



Taxation of cross-border mergers and acquisitions

Malaysia

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Malaysia

Introduction

Malaysia is a member of the British Commonwealth and its tax system has its roots in the British tax system. The British introduced taxation to the Federation of Malaya (as Malaysia was then known) in 1947, during the British colonial rule with Income Tax Ordinance, 1947. The ordinance was repealed with the enactment of the Income Tax Act, 1967, which came into effect on 1 January 1968, and since then, further tax legislation has been introduced.

The current principal direct taxation legislation consists of the following:

- Income Tax Act, 1967 (ITA), which provides for the imposition and collection of income tax
- Real Property Gains Tax Act, 1976 (RPGT Act), which is imposed on profits from the disposal of real properties in Malaysia and shares in real property companies (RPC)
- Petroleum (Income Tax) Act, 1967, which is imposed on profits from petroleum operations
- Promotion of Investments Act, 1986, which provides for tax incentives for persons engaged in promoted industries or activities
- Stamp Act, 1949 (Stamp Act), which imposes stamp duty on various instruments.

In Malaysia, the Securities Commission is responsible for implementing guidelines for regulating mergers, acquisitions and takeovers involving public companies. The regulations for the banking and finance sectors are mainly the responsibility of the Central Bank of Malaysia (Bank Negara). Bank Negara is also responsible for currency flows to and from the country. For mergers and acquisitions (M&A) involving parties

undertaking manufacturing activities, the approval of the Ministry of International Trade and Industry may be required.

Guidance on government policies and procedures can be obtained from the Malaysian Investment Development Authority (MIDA) — formerly known as the Malaysian Industrial Development Authority — which is the government's principal agency for the promotion of the manufacturing and services sectors in Malaysia.

Recent developments

In a move to keep Malaysia competitive in the region, the country has gradually reduced its corporate tax rates from 27 percent in year of assessment (YA) 2007, to 26 percent in YA 2008, 25 percent for YA 2009–2015, and 24 percent for YA 2016 and later years.

In addition, the Malaysian government has implemented a Goods and Services tax (GST) from 1 April 2015.

Asset purchase or share purchase

Generally, in the Malaysian context, mergers and acquisition (M&A) transactions are undertaken via the acquisition of shares or a business (e.g. asset purchase).

Purchase of assets

Purchase price

Generally, the acquisition price is not deductible (it is a capital cost) except for the cost incurred to acquire qualifying assets in an asset purchase deal (as discussed later in this report).

Goodwill

For tax purposes, the amount of goodwill written off or amortized to the income statement of the company is non-deductible on the grounds that the expense is capital in nature.

Depreciation

The ITA contains provisions for granting initial and annual tax-depreciation allowances on qualifying capital expenditure incurred in acquiring or constructing industrial buildings

(as defined) and qualifying plant and machinery used for the purposes of the taxpayer's business (subject to certain conditions). The main rates of initial and annual allowances are as follows:

Type of allowance	Initial allowance	Annual allowance
Industrial building	10% of qualifying expenditure	3% of qualifying expenditure
Heavy machinery and motor vehicles	20% of qualifying expenditure	20% of qualifying expenditure
Plant and machinery (general)	20% of qualifying expenditure	14% of qualifying expenditure
Office equipment, furniture and fittings and others	20% of qualifying expenditure	10% of qualifying expenditure

Source: KPMG in Malaysia, 2016

In addition to these allowances, the ITA allows (among other things):

- a tax deduction for capital expenditure on replacement assets that have a life span of 2 years or less and are used for the purposes of the taxpayer's business (e.g. bedding and linen, crockery and glassware, cutlery and cooking utensils, and loose tools)
- accelerated capital allowance for information and communication technology (ICT) equipment (including computers and software), effective from YA 2009 to YA 2016
- a capital allowance equal to the amount of expenditure for small value assets that each cost up to 1,300 Malaysian ringgits (MYR) where the total capital expenditure of such assets generally does not exceed MYR13,000 (the limit of MYR13,000 does not apply to small and medium-sized enterprises)
- accelerated capital allowance for security and surveillance equipment (effective from YA 2008 to YA 2015).

Separate rates apply to certain capital expenditure in, among others, the plantation, mining, forestry, agriculture and hotel industries.

Balancing allowances or charges may be triggered when a taxpayer disposes of a qualifying capital item (e.g. industrial buildings, plant and machinery).

