tax. In such cases, the director general has powers to re-compute or adjust income and impose a tax liability on the person.

Furthermore, section 140A introduced with effect from 1 January 2009, requires taxpayers to determine and apply the arm's length price to controlled transactions. This section further allows the director general to disallow transactions (pertaining to goods, services, intangibles and financial transactions) undertaken between associated enterprises, if he has reasons to believe that such transactions are excessive or not at arm's length.

The introduction of the transfer pricing rules and guidelines in 2012 guided the taxpayers on the exact documentation requirements from a Malaysian transfer pricing perspective.

## Associated enterprise

According to the guidelines, two companies are regarded as associated enterprises if one company participates directly/indirectly in the management, control or capital of the other company; or in case the same persons participate directly/indirectly in the management, control or capital of both the companies.

Furthermore, any permanent establishment (PE) needs to be treated as distinct and separate enterprise from its head office or other branches.

## Exemptions from guidelines

Specific exemptions are provided from the applicability of guidelines in the following cases:

- Person being an individual not carrying on business;
- Person having business with gross income not exceeding MYR 25 million or total related party transactions not exceeding MYR 15 million;
- Person providing financial assistance not exceeding MYR 50 million;
- Transactions involving financial institutions;
- Transactions between two persons who are both assessable to tax in Malaysia and it can be proven that any adjustments made under guidelines will not alter the total tax payable by such persons.

## Arm's length principle

In line with the Organisation for Economic Co-operation and Development (OECD) guidelines, the IRBM adopts arm's length principle as a basis for benchmarking intra-group transactions.

## Transfer pricing documentation

### Contemporaneous documentation

Contemporaneous documentation needs to be prepared **at the point when the taxpayer is developing or implementing any arrangement or transfer pricing policy with its related parties.**

The list of documents required:

- Organisational structure
- Nature of business or industry and market conditions
- Details of controlled transactions
- Pricing policies
- Comparability, functional and risk analysis
- Selection of a transfer pricing method
- Application of the transfer pricing method
- Supporting documents for developing the transfer pricing analysis

Furthermore, taxpayers need to review the price at the end of the year and update the documentation if there are any material changes.

### Submission of documentation

Taxpayers are not required to submit documentation on an annual basis. However, it needs to be submitted to the IRBM within 30 days of the request.

### Selection of method

Although the taxpayer is given the right to choose any method, the guidelines encourage using transactional profit methods only in cases when traditional transactional methods cannot be reliably applied or cannot be applied at all.

Furthermore, guidelines specifically disregard methods that are based on global formulary apportionment on the convention that such arrangements are arbitrary and could not be considered a reliable approximate of arm's length conditions.

### Comparability period

For comparability analysis, multiple year data of comparables may be used. However, for benchmarking a controlled transaction, the results of uncontrolled transactions for the same base year must be taken.

## Certain specific transactions

### Intra-group services

Guidelines caution to check for non-chargeable (non-beneficial) elements in the following services:

- Shareholder activities;
- Duplicative services;
- Services that provide incidental/passive association benefits; or
- On-call services.

For intra-group services, the taxpayer needs to evaluate the following factors (benefit test):

- Economic or commercial value of benefits received from services;
- Willingness of independent enterprise to pay for similar services; and
- The charges for intra-group services must be consistent with the benefits received.

The guidelines further provide that for intra-group services, the service recipient may apply an external comparable uncontrolled price (CUP) method together with a benefit test. With regard to service provider, the guidelines suggest that both the CUP method and the cost plus method (CPM) may be applied.

### Cost contribution arrangements

The Malaysian guidelines accept intra-group cost contribution arrangements (CCA). To demonstrate whether CCA accords to arm's length principle, the following matters should be addressed:

- CCA should be entered into with prudent and practical business judgment.
- Reasonable estimation must be made for the expected benefit from CCA.
- Terms of the CCA should be agreed upon up-front and in accordance with economic substance, judged by reference to circumstances known or reasonably foreseeable at the time of entering into the arrangement.

### Intangibles (other than the CCA)

Ideally, the CUP method needs to be used in benchmarking transactions involving intangible properties. However, in cases where reliable comparables are not available, the taxpayer can apply the residual profit split method (PSM) or any other method.

### Intra-group loans

For intra-group loans, the CUP method is considered most reliable. Local indices such as the Kuala Lumpur Inter Bank Offered Rate (KLIBOR) may be readily used to benchmark intra-group loans.

## Reporting and compliance

### Income tax return

Income tax return should be filed within seven months of the end of the financial year of the company.

All Malaysian companies having related party transactions during the year are required to disclose their domestic and cross-border related party transactions under Part N of the income tax return (Form C).

Furthermore, Part R4 of Form C explicitly requires taxpayers to state whether documentation has been prepared or not.

### Additional disclosure forms

IRBM may ask taxpayer to provide additional details in **Form MNE** (cross-border transactions) or **Form JCK** (domestic transactions), as may be applicable. The taxpayer is required to provide such details within 30 days.

