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Scope of withholding tax			
❖ <b>Withholding tax is restricted to the following types of payments made to non-residents.</b>			
Type of income	Withholding tax section	Rate %	Form
❖ Interest	109	15	37
❖ Royalty	109	10	37
❖ Contract payments	107A	10+3	37A
❖ Public entertainers (individual)	109A 109B	15	
❖ Special classes of income	109F	10	37D
❖ Gains or profits derived from Malaysia		10	37F

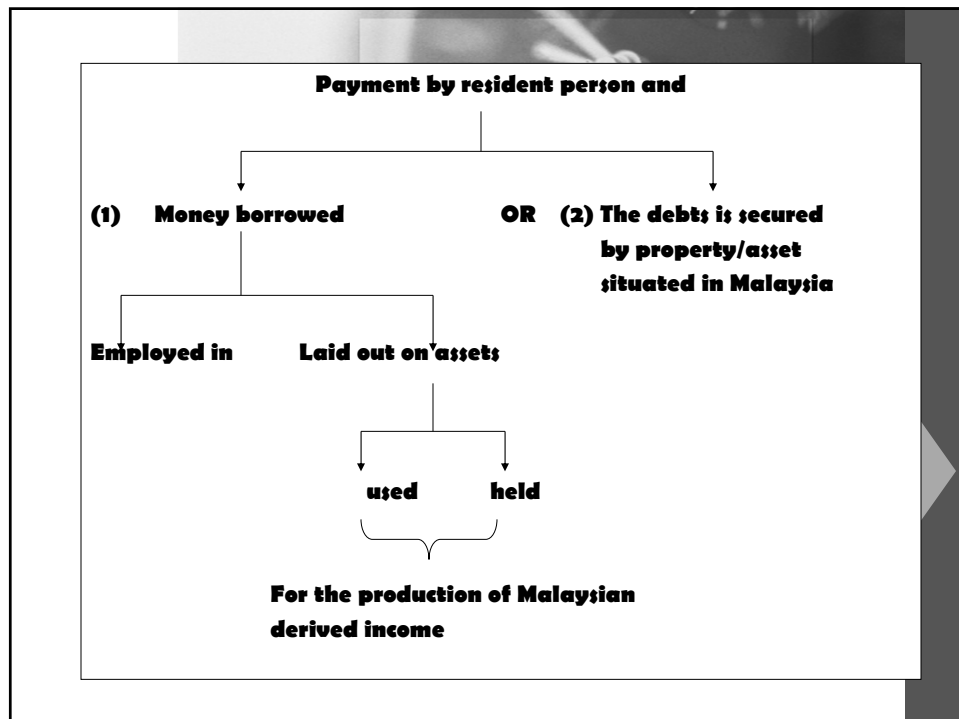
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## Derivation of interest income (S 15)

Interest shall be deemed to be derived from Malaysia:

- 1) If responsibility for payment of interest lies with the Government, a state Government or a local authority; or
- 2) If the interest is charged as an expense against any income accruing in or derived from Malaysia

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## PYQ

### March/June 2021 Q4(b)

Magic Pte Ltd (MPL), a company incorporated and tax resident in Singapore, has branches in Malaysia and Indonesia. MPL's branches pay royalties to its parent company, Magic Holdings Inc (MH), a US incorporated company.

#### Royalties

For the financial year ended 31 May 2021, the royalty payable was RM300,000 for the Malaysian branch and RM200,000 for the Indonesian branch. The Malaysian branch has made the full payment of RM500,000 for both branches.

#### Warehouse construction

MPL's Malaysian branch has engaged the services of a UK contractor to construct a new warehouse in Selangor, Malaysia for RM20 million, consisting of the following:

	RM'000
Construction materials	8,300
Design services for drawings done in the UK	1,700
Construction services (including piling works) in Malaysia	10,000

The piling works are subcontracted by the UK contractor to a local resident contractor in Malaysia for RM2 million. The UK contractor has requested MPL's Malaysian branch to pay the RM2 million directly to the local resident contractor.

**(b) Explain whether withholding tax should be deducted from the royalty and construction payments made by Magic Pte Ltd's Malaysian branch, and state the applicable rates.**

(7 marks)

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## PYQ

#### Royalty

As MPL's Malaysian branch is making royalty payments to its US parent company, it is required to deduct withholding tax at the prevailing rate of 10% (s.109 ITA 1967).

However, the amount subject to withholding tax is only the royalty deemed to be derived from Malaysia. A royalty is deemed to be derived from Malaysia if the responsibility for the royalty payment is with a resident or the amount is charged against any income derived from Malaysia (s.15 ITA 1967).