A balancing allowance arises when the asset's market value or sale price, whichever is higher, is lower than the asset's residual or tax written-down value. A balancing charge arises when the asset's market value or sale price, whichever is higher, exceeds the asset's residual or tax written-down value. However, the amount of balancing charges to be imposed is

limited to the amount of capital allowance claimed on the asset before its disposal. Capital allowances claimed on qualifying assets that are disposed of within 2 years may be subject to clawback at the discretion of the Inland Revenue Board (IRB). This typically applies on the disposal of luxury goods.

The provisions on balancing allowances, balancing charges and clawbacks are applicable unless the disposal falls within the ITA's controlled transfer provisions. In a controlled transfer situation, the assets are deemed to transfer at their respective residual values such that no balancing charges or allowances arise.

A controlled transfer situation occurs when:

- the seller of the asset is a person over whom the acquirer of the asset has control
- the acquirer of the asset is a person over whom the seller of the asset has control
- some other person has control over the seller and the acquirer of the asset
- the disposal is effected as a result of a plan of reconstruction or amalgamation of companies
- the disposal is effected by way of a settlement, gifts or devolution of the property in the asset on death.

Tax attributes

The main tax incentives available in Malaysia include pioneer status (an exemption based on statutory income) and investment tax allowance (based on capital expenditure).

These incentives are mutually exclusive and limited to promoted activities or products.

Another form of tax incentive is the reinvestment allowance (RA), which is available to resident companies in the manufacturing and agricultural sectors undertaking expansion, modernization, automation or diversification activities.

Any incentives granted to a company cannot be transferred to the acquirer of assets. Thus the acquirer in an asset deal may need to apply to the authorities for new incentives, where applicable.

Value added tax

In Malaysia, there is an indirect tax framework that consists of the following core taxes and duties:

- service tax (repealed as of 1 April 2015)
- sales tax (repealed as of 1 April 2015)
- import duty
- export duty
- excise duty.

GST was implemented as of 1 April 2015 to replace service tax and sales tax. GST is levied at 6 percent on the supply of goods and services made in Malaysia in the course or furtherance of a business by a GST-registered person unless such supplies are zero rated, exempted or given relief. GST is also charged on the importation of goods and services.

In a purchase of assets, it is important to determine whether the items purchased (e.g. machinery, equipment or raw materials) are exempt from sales tax (where such items were acquired prior to the implementation of GST), import duty or excise duty. Where there is such an exemption, the company purchasing the items must officially inform the Royal Malaysian Customs Department of the change in ownership.

For the purchasing company to enjoy the tax/duty exemption on the goods purchased, an application must be made to the Minister of Finance (MOF) to inform the MOF of the transfer of ownership and to obtain approval to extend the tax/duty exemption to the purchasing company.

Where the exemption is granted based on the same grounds as stated previously by the vendor company, the company purchasing the goods must adhere to the same conditions attached to the exemption (e.g. the machinery, equipment and raw materials must be used to manufacture the same finished product).

Typically, an asset sale triggers an obligation for the seller to cancel or modify existing indirect tax licenses and for the acquirer to apply for new licenses.

Transfer taxes

The stamp duty imposed on the disposal of property (except stock, shares, marketable securities and accounts receivable or certain book debts) is based on the value of the transaction. For every MYR100 or fraction thereof of the monetary value of the consideration or the market value of the property, whichever is greater, the rates of stamp duty are as follows:

- MYR1 on the first MYR100,000
- MYR2 on any amount over MYR100,000 but not exceeding MYR500,000
- MYR3 on any amount over MYR500,000.

The rates imposed on other instruments are outlined in the First Schedule of the Stamp Act.

Several kinds of relief are provided in the Stamp Act, including two key reliefs relating to M&A.

Section 15 of the Stamp Act provides relief from stamp duty in connection with a plan for the reconstruction or amalgamation of companies if the following conditions (among others) are met:

- The transferee company must be registered or incorporated in Malaysia, or have increased its capital with a view to acquiring the undertaking of, or not less than 90 percent of the issued share capital of, any existing company.

