

# TAX EVASION & TAX AVOIDANCE

**Tax Evasion:** using illegal means to avoid tax

**Tax avoidance:** legally avoid tax.

**IRB's viewpoint:** would like to limit such practices if it were of the opinion that such scheme are not commercially justifiable or merely set up to avoid tax.

**Anti avoidance provision:** Section 140, 140A, 141

# Anti-avoidance

	Purpose	Nature	Example
Specific	Introduced into a tax act for the purpose of countering a particular form of tax avoidance	Usually worded in such a way that leaves no doubt as to what it covers ie mandatory in its application	<ul style="list-style-type: none"> <li>•S32(3)(a) which prevents the benefit of living accommodation provided by an employer from being restricted 30% of S13(1)(a) where the employee is a non service director of a controlled company</li> <li>•S141</li> </ul>
General	Intended to catch all & any unspecified forms of tax avoidance which fall within the ambit of the section	Depend upon the exercise of the DG's discretion	Section 140

# TAX AVOIDANCE – S 140

- **Section 140** provides that where the DG believes that any transaction has the direct or indirect effect of:
  - altering the incidence of tax
  - relieving any person from tax or from having to file a tax return
  - Evading or avoiding tax; or
  - Hindering or preventing the operation of the Act

Once a transaction comes within the scope of S140, the DG may:

- ✓ treat the income of a person from any source as the income of another person
- ✓ revise the tax liability of any person or impose a tax liability on any person
- ✓ Issue an assessment/additional assessment in respect of any person as may be necessary; and
- ✓ Nullify the right of repayment of tax or require the return of any tax that had been paid

Eg 50.3, 50.4 , 50.5 pg 532

# TAX AVOIDANCE – S 140

- Recent tax avoidance case: Yeoh Eng Hock Holdings (pg 540)
- Principles to observe : Refer Pg 544

Eg 50.3, 50.4 , 50.5 pg 532

# TAX AVOIDANCE – S 141

- **S141** extends the power of DG to make adjustments in respect of dealings between a resident and the non-resident on the basis of close connections between these two persons.
- It is directed at transactions which are arranged to ensure that profits are not taxed in Malaysia.
- DG has the power to tax the profits which the resident has not in fact made but which he might reasonably be expected to have made had he done the business on ordinary commercial terms.

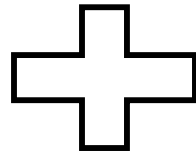
# TAX AVOIDANCE – S140A

- **S140A** was enacted ( incorporating TP & thin capitalization provision) to empower the DG to make the relevant tax adjustments on transactions of goods, services, and financial assistance carried out between associated persons based on the arm's length principle.
  - DG may substitute the price on certain transactions where the DG is of the opinion that such price does not reflect the arm's length price.
  - As for thin capitalization, the portion of the interest or other financial charges that relate to the amount of financial assistance which is deemed excessive will not be granted a tax deduction.

# New definition of Control

Meaning of control  
(Wef 1.1.2019)

