

# e-tax news



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## Summary of Changes in Labuan Tax Legislation

In line with Malaysia's commitments as a member of the Inclusive Framework on Base Erosion and Profit Shifting (BEPS) to address tax evasion and harmful tax practices under BEPS Action 5: Harmful Tax Practices, significant changes have been made to the Labuan tax legislation including the elevation of substantial activities requirements in Labuan. As a result, the following tax legislations have been enacted:

- 1) Labuan Business Activity Tax (Requirements for Labuan Business Activity) Regulations 2018 ("Regulations") which became effective from 01 January 2019; and
- 2) Labuan Business Activity Tax (Amendment) Act 2020 ("LBATAA") which gazetted on 10 February 2020 and became effective on 11 February 2020.

which had brought enormous changes to the landscape of Labuan tax regime than ever before.

The major changes of the tax legislation in Labuan are summarised below to ease your reference:

### Compliance & Reporting for Labuan entities

- i. **Form LE1** - Return of Profits by A Labuan Entity Under Section 5 And Subsection 2B(1A) of the Labuan Business Activity Tax Act 1990

Main changes of Labuan tax return form and its tax implications:

	New LE 1	Old LE 1	Our Comments
A5 – Employer’s no.	Applicable	N/A	Effective from YA 2020, a Labuan entity is required to comply with substantive requirement (i.e. minimum number of employee). Thus, a Labuan company is now required to submit the employer’s tax return (Form E).
A 12 - Net profit as reflected in the audited accounts in respect of the Labuan business activity (Labuan trading or Labuan non-trading activity)	Applicable	N/A	<p>A Labuan company may have more than one trading and/or non-trading activities that generate its business income. Hence, there is a new requirement to ensure the selection of the correct business code for each business activity and the applicable tax rate as per the new LE 1 Form. The selection of the correct business code is not reference to its principal activity.</p> <p>Thus, segregation of the income and the allocation of expenses for each business code must be computed correctly based on acceptable methodology by the MIRB to derive at a net profit for each business code in order to complete the LE 1 Form and reporting the correct tax liability.</p>
B1, B2 and B3 – Notification of Country-by-Country Reporting (CbCR)	Applicable	N/A	A Labuan entity is required to comply with proper notification and declaration of the Country-by-Country Reporting (CbCR).

ii. **Form LE 4 / LE 5- Statutory Declaration Under Sections 5 / 10 of the Labuan Business Activity Tax Act 1990**

4. Keuntungan bersih \* **termasuk / tidak termasuk** pendapatan yang diperoleh daripada royalti dan pendapatan lain yang diperoleh daripada pengeksploitan secara komersial **hak harta intelek**.

4. *The net profits \* include / do not include any income derived from royalty and other income derived from the commercial exploitation of an intellectual property right.*

5. Entiti Labuan tersebut menjalankan suatu aktiviti perniagaan Labuan iaitu **selain aktiviti pemegangan ekuiti tulen** dan telah \* **mematuhi / tidak mematuhi** Peraturan-Peraturan Cukai Aktiviti Perniagaan Labuan (Kebendak Bagi Aktiviti Perniagaan Labuan) 2018 [P.U. (A) 392/2018] sepanjang tahun taksiran seperti berikut:-

5. *The said Labuan entity carries on a Labuan business activity which is other than pure equity holding activity and has \* complied / not complied with the Labuan Business Activity Tax (Requirements For Labuan Business Activity) Regulations 2018 [P.U. (A) 392/2018] throughout the year of assessment as follows:-*

5.1 Bilangan pekerja sepenuh masa tahunan di Labuan: ..... pekerja; dan  
*Number of annual full time employees in Labuan: ..... employees; and*

5.2 Amaun perbelanjaan operasi tahunan di Labuan: RM .....  
*Amount of annual operating expenditure in Labuan: RM .....*

6. Entiti Labuan tersebut menjalankan suatu aktiviti perniagaan Labuan iaitu **aktiviti pemegangan ekuiti tulen** dan telah \* **mematuhi / tidak mematuhi** syarat-syarat berikut:-

6. *The said Labuan entity carries on a Labuan business activity which is a pure equity holding activity and has \* complied / not complied with the following conditions:-*