- Not less than 90 percent of the consideration for the acquisition (other than that relating to the transfer to, or discharge by, the transferee company of liabilities of the existing company) consists of:

- the issue of shares (when an undertaking is to be acquired) in the transferee company to the existing company or to holders of shares in the existing company
- the issue of shares (when shares are to be acquired) in the transferee company to the holders of shares in the existing company in exchange for the shares held by them in the existing company.

The approval of the collector of stamp duties is required, and anti-avoidance provisions under section 15 may claw back the stamp duty relief (if granted) under certain circumstances.

Section 15A(2) of the Stamp Act provides relief from stamp duty in the case of a transfer of property between associated companies on any instrument if the collector of stamp duties is satisfied that (among other things):

- the effect of the transaction is to transfer a beneficial interest in property from one company with limited liability to another company and the companies are associated (i.e. one company is the beneficial owner of at least 90 percent of the issued share capital of the other)
- a third company with limited liability is the beneficial owner of not less than 90 percent of the issued share capital of each of the companies.

There are also anti-avoidance provisions in section 15A.

The Stamp Act empowers the MOF to exempt specific transactions from stamp duty, but this power is rarely exercised.

Purchase of shares

Tax incentives

Tax incentives are granted to companies that undertake promoted activities. A change in ownership of a Malaysian company should not affect the tax incentive it enjoys as long as the company continues to carry out the promoted activity under the tax incentive.

However, there are instances where the Malaysian tax incentive is granted with equity conditions attached, whether directly or indirectly. In these cases, the change in ownership of the company enjoying the incentive may affect the grant of such incentives. As such, it is advisable to ascertain the tax incentives currently enjoyed by the target Malaysian company and any conditions attached to them.

Regulatory issues

Limitations on foreign ownership apply to some extent to a purchase of shares.

A locally owned company may deduct 20 percent of the cost of acquiring a foreign-owned high technology company each year over a period of 5 YAs (subject to certain conditions). This treatment is effective for applications received from 3 July 2012 to 31 December 2016.

Indirect tax issues

Compared to an asset purchase, indirect tax issues are less significant in the context of a share purchase. However, any historical liabilities that exist remain with the target company despite the change in ownership.

Tax indemnities and warranties

Tax indemnities and warranties are discussed in this chapter's section on tax clearances.

Tax losses

Losses and capital allowances not used in a YA can be carried forward indefinitely, provided the company is not dormant. If the company is dormant, it must satisfy the IRB that more than 50 percent of its shareholders on the last day of the basis period in which the losses or capital allowances arose are the same as on the first day of the basis period in which the unabsorbed losses or capital allowance are to be used.

Unused business losses may be set off against income from any business source. However, unused capital allowances may only be set off against income from the same business source in which the capital allowances arose.

Crystallization of tax charges

The advisors to the prospective purchaser may undertake a due diligence review of the books and records of the target company to ascertain the tax position of the target company and identify potential tax liabilities.

Pre-sale dividend

Generally, a company is allowed to pay pre-sale dividends. Dividend payments are discussed later in this report.

Malaysia does not impose withholding tax (WHT) on dividend payments.

Transfer taxes

Transfers of shares in an unlisted Malaysian company attract stamp duty at the rate of 0.3 percent of the value of shares transferred. Based on the guidelines issued by the IRB's Stamp Duty Unit on 21 April 2001, the value of shares transferred for stamp duty purposes is the highest value of the following:

- par value
- net tangible assets (NTA)
- price-earnings multiple or price-earnings ratio
- actual sale consideration.

The transfer of securities on the Central Depository System does not attract ad valorem stamp duties at 0.3 percent; instead, the contract notes may attract stamp duty at 0.1 percent. However, according to Stamp Duty Remission Order 2003, all contract notes relating to the sale of any shares, stock or marketable securities listed on a stock exchange approved under subsection 8(2) of the Securities Industry Act 1983 are waived from stamp duty in excess of MYR200, calculated at the prescribed rate in item 31 of the First Schedule to the Stamp Act.

Reliefs available for stamp duty and transfer taxes are discussed earlier in this report.

Tax clearances

It is seldom possible to obtain a clearance from the IRB (or from the Royal Malaysian Customs Department) giving assurance that a potential Malaysian target company has no tax arrears without tax or customs audits taking place. Therefore, it is usual to include tax indemnities and warranties in the sale agreement. The extent of the indemnities or warranties is subject to negotiation between the vendor and purchaser.

