

e-TAX NEWS

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WITHHOLDING TAX - INCOME TAX [EXEMPTION] (NO.9) ORDER 2017

A quick recap of the withholding tax development in the recent months. The scope of withholding tax has been widened to include both services rendered onshore and offshore that came into effect on 17 January, 2017 under the Finance Act 2017. Income Tax [Exemption] (No.9) Order 2017 (PU Order) has been issued on 24 October, 2017 and will be effective retrospectively from 6 September, 2017.

Under the above PU Order, the following income received by a non-resident person will not be subject to withholding tax if the services are rendered outside Malaysia:-

a) Section 4A(i) of the Income Tax Act, 1967

- Services rendered in connection with the use of property or rights belonging to the non-resident; or
- The installation or operation of any plant, machinery or other apparatus purchased from the non-resident.

b) Section 4A(ii) of the Income Tax Act, 1967

- Technical advice, assistance or services, rendered in connection with technical management or administration of any scientific, industrial or commercial undertaking, venture, project or scheme.

The above PU Order has reinstated the previous withholding tax treatment for “technical services” where only services rendered in Malaysia will be subject to withholding tax in Malaysia. In other words, no withholding tax will be imposed on services rendered outside Malaysia by the non-resident.

Please refer to the following table to ease your understanding:-

Period	Section 4A(i) and 4A(ii)	Implication
Prior to 17 January 2017	Services performed outside Malaysia	Not subject to withholding tax
17 January 2017 - 5 September 2017	Services performed outside Malaysia	Subject to withholding tax
6 September 2016 onwards	Services performed outside Malaysia	Not subject to withholding tax

PKF comments:

The above is indeed a good news to many businesses in Malaysia, especially multi-national companies, which were caught off guard on the re-imposition of withholding tax on offshore services. With the latest development on the withholding tax landscape in Malaysia, it appears that withholding tax will be a main area of focus by the Inland Revenue Board (IRB) and there are many contentious issues that have yet to be addressed which we summarised below:-

- The wide interpretation of the scope of “royalty” by the IRB especially those involved the usage of online services or support, thus the scope of services may be potentially be interpreted by the IRB as within the ambit of “royalty” and be subject to withholding tax.
- Intra-group services charged by foreign holding company may have both elements of services and royalty, the basis of charge for both elements must be clearly identified based on commercially justifiable basis in order to avoid any future dispute with the IRB.
- The withholding tax exemption is provided by way of a PU Order where the amendment to Section 15A of the Income Tax Act, 1967 (ITA) remains unchanged. Section 15A of the ITA was amended in Finance Act 2017 to allow the imposition of withholding tax on technical services for both services rendered in Malaysia and outside Malaysia. Therefore, is the above withholding tax exemption granted by the IRB a temporary measure which may be revoked in the near future?
- What supporting documentation will be requested or verified by the IRB during a tax audit based on the above development on the withholding tax landscape in Malaysia? We believe the IRB will conduct more stringent and detailed verification of the supporting documents in order to understand the substance of the services rendered. For multi-national companies, will the visit of any personnel from the holding company be subject to dispute of the services rendered in Malaysia and be subject to withholding tax?
- If both elements of onshore and offshore services exist, will the IRB challenge the basis of allocation adopted and what supporting documentation is required to be maintained by the taxpayer in order to justify the basis of apportionment adopted?
- Any transitional provision will be issued by the IRB to address the issues for the payment made prior to 6 September, 2017? What approach should be adopted by the taxpayer in the time being until such announcement is made?
- Malaysia has a wide treaty network with many foreign countries and Double Tax Agreements prevail over local tax laws. However, due to the wide and different interpretation adopted by the IRB, what is the tax risk of the taxpayer that adopts the treaty protection which is not in line with the IRB's interpretation?

With the latest development on the withholding tax landscape in Malaysia, taxpayers are advisable to review their cross-border contractual and payment arrangements to assess their withholding tax risk has been properly identified and sufficient supporting documentation is maintained to defend against any dispute with the IRB as we believe the IRB may adopt a more stringent requirement to justify the services as rendered outside Malaysia.

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