

Malaysia Enacts Finance Act 2017 – Expanded Scope of Withholding Tax

On 16 January 2017, Malaysia enacted the Finance Act 2017, effective as of 17 January 2017, incorporating changes on the scope of Withholding Tax (WHT) on technical services and royalties and further clarifications on penalty provisions for Country-by Country Reporting (CbC reporting).

The key changes with regard to WHT are the following:

- The scope of WHT on technical services has been expanded; henceforward technical services rendered by a non-resident taxpayer to a Malaysian resident are subject to WHT regardless where the services were physically performed.
- The definition of royalty has been expanded to include items such as software and communication via satellite. Such amounts are from now on subject to 10 % WHT which may be reduced under tax treaties.

1. CHANGES IN THE WHT REGIME

Expanded Scope of Technical Services

Technical services are defined as technical advice, assistance or services in connection with technical management or administration. Technical management comprises amongst others the provision of marketing, architectural, computer programming, legal services and the supply of technical and software personnel. The term “administration” includes amongst others planning and co-ordination, financial management consultation. However, day to day administrative work, such as bookkeeping and other routine services (no specialized knowledge, skills or expertise are needed) does not fall under the category “administration”; those amounts are not subject to WHT.

Under the previous WHT regime payments made by a Malaysian resident taxpayer to a non-resident taxpayer for technical services were subject to WHT only if the services had been physically performed in Malaysia. Therefore, in order to calculate the correct amount subject to WHT a detailed break-down of the service fee was necessary.

From now on all payments made by a Malaysian resident taxpayer to a non-resident taxpayer for technical services are subject to 10 % WHT regardless where the services are physically performed.

The following examples illustrate the changes:

1. A UK based company is engaged in providing technical (architectural) services in connection with a hospital development in Kuala Lumpur. For rendering the services, staff of the UK firm will be traveling to Kuala Lumpur for on-site visits and discussions with local business partners. However, the main part of the requested work including drawing the design and construction plans will be performed in the UK office.

Under previous Income Tax Act rules the service fees paid to the UK firm would have been subject to WHT insofar as the fees relate to the services rendered in Malaysia (e.g. service fees related to on-site visits).

Henceforth, the entire service fee is subject to WHT. The Malaysian service recipient has to withhold the WHT of 10 % on the whole amount and has to remit it to the Inland Revenue Board (IRB).

2. A Singapore based legal firm provides legal services to a Malaysian taxpayer, the services have been wholly performed in the Singapore offices.

Previously, the service fee paid to the legal firm was not subject to WHT. Under the new rules the Malaysian service recipient has to withhold 10 % WHT on the whole amount.

Expanded Definition of Royalty

The Finance Act also expands the definition of “royalty” subject to WHT. Henceforward, the term royalty includes any consideration for the right to use software, the reception of or the right to receive visual images or sounds transmitted to the public by satellite, cable, fibre optic or similar technology or in connection with television or radio broadcasting. Further, royalties paid for the use of or the right to use radio frequency spectrums.

The expansion of the scope of WHT on technical services and the expansion of the royalty definition may impact the business activities of Malaysian taxpayers significantly. As the new rules do apply since 17 January 2017 Malaysian taxpayers should

- review existing service agreements with non-resident service providers whether the calculation of WHT needs to be adjusted in order to comply with the regulations.

- consider the changes in current or future negotiations of new or renewed service agreements.
- review existing royalty agreement as to whether the calculation of WHT has to be adjusted considering the broader royalty definition.

2. PENALTY PROVISION FOR CBC REPORTING

On 23 December 2016 Malaysia issued the Income Tax Rules 2016 to implement CbC reporting requirements in line with Base Erosion Profit Shifting (BEPS) Action 13. Accordingly, Malaysian taxpayers with a consolidated turnover of 750 mEUR have to file a CbC report in which amongst others, the following information for each group entity has to be shown: income allocation, taxes paid, headcount, business activities, profit (or loss), tangible assets others than cash and cash equivalents.

In order to ensure compliance with the changes, penalties for the failure to furnish CbC reports, incorrect reporting or omission of information have been published. Thus, failure to comply with the rules may result in a fine between 20,000 RM and 100,000 RM and/or imprisonment for a maximum of 6 months.

Luther LLP

Heike Riesselmann, German Certified Tax Advisor
Manager – International Tax Services

Phone: + 65 6408 8067

Mobile: +65 9489 0338

heike.riesselmann@luther-services.com

Philipp Kersting

Director

Luther Corporate Services Sdn Bhd, Kuala Lumpur

Phone +60 (0)3-21660085

Mobile +60 1228 751 97

philipp.kersting@luther-services.com

Copyright

These texts are protected by copyright. You may make use of the information contained herein with our written consent, if you do so accurately and cite us as the source.

Please contact the editors in this regard.

Please contact the team for further information. All contact details can be found on our website www.luther-lawfirm.com.

Disclaimer

Although every effort has been made to offer current and correct information, this publication has been prepared to give general guidance only. It will not be up-dated and cannot substitute individual legal and/or tax advice. This publication is distributed with the understanding that Luther, the editors and authors cannot be held responsible for the results of any actions taken on the basis of information contained herein or omitted, nor for any errors or omissions in this regard.

If you do not want to receive this newsletter in future, please send an e-mail to haslinda.hamid@luther-lawfirm.com