As noted, the advisors to the prospective purchaser may undertake a due diligence review of the books and records of the target company to ascertain the tax position of the target company and to identify potential tax liabilities.

Choice of acquisition vehicle

Local holding company

Foreign companies commonly set up Malaysian-resident holding companies to acquire shares or assets in Malaysia. Regardless of where a holding company is incorporated, it is considered a tax-resident in Malaysia if it is managed and controlled in Malaysia. Generally, a company is regarded as being managed and controlled in Malaysia if its directors' meetings are held there.

Historically, Malaysia adopted the imputation system of dividend payments, in which the corporate income tax paid by a company on its profits was fully passed on or imputed to the shareholders when a dividend (other than an exempt dividend) was paid. Therefore, the dividend was paid net of tax but had an imputation tax credit attached. A company receiving taxable dividends from a Malaysian resident company was taxable at the appropriate corporate income tax rate but could claim the tax credit attached to the dividend to offset the resulting tax liability. Thus, one advantage of using a Malaysian resident holding company to hold shares in a Malaysian resident target company was the ability to claim a refund of tax credits when there was sufficient interest cost to offset the taxable dividend income.

As of 1 January 2008, a single-tier system replaced the imputation system. Under the new system, the tax payable by a resident company constitutes a final tax. Dividends paid under the single-tier system are tax-exempt for the shareholders. Transitional provisions allowed the imputation system (with some amendments) to be used until 31 December 2013. Under the single-tier system, tax relief can no longer be obtained by offsetting interest expense against dividend income because dividends are tax-exempt. Surplus expenses in holding companies, including those listed on Bursa Malaysia, cannot be carried forward.

Issues of interest restriction and allocation can arise when a company has an interest expense and a variety of income-producing and non-income-producing investments. As of 1 January 2009, thin capitalization and transfer pricing provisions have been introduced to the ITA.

Foreign-sourced income received in Malaysia by a resident company (other than a resident company carrying on the business of banking, insurance, shipping or air transport) is exempt from tax (with only limited exemptions for banking businesses). Hence, it may be advantageous to use a Malaysian holding company to hold a foreign investment, as foreign-sourced dividend income (including trading profits from a foreign branch) and gains on the sale of subsidiaries are generally not subject to tax. However, interest costs and other costs attributed to foreign-sourced income incurred by the Malaysian holding company to fund the foreign investment would be wasted.

In relation to thin capitalization, section 140A(4) of the ITA, which has effect from 1 January 2009, provides that where the value of all financial assistance to an associated person is excessive in comparison to the fixed capital of the recipient of the financial assistance, the interest, finance charge or other consideration payable on the excess value is not deductible.

Under section 140A(5) of the ITA, an associated person is one who has control over the recipient of the financial assistance, is controlled by the recipient of the financial assistance, or, together with the recipient of the financial assistance, is controlled by a third person. It should not be assumed that control refers only to shareholding control.

Although section 140a(4) was technically effective from 1 January 2009, its actual implementation has been deferred to the end of December 2017.

Non-resident intermediate holding company

Malaysia has concluded agreements for the avoidance of double taxation agreements with an extensive number of countries. (Not all have been ratified, however, and not all are comprehensive). For the list of treaties and reduced withholding tax rates at the end of this report.

Local branch

In Malaysia, both a branch and a subsidiary are generally subject to the same tax filing and payment obligations.

Malaysia does not impose branch profits tax on the remittance of branch profits. Therefore, the profits of a local branch may be freely repatriated back to its head office without attracting further tax liabilities in Malaysia.

However, where profits are repatriated in the form of (among other things) royalties, interest or payments for management fees, Malaysian WHT may be applicable.

Limited liability partnership

The Limited Liability Partnerships (LLP) Act 2012 introduced the concept of an LLP.

For income tax purposes, an LLP is treated as a separate legal entity from its partners. The income of the LLP is taxed at the LLP level. Consequently, the partners are not liable to tax on their share of income from the LLP (whether distributed or not).

Joint venture

A joint venture can be either unincorporated or incorporated. If unincorporated, it needs to be determined whether it is a partnership.

A partnership is not taxed as an entity. Instead tax is charged at the partners' level on their share of the adjusted income from the partnership. The divisible income is allocated among the partners according to their profit-sharing formula, and the capital allowances (also allocated according to the profit-sharing formula) are deducted from the partners' chargeable income. If there is a partnership loss, each partner may offset their share of the loss against their income from other sources.