6.1 Keperluan pengurusan dan kawalan di Labuan \* **dipatuhi / tidak dipatuhi**; dan  
*Has \* complied / not complied with management and control requirements in Labuan; and*

6.2 Amaun perbelanjaan operasi tahunan di Labuan: RM .....  
*Amount of annual operating expenditure in Labuan: RM .....*

DAN \* SAYA / KAMI MEMBUAT AKUAN INI dengan kepercayaan bahawa apa-apa yang tersebut di dalamnya adalah benar, serta menurut peruntukan-peruntukan Akta Akuan Berkanun 1960.  
*AND \* I / WE MAKE THE SOLEMN DECLARATION conscientiously believing the same to be true, and by virtue of the provisions of the Statutory Declarations Act 1960.*

	<b>New Form LE 4 / LE5</b>	<b>Old Form LE 4 / LE 5</b>	<b>Our Comments</b>
Paragraph 4 - To confirm there is no income derived from royalty and other income derived from the commercial exploitation of an intellectual property right	Applicable	N/A	The Labuan entity is required to make a self-declaration in the New Form LE 4 / LE 5 that it has no income derived from royalty and other income derived from the commercial exploitation of intellectual property right.
Paragraph 5 – To confirm the Labuan entity has complied with the substantive requirement	Applicable*	N/A	The Labuan entity is required to make a self-declaration in the New Form LE 4 / LE 5 that it has complied with the substantive requirement for each income stream.  <i>*Applicable to entities operate business other than pure equity holding activity.</i>
Paragraph 6 – To confirm the Labuan entity has complied with the substantive requirement	Applicable*	N/A	The Labuan entity is required to make a self-declaration in the New LE 5 that it has complied with the substantive requirement by each income stream.  <i>*Only stated in Form LE 5 and applicable to entity operate pure equity holding activity.</i>

## Enforcement and Operation

A summary of the new provisions and the corresponding tax implications from the amendments made to LBATAA effective from YA 2020 as below:

No.	Provision under LBATAA	Subject	Our Comments
1.	Subsection 6(2)	Power to raise assessments/additional assessments	<p>IRBM is authorised to conduct routine tax audit periodically as part of the new feature in the Labuan tax system similar to the provisions under Income Tax Act 1967 ("ITA").</p> <p>The purpose of conducting tax audit is to ensure the compliance with the new tax legislation under LBATAA and the substance requirement.</p>
2.	Section 6D	Right of appeal against assessment	Aggrieved towards assessment made by the IRBM, a taxpayer may appeal to the Special Commissioner in the same manner under the ITA.
3.	Section 17C	General anti-avoidance provision	The IRBM may disregard and make adjustments in relation to certain transactions of altering the incidence of tax, relieving, evading or avoiding liability to pay tax. This is an anti-avoidance provision to avoid aggressive tax planning structure of a Labuan entity without any substance.
4.	Section 17D	Adjustment of transfer pricing	<p>This provision is introduced to closely scrutinise transactions with related parties. With this amendment, the IRBM may substitute the price in a related transaction if the transaction was not made at arm's length.</p> <p>Moving forward, the IRBM may issue similar guidelines than those under the ITA including the preparation of transfer pricing documentation in order to justify the arm's length principle in respect of related party transactions.</p>
5.	Sections 22B, 22C and 22D	Power to the DG to access to company's information, premise and record keeping	IRBM can call, access and inspect record, premises and necessary documents to facilitate the conduct of tax audit/investigation.

In consideration of the changes in Labuan tax legislation which has been stated above but not limited to, international network of companies with Labuan entities within the group are advised to look into their tax position in an urgent basis in order to manage any tax implications arising from the above amendments. PKF's team of experienced tax advisory professionals in Malaysia will be pleased to help.

#### How PKF can help you:

1. To provide audit, accounting and tax compliance services as required under the new Labuan tax legislation;
2. To provide advisory services in identifying the correct business code based on each activity of the Labuan entity;
3. To provide tax advisory and tax audit support services due to the new tax legislation in Labuan as Labuan entity may be subject to periodical tax audit;
4. To assist on preparing transfer pricing documentation due to the new tax legislation in Labuan;
5. To assist in applying tax clearance before closure of tax file; and
6. To seek clarification and appeal to IRBM.

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