### Transfer pricing audit/assessment

The IRBM carries out two types of transfer pricing audits.

#### Desk audit

- A desk audit is conducted at IRBM's office, where, the taxpayer may be asked to provide information or even called for a meeting.
- A desk audit cases may be referred for a field audit action, if required.

#### Field audit

- A field audit is conducted at the taxpayer's premises subject to prior notice in this regard.



## APA and MAP procedures

The taxpayer may apply for a unilateral or bilateral Advance Pricing Agreement (APA) for a period of three to five years. Moreover, the taxpayer can also apply for rollback provisions for preceding financial years if it can be demonstrated that the facts and circumstances surrounding those years are substantially the same.

Only taxpayers who are a company or a PE of a company can apply for APA, if they fulfil the following criteria:

- The taxpayer has a turnover exceeding MYR 100 million; and the value of the proposed APA transactions exceeds the following limits:
  - for sales, if it exceeds 50% of the turnover;
  - for purchases, if it exceeds 50% of the total purchases;
  - for other transactions, if the total value exceeds MYR 25 million.

- All covered transactions must relate to income that is chargeable to tax in Malaysia.
- In cases involving financial assistance, where the value of transactions exceed MYR 50 million.

After entering into an APA, the taxpayer needs to file annual compliance reports for relevant transactions.

The taxpayer may also apply for a Mutual Agreement Procedure (MAP) within a specified time limit as may be applicable as per the relevant tax treaty. In case, the time limit is not specified under the relevant treaty, the time limit of three years, mentioned in Article 25 of the OECD's Model Tax Convention on Income and Capital shall prevail.

## Penalties and other consequences of non-compliance

Following penalties may be applicable:

Particulars	Rate of penalty (Percentage of tax adjusted)		
	Normal case	Voluntary disclosure after taxpayer has been informed but before the audit commences	Voluntary disclosure before the case is selected for audit
Understatement or omission of income	45%	35%	15%
Non-maintenance of contemporaneous documentation	35%	30%*	15%*
Documentation not prepared according to the guidelines	25%	20%	10%
Taxpayer exempt from guidelines but transfer prices not at ALP	25%	-	-

\*Upon voluntary disclosure, the taxpayer is still required to prepare transfer pricing documentation.

Furthermore, in cases of repetition of offence, the rate of penalty shall be increased by 20% as compared to the last penalty rate imposed for the previous offence but to a maximum of 100% of the amount of tax adjusted, where:

- The taxpayer obstructs or interferes with the transfer pricing audit; or
- The taxpayer fails to comply with the arm's length principle after the previous audit.

## BEPS/CbC applicability

Malaysia has formally announced to the implementation of Country-by-Country (CbC) reporting requirements in line with Action 13 of OECD/G20 Base Erosion and Profit Shifting (BEPS) Project. However, draft legislation in this regard is awaited.

Furthermore, it is important to note that on 27 January 2016, Malaysia became one of the signing members of the Multilateral Competent Authority Agreement (MCAA) which enables an automatic exchange of CbC information within its signing members.



# SUMMARY OF TRANSFER PRICING REQUIREMENTS

<b>Effective from</b>	1 January 2009
<b>Compliance requirements</b>	<ul style="list-style-type: none"><li>• All Malaysian companies having related party transactions during the year are required to disclose their domestic and cross-border related party transactions in the annual income tax return.</li><li>• Taxpayer must state whether documentation is prepared or not.</li><li>• Documentation compliance is required for taxpayers with:<ol style="list-style-type: none"><li>i. Gross income exceeding RM 25 million (USD 6.12 million), and total related party transactions exceeding RM 15 million (USD 3.67 million),</li><li>ii. For financial assistance, the threshold is RM 50 million (USD 12.23 million)</li></ol></li><li>• The taxpayer may be asked to submit further details on cross-border/ domestic transactions in applicable forms as and when required by the tax authorities.</li><li>• The income tax return needs to be filed within seven months of the end of relevant financial year.</li></ul>
<b>Penalties</b>	Stringent penalty norms divided between three scenarios, normal scenario, and voluntary disclosure after informing the taxpayer but before the audit commences and voluntary disclosure before the case selected for audit. Penalty is increased by 20% in case of a repetitive offence.
<b>Method and preference for comparable</b>	Five methods as defined by the OECD with guidance for methods to be selected for few specific transactions. Preference for local comparables along with usage of multiple year data.
<b>Peculiar features</b>	Contemporaneous documentation needs to be prepared at the point when the taxpayer is developing or implementing any arrangement or transfer pricing policy with its related parties.
<b>Safe harbour and APA</b>	The taxpayer may apply for a unilateral or bilateral APAs, for a period of three to five years. Only taxpayers who are a company or a PE of a company can apply for APA, if they fulfil certain criteria.
<b>BEPS/CbC applicability</b>	Formal announcement to implement CbC reporting requirements in line with Action 13 of OECD/G20 BEPS Project was made. However, draft legislation in this regard is awaited.



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