Choice of acquisition funding

The financing of a transaction can be in the form of shares or loan notes, cash, asset swaps or a combination of different types of consideration.

Debt

Where the consideration is in the form of cash, the acquirer may have to raise external borrowings, which may involve a variety of regulatory approvals.

Incidental costs of raising loan finance, such as legal, rating and guarantee fees, are viewed as capital costs and so are non-deductible (except for certain Islamic financing and asset-backed securitizations).

Borrowings from a non-resident may require exchange control approval.

Malaysia introduced thin capitalization legislation with effect from 1 January 2009. However, the implementation of the legislation and publication of the related detailed rules, including the permitted ratio, has been deferred to the end of December 2017.

Investment in foreign currency asset

Malaysian resident corporations with domestic borrowings that wish to invest in 'foreign currency assets' are required to seek prior approval from Bank Negara for overseas investments through conversion of MYR exceeding MYR50 million per calendar year. The MYR50 million refers to investment abroad by the resident entity and other resident entities within its group of entities with a parent-subsidiary relationship. The threshold for Malaysian-resident individuals is MYR1 million per calendar year.

Malaysian residents with domestic borrowings are free to invest in foreign currency funds maintained onshore or offshore. Malaysian residents with no domestic borrowing are also free to invest abroad.

Foreign currency borrowing and ringgit borrowing

A resident company is allowed to borrow any amount in foreign currency:

- from licensed onshore banks
- from resident and non-resident entities within its group
- from its resident and non-resident direct shareholders
- through the issuance of foreign currency debt securities to another resident.

A resident company may obtain foreign currency credit facilities of up to MYR100 million equivalent in aggregate from other non-residents that are not part of its group of entities. The limit is based on the aggregate borrowing for the group of resident entities with a parent-subsidiary relationship.

Borrowing is defined as any credit facility, financing facility, trade guarantee or guarantee for payment of goods, redeemable preference share, Islamic redeemable preference share, private debt security or Islamic private debt security other than (among others):

- operational leasing facilities
- factoring facilities without recourse
- performance or financial guarantees.

Deductibility of interest

Deductibility of interest costs is governed by sections 33(1) and 33(2) of the ITA. A deduction may be claimed under section 33(1) for an interest expense that is wholly and exclusively incurred in the production of a company's gross income. A company with an ongoing business may deduct the interest expense pursuant to the same section if the expense

relates to a loan used for the working capital purposes of the company. An investment holding company may deduct its interest expense against its taxable investment income pursuant to section 33(1).

However, under the single-tier system (discussed earlier), the interest cost incurred by an investment holding company would be lost because the investment income (i.e. dividend income) would be tax-exempt.

The deductibility of the interest expense would also be restricted by section 33(2), when monies borrowed are used directly or indirectly for non-trade purposes (e.g. investments or loans other than for business purposes). This section applies to companies with ongoing businesses that undertake non-business investments. The interest restricted can only be allocated and set off against the taxable income, if any, derived from the non-business investments or loans to which the monies have been applied; the interest expense cannot be set off against business profits. Inefficiencies could arise where these non-trade applications do not produce sufficient taxable income because the restricted interest expense is then lost. For companies with interest expense and non-trade applications, managing interest restriction can be a major issue.

With effect from YA 2014, a taxpayer is only eligible to deduct interest from money borrowed against its income when such interest is due to be paid. If interest is only accrued in the books of a taxpayer with no stipulated date of payment, interest accrued in that YA is not deductible.

There are also transfer pricing and thin capitalization issues to consider (discussed in this chapter's section on local holding companies).

Withholding tax on debt and methods to reduce or eliminate WHT

Interest paid or credited to any person who is not tax-resident in Malaysia, other than interest attributable to a business carried on by such person in Malaysia, is generally subject to Malaysian WHT at the rate of 15 percent on the gross amount. A tax treaty between Malaysia and the recipient's country of residence may reduce the rate of WHT. A certificate of residency of the non-resident company must support the reduction. Interest payments to non-resident companies without a place of business in Malaysia in respect of sukuk issued in any currency and debentures issued in MYR (other than convertible loan stocks approved or authorized by, or lodged with, the Securities Commission or securities issued by the government of Malaysia) are exempt from WHT. ('Sukuk' are certificates of equal value that evidence undivided ownership or investment in assets using Shariah principles and concepts endorsed by the Shariah Advisory Council.)