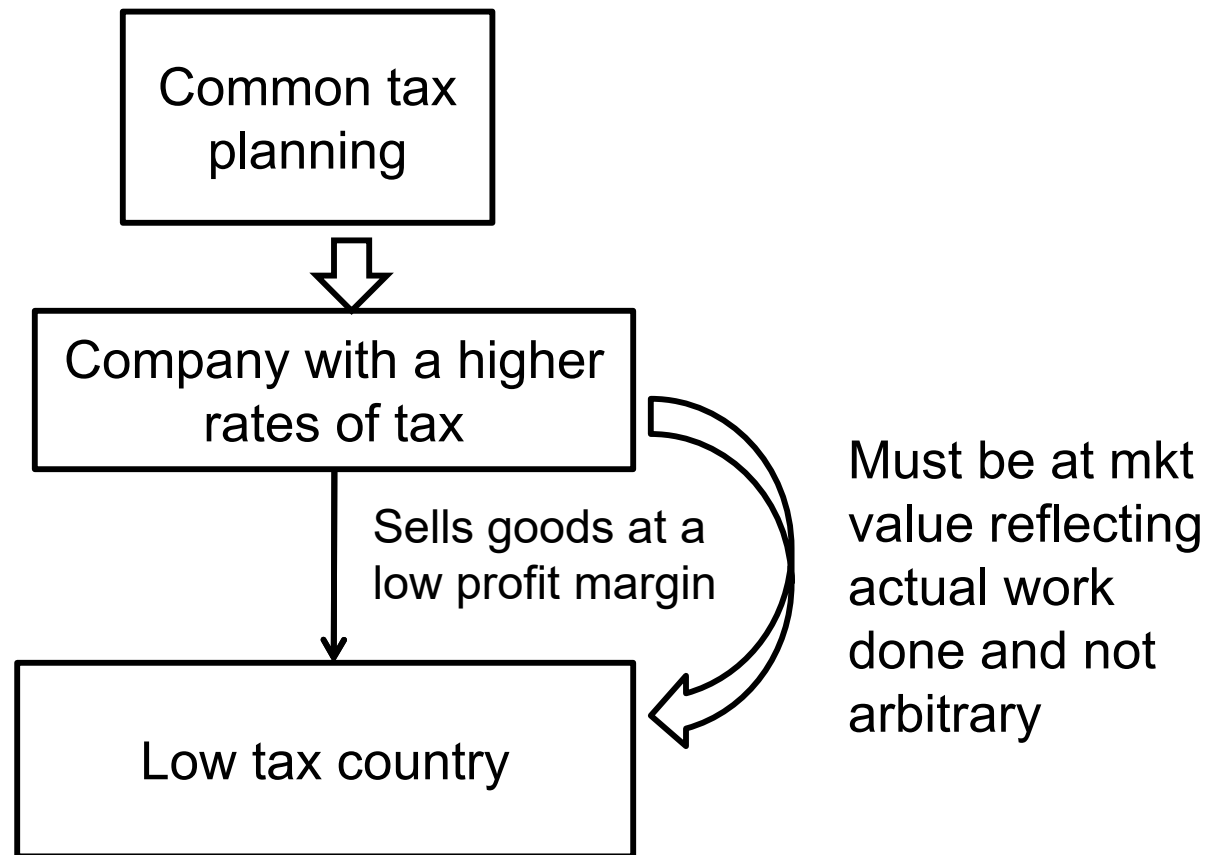
>20%



1. Proprietary rights
2. Business activities/price influence
3. Appointment of board of directors

Diagram – Pg 457

# Transfer Pricing



Transfer pricing rules to ensure all multinational companies (with HC in overseas and branch/ subsi in M'sia) pay their fair share of tax based on prevailing mkt value of goods



# Introduction

- ❑ TP risks arises when companies/individuals are engaged in controlled transactions (transactions between associated persons).
- ❑ The meaning of “associated persons”:

## Section 139(7)

One of whom  
has control  
over the other

Individuals who  
are relatives of  
each other

Persons, both of  
whom are  
controlled by  
some other  
person

## Section 2(4)

### ***Related companies***

Related within  
two or more  
companies in  
the same group  
or holding *more  
than 50% of  
shares* in each  
of two or more  
companies.

## Section 138

the meaning of  
“control” and  
makes  
reference to  
*direct or indirect  
control*

## Malaysian TP Guidelines

One company  
participates  
directly or  
indirectly in the  
management,  
control or  
capital of the  
other or both  
companies.