The following interest paid or credited to a non-resident is also exempt from WHT:

- interest paid or credited to any person in respect of sukuk originating from Malaysia other than convertible loan stock issued in any currency other than MYR and approved or authorized by, or lodged with, the Securities Commission or approved by the Labuan Financial Services Authority
- income of a unit trust in respect of interest derived from Malaysia and paid or credited by any bank or financial institution licensed under the Banking and Financial Institutions Act, 1989, the Islamic Banking Act, 1983, or any development financial institution regulated under the Development Financial Institutions Act 2002.

The tax withheld must be remitted to the IRB within 1 month of the earlier of the paying or crediting of such amount. If not, a penalty of 10 percent of the amount unpaid may be imposed and deduction for the interest expense is disallowed until the penalty and WHT are settled.

As of 1 January 2011, the IRB may impose a penalty for an incorrect return if a tax deduction on interest expense is claimed and the WHT and penalty are not paid by the due date for submission of the tax. Instead of borrowing directly from an offshore location, it may be possible to arrange funding through Labuan. Interest payments to a Labuan company are not subject to WHT (provided that the recipient is a Malaysian tax-resident). Exchange control approval may be required.

Checklist for debt funding

Where a Malaysian company is considering debt funding, the following issues should be considered (among others):

- Malaysian WHT on interest paid or credited to a non-resident lender and whether there are ways to minimize or mitigate the impact (as discussed earlier in this report)
- where the debt funding is to be received from a related party, issues relating to the thin capitalization rules (implementation deferred to the end of December 2017), transfer pricing (discussed later in this report) and deductibility of interest (discussed earlier)
- Malaysian exchange controls (discussed earlier).

Equity

Companies must pay registration fees on the amount of their authorized share capital. The registration fee starts at MYR1,000 for an authorized share capital of not more than MYR400,000 and increases gradually to MYR70,000 for an authorized share capital above MYR100 million. The registration fee is only deductible for companies having an authorized capital of up to MYR2.5 million on the incorporation date.

The tax implications of dividend payments are discussed in this chapter's section on local holding companies.

Hybrids

A commonly used hybrid is the redeemable preference share (RPS), which is usually treated as a form of equity for tax purposes. The use of the RPS allows for flexibility of redemption, which is generally regarded as a repayment of capital (assuming it occurs on a one-off basis).

The RPS can be redeemed either out of profits that would otherwise be available for dividends or out of the proceeds of a fresh issue of shares made for the purposes of the redemption. When the RPSs are redeemed other than from the proceeds of a fresh issue of shares, an amount equal to the nominal value of the shares redeemed has to be transferred out of profits otherwise available for dividend distribution to a capital redemption reserve.

The IRB has indicated that RPS distributions generally are not treated as interest for tax purposes.

Discounted securities

Where discounted securities are issued, it must be established whether the discount element is in the nature of interest. If so, refer to the discussions earlier in this report on debt funding.

Deferred settlement

Generally, tax relief under the ITA is claimed when the relevant cost has been incurred, even where the payment is deferred. Generally, Malaysian WHT obligations crystallize on the earlier of paying or crediting a non-resident.

Other considerations

Concerns of the seller

RPGT is a capital gains tax imposed on gains on disposals of real property located in Malaysia or shares in an RPC. An RPC is a company that owns real property in Malaysia or shares in other RPCs to the extent the value of its real property or shares (in other RPCs) or both, exceeds 75 percent of the total tangible asset value of the company at the relevant time.

As of 1 January 2014, chargeable gains are taxed at the following rates:

- 30 percent for disposals within 3 years after acquisition
- 20 percent for disposals in the 4th year after acquisition
- 15 percent for disposals in the 5th year after acquisition
- 5 percent for disposals more than 5 years after acquisition
- exempt for disposals by an individual who is a Malaysian citizen or permanent resident more than 5 years after acquisition
- for an individual who is not a Malaysian citizen or permanent resident, the rate is 30 percent for disposals within 5 years after acquisition and 5 percent for disposals more than 5 years after acquisition.

Generally, a gain arises when the disposal price exceeds the acquisition price of the real property or the shares in an RPC.