# Introduction

❑ The above are regulated/guided by the following:

- **Arm's length provision Section 140A;**
- **TP Rules (May 2012);**
- **TP Guidelines (July 2012);**
- **TP Audit Framework; and**
- **MNE Form.**

# Malaysian TP Guidelines

**Released on 20 July  
2012(updated July  
2017)**

**New tax penalty  
regime**

**Preference of local  
comparable  
companies**

**Detailed  
contemporaneous  
documentations  
taxpayers should  
maintained,  
especially in  
relation to intra-  
group services**

**TP documentation  
should be made  
available to the IRB  
within 30 days of a  
request being made  
( NOTE)**

**Taxpayers outside  
the thresholds  
specified can opt to  
prepare a “short-  
form” TP  
documentation**

## **Threshold for preparing a full scope TP documentation:**

- ✓ Gross income > RM 25 million & the total amount of RPTs > RM 15 million;
- ✓ Provides financial assistance > RM 50 million.

## **Failure to Furnish Contemporaneous TP Documentation(NOTE)**

- On conviction, liable to a fine of  $\geq \text{RM}20,000$  and not  $\leq \text{RM}100,000$ ; or  
Imprisonment for a term not  $> 6$  months  
or to both
- No prosecution, liable to a fine of  $\geq \text{RM}20,000$  and not  $\leq \text{RM}100,000$

**Effective date: 1.1.2021**

# Surcharge on TP Adjustment

- Penalty rate under Section 113(2)

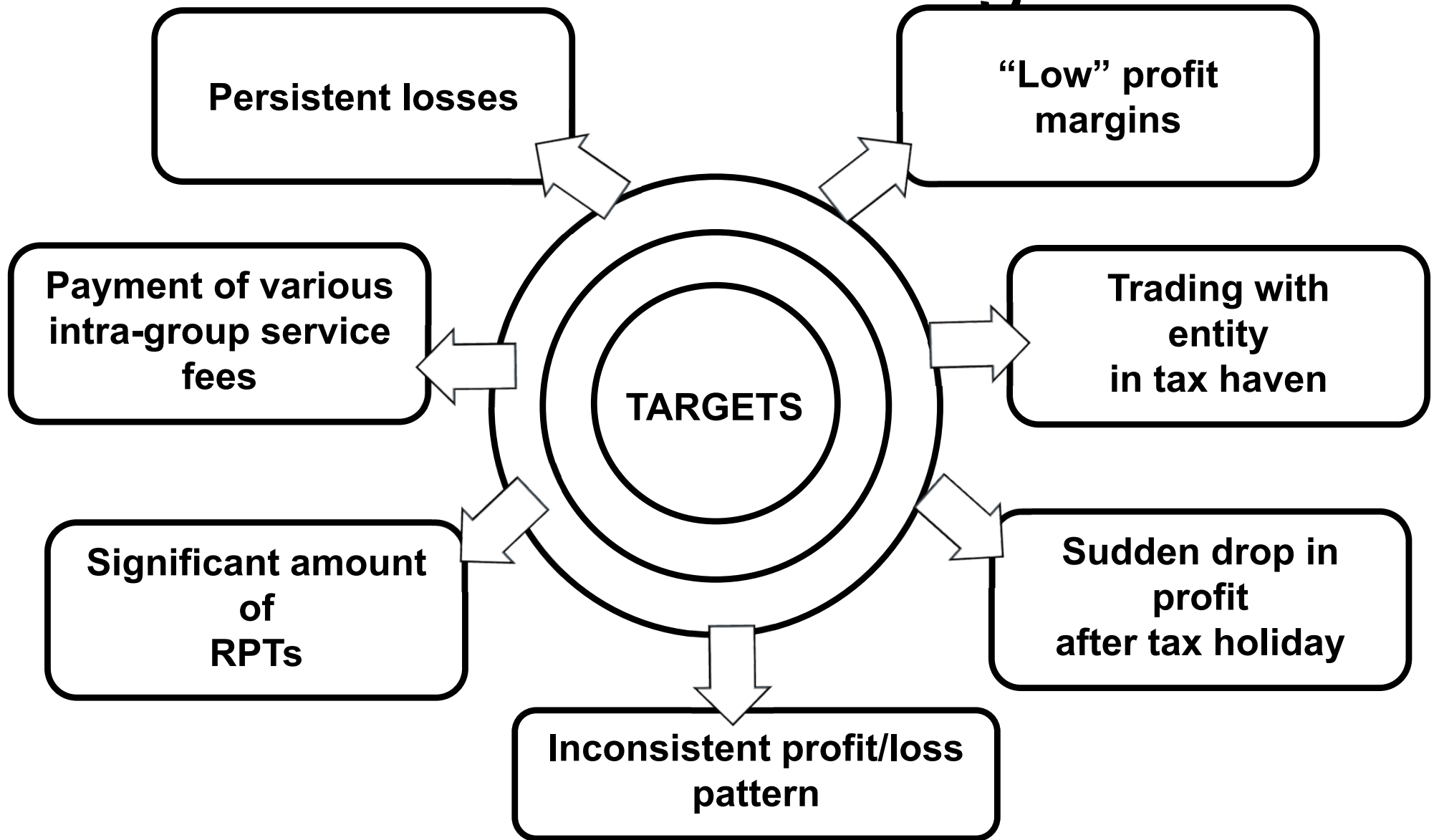
NO	Condition	Penalty rate Audit case	( TP issues) Voluntary Disclosure
1	TP( who is required to prepare TP documentation in accordance with the TP Guidelines 2012) did not prepare TP documentation	50%	N/A
2	TP prepared TP documentation and submitted documentation ( together with voluntary disclosure) but did not fully comply with the requirements under the TP Guidelines 2012; or TP prepared a comprehensive and quality TP documentation but failed to submit it within 30 days from the date of the written request issued by the IRB	30%	20%