The seller and acquirer of a chargeable asset must each make a return to the IRB within 60 days of the date of disposal (as defined) in the prescribed form, supported by the details stipulated in the form. Where the market value of the asset is used, a written valuation by a valuer must be submitted.

The purchaser is required to withhold and remit to the IRB the lower of the whole amount of the money received or 3 percent of the total value of the consideration.

Exemptions

Where, with the prior approval of the Director General of the IRB, a chargeable asset is transferred between companies and the transferee company is resident in Malaysia, the transfer is treated as one from which no gain or loss arises in any of these circumstances:

- The asset is transferred between companies in the same group to bring about greater efficiency for a consideration consisting substantially of shares (i.e. at least 75 percent) and the balance in cash.
- The transfer is a result of a plan of reorganization, reconstruction or amalgamation.
- A liquidator of a company distributes the asset and the liquidation of the company was made under a plan of reorganization, reconstruction or amalgamation.

The Director General shall not pre-approve the transfer or distribution of an asset under the last two categories above unless satisfied that the asset is transferred to implement a plan that complies with the government's policy on capital participation in industry. Under these approved transfers, the date of the transferee's acquisition of the chargeable asset is deemed to be the original date of acquisition of the chargeable asset by the transferor. Various anti-avoidance provisions may apply.

The RPGT act empowers the MOF to exempt specific transactions from RPGT, but this power is rarely exercised in practice.

Group relief/consolidation

The concept of grouping for tax purposes in Malaysia was introduced for selected industries, such as forest plantations and rubber plantations, and selected products in the manufacturing sector, such as biotechnology, nanotechnology, optics and phonics, as well as for certain food products. As of YA 2006, group relief is extended to all other companies.

A company resident and incorporated in Malaysia may now surrender up to 70 percent of its adjusted loss for the basis period to one or more related companies resident and incorporated in Malaysia. To qualify for this treatment, there must be at least 70 percent common ownership through

Malaysian companies. There are various restrictions on how tax losses can be transferred; these include definitions of 'group' and a requirement for common year-ends. Companies enjoying certain tax incentives are ineligible.

Transfer pricing

Transfer pricing is an issue of concern to taxpayers in Malaysia in the context of related-party transactions.

In July 2003, the IRB issued formal transfer pricing guidelines, which broadly follow the arm's length principle established under the Organisation for Economic Co-operation and Development's (OECD) transfer pricing guidelines. Generally, the OECD and IRB guidelines prescribe that all transactions between associated parties should be on an arm's length basis.

The IRB guidelines cover transactions between:

- associated enterprises within a multinational group where one enterprise is subject to tax in Malaysia and the other enterprise is located overseas
- associated companies within Malaysia.

The scope of the guidelines includes transactions involving lending and borrowing money.

As of 1 January 2009, the Director General of the IRB has been accorded the power (under section 140A of the ITA) to adjust the transfer price of transactions between associated persons when they are of the opinion that the transfer price is not at arm's length. Thus it is increasingly important that taxpayers can demonstrate that their pricing of goods and services with associated persons is at arm's length.

Taxpayers must ensure that they have sufficient contemporaneous documentation to substantiate the arm's length nature of their transfer prices in accordance with the MOF's Income Tax (Transfer Pricing) Rules 2012.

To enhance certainty on pricing issues for intercompany transactions, the government has introduced an advance pricing arrangement (APA) mechanism. The APA provides a means to predetermine prices of goods and services to be transacted between a company and its associated companies for a specified period. APAs offer considerable security in terms of transfer pricing, although the timeframe to negotiate and conclude the APA should be considered.

For purposes of the APA program, the MOF issued Income Tax (Advance Pricing Arrangement) Rules 2012, along with revised Transfer Pricing Guidelines 2012 and Advance Pricing Arrangement Guidelines 2012.

In order to further monitor and tighten compliance with transfer pricing requirements, the corporate tax return form incorporates a new check box for corporate taxpayers to declare whether transfer pricing documentation has been prepared.

Dual residency

Under the ITA, a holding company is considered tax-resident in Malaysia if it is managed and controlled in Malaysia, regardless of where it is incorporated. Generally, a company is regarded as being managed and controlled in Malaysia if its directors' meetings are held there.

It may also be possible that a foreign company may be viewed as a tax-resident in the jurisdiction of its incorporation.

An applicable tax treaty may resolve issues arising due to a company having dual residency.

Foreign investments of a local target company

Generally, Malaysian companies are allowed to undertake foreign investments (bearing in mind the comments in this report in the section on investment in foreign currency assets).

As mentioned above, foreign-sourced income received in Malaysia by a resident company is exempt from tax unless the recipient carries on the business of banking, insurance, shipping or air transport (with limited exemptions for banking businesses). However, the non-deductibility of costs attributable to foreign-sourced income should be considered.

Tax-neutral reorganizations or mergers

Malaysia does not have a capital gains tax regime except for RPGT, which applies to transactions relating to land and shares in RPCs where such transactions are not subject to the ITA.

For reorganizations or mergers, the Malaysian tax regime allows limited exemptions in the following scenarios:

- Where the transfer of assets for which capital allowances (tax depreciation) have been claimed falls within the ITA's controlled transfer provisions, the assets are deemed to be transferred at their respective tax residual values such that no balancing charges or allowance arises.
- Where the transfer of assets or shares falls within sections 15 or 15A of the Stamp Act and meets the relevant conditions therein, the transaction is relieved from stamp duty.
- The MOF is empowered to exempt specific transactions from stamp duty, but this power is rarely exercised.
- The government may issue specific exemptions from specific taxes (e.g. income tax, stamp duty and RPGT) from time to time by way of statutory orders.
- In relation to RPGT, where, with the prior approval of the Director General of the IRB, a chargeable asset is transferred between companies and the transferee company is resident in Malaysia, the Director General shall treat the transfer as though no gain or loss has arisen in any of these circumstances:
 - the asset is transferred between companies in the same group to bring about greater operational efficiency for a consideration consisting substantially of shares (i.e. not less than 75 percent in shares) and the balance in cash

- the transfer is a result of a plan of reorganization, reconstruction or amalgamation
- a liquidator of a company distributes the asset and the liquidation of the company was made under a plan of reorganization, reconstruction or amalgamation.

For transfers under the second and third bulleted items, the scheme concerned must comply with the government's policy on capital participation in industry.

Approval is at the IRB's discretion, and various conditions must be met.

The RPGT act empowers the MOF to exempt specific transactions from RPGT, but this power is rarely exercised.

Comparison of asset and share purchases

Advantage of asset purchases

- The purchase price of qualifying assets (or a proportion) may be depreciated for tax purposes in the form of capital allowances.
- Liabilities and business risks of the vendor company are not transferred.
- Possible to acquire only certain parts of a business.
- Interest incurred to fund the acquisition of plant, equipment and other assets that will be used in the trade or business is generally tax-deductible.
- Purchaser may claim RA if it has incurred qualifying capital expenditure for the purposes of a qualifying project and has operated in that business for at least 36 months. Where the asset is disposed of within a period of 5 years from the date of purchase of the asset, the RA claimed by the seller is clawed back. Where the assets for which the RA has been claimed are acquired under a controlled transfer in which the transferor has previously claimed RA, the purchaser cannot claim RA on the same assets.
- Purchaser may be able to claim new incentives, where applicable.

Disadvantages of asset purchases

- Possible clawback of capital allowances claimed by the vendor in the form of a balancing charge.
- Clawback of RA, if the qualifying asset is disposed of within 5 years from the date of acquisition.
- Higher stamp duties on the transfer of certain assets.
- Benefits of any losses or unused tax attributes remain in the vendor company.
- Benefits of incentives remain in the vendor company.
- Possible need to cancel and apply for various indirect tax licenses.

Advantages of share purchases

- No capital allowance or balancing charge clawbacks on vendor and no withdrawal of RA.
- Purchaser may be able to use and benefit from unused tax attributes and, tax incentives of the target company.
- Lower stamp duties payable on the transfer of shares compared with other physical assets.
- Target company may continue to enjoy tax incentives.

Disadvantages of share purchases

- Purchaser may acquire historical tax and other liabilities.
- No deduction or depreciation allowances (capital allowances) are available for the purchase cost of shares.
- No re-basing of underlying assets.
- Purchaser may not be able to use the unused tax losses or capital allowances available in the target company where there is a substantial change in shareholders. However, this only applies to dormant companies.
- Deductions for interest incurred to fund the acquisition of shares subject to restriction.

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