# Surcharge on TP Adjustment

- Penalty rate under Section 113(2)

NO	Condition	Penalty rate Audit case	( TP issues) Voluntary Disclosure
3	TP prepared a comprehensive and quality TP documentation in accordance with TP Guidelines 2012 and submitted it within 30 days from the date of the written request issued by the IRB ( for voluntary disclosure cases, it is submitted when the voluntary disclosure is made)	0%	0%
	Effective 1 January 2021, a surcharge of <b>up to 5%</b> could also be imposed on <b>transfer pricing adjustment</b> made even if it does not result in any additional tax payable.		

# TP audit red flags



## **Interest on financial assistance granted in a controlled transaction (Earning Stripping Rules)**

- ❑ For interest expenses exceeding RM500,000
- ❑ Applicable to transactions with:
  - (i) an associated person outside Malaysia
  - (ii) an associated person outside Malaysia which operates through a permanent establishment in Malaysia
  - (iii) a 3rd party outside Malaysia where the financial assistance is guaranteed by holding company or group of companies
- ❑ Not applicable to licensed banks, investment banks, etc.



# Interest on financial assistance granted in a controlled transaction (Earning Stripping Rules)

$$\text{Tax EBITDA} = [A] + [B] + [C]$$

	Include	Exclude
Interest expenses	<ul style="list-style-type: none"><li>• interest in all forms of debt</li><li>• payments economically equivalent to interest.</li></ul>	(a) any interest expenses incurred in connection with the raising of finance (e.g. guarantee fee); or (b) any interest expenses incurred which is not allowable in ascertaining the adjusted income under the Act before any restriction on the deductibility of interest is made under section 140C of the Act of a person from the business source.

**Max interest expense allowable = 20% x Tax EBITDA**

**Excess c/f to be utilized in the subsequent year and st max amount rule**

## Interest on financial assistance granted in a controlled transaction (Earning Stripping Rules)

A	Adjusted income of business ( before interest expense)
B	Qualifying deductions allowed by PU(A) Orders relating to: (a) Special deduction; (b) Double deduction
C	Interest expense paid to overseas related companies
	Example 37.8(pg 431)

## **Interest on financial assistance granted in a controlled transaction (Earning Stripping Rules)**

**Max interest expense = 20% x Tax EBITDA allowable**

**Excess c/f to be utilized in the subsequent year and subject to:**

- Max amount of interest ascertained in the above**
- Shareholders of the first day and last day of the basis period for the YA following the year in which such amount was ascertained is substantially the same**