As MPL is not tax resident in Malaysia, the royalty is deemed to be derived from Malaysia if the amount payable is charged against any income accruing in or derived from Malaysia. Therefore, only the RM300,000 would attract withholding tax.

In respect of the royalty for the Indonesian sales, the amount cannot be deducted from or charged against the Malaysian trading income (as the amount is not wholly and exclusively incurred in the production of the Malaysian income). Therefore, the RM200,000 is not subject to withholding tax.

#### Construction of new warehouse building

The construction services paid to a non-resident could fall under special classes of income (s.4A/109B ITA 1967) or contract payments (s.107A ITA 1967).

If the payment to a non-resident is in respect of services in relation to a contract in Malaysia, which results in a place of business for the non-resident in Malaysia, then the withholding tax provision under contract payments (s.107A ITA 1967) is applicable.

Under the tax legislation, a construction, assembly and installation site constitutes a place of business. Therefore, the contract sum made to the UK contractor should be regarded as a contract payment. The applicable withholding tax rates (s.107A ITA 1967) are:

- 10% of the Malaysian service portion, on the account of the non-resident contractor; and
- 3% of the Malaysian service portion, on the account of the employees of the non-resident contractor.

#### Amount subject to withholding tax

	RM'000
Construction materials	0
Design services rendered outside Malaysia	0
Construction services, including piling works (note)	10,000
	<u>10,000</u>
13% withholding tax	<u>1,300</u>

**Note:** The contract sum for the piling works is due to the UK contractor. The UK contractor merely instructs MPL's Malaysian branch to make the payment to the local resident subcontractor. Therefore, as the amount is still due to the UK contractor, the amount should attract withholding tax.

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## PYQ DEc22 Q4

- Gading Sdn Bhd (GSB) operates a five-star hotel in Penang, Malaysia, and is a service tax registrant.
- The company decided to refurbish the hotel and has temporarily closed it. As there are some long-stay guests, the company has decided to put these guests in another hotel in Malaysia, which is also a service tax registrant. GSB charges the guests and the other hotel charges GSB for this accommodation.
- For the refurbishment project, GSB has appointed Nice Design Pte Ltd, a Singapore resident company, to carry out the design work for RM2 million. Their services are rendered over a four-week period, with two weeks of the work being performed in Malaysia.
- The refurbishment project itself will be undertaken by a US-based contractor, Strong Renovators (SR), for RM20 million. The refurbishment period will last for nine months, and it has been determined that RM8 million relates to the supply of materials.
- GSB will pay management services fees of RM200,000 to its Indonesian holding company, PT Gading Resorts, to oversee the refurbishment project. Their services are wholly performed in Indonesia.

**(a)(iii) Explain the withholding tax implications in respect of the various amounts payable by GSB to its non-resident service providers. Compute the applicable withholding tax, where relevant. Where the payments are also subject to service tax, explain how this would impact the incidence of withholding tax.**

(6 marks)

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## PYQ DEc22 Q4

### (iii) Withholding tax implications for payments made to non-resident service providers

#### Design service fees payable to NDPL

Service fees to the extent where the services are performed in Malaysia are subject to withholding tax of 10%. As two out of four weeks of the services (i.e. 50% of the RM2 million services) are being performed in Malaysia, the proportion of the fees relating to the Malaysian services (i.e. RM1 million) should be subject to withholding tax.

As the design fees also attract service tax, the question then is whether the amount subject to withholding tax should be inclusive of service tax. Withholding tax is effectively the tax of the non-resident and therefore, in calculating the withholding tax amount, it should be based on the income of the non-resident. As the applicable service tax does not form income of the non-resident, it should not be included in computing the withholding tax amount. The withholding tax exposure would therefore be RM100,000 (10% x 50% x RM2 million).

#### Refurbishment service fees payable to Strong Renovators

The refurbishment services for a period of nine months would result in Strong Renovators having a place of business in Malaysia. Therefore, the refurbishment service fees should be regarded as contract payment for withholding tax purposes. The applicable withholding tax rate would be 13%, calculated based on the Malaysian service portion of the contract. Therefore, the applicable contract sum subject to withholding tax would be RM12 million, after excluding the supply of materials (RM20 million – RM8 million). The applicable withholding tax amount is RM1,560,000.

#### Management service fees payable to PT Gading Resorts

As the management services are wholly performed outside Malaysia, withholding tax is not applicable.

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### Consequences of not deducting & remitting tax

- ❖ Penalties – 10% of the withholding tax amount which he fails to pay
- ❖ Allowed as a deduction only upon payment of WHT + penalty (\*) (NOTE)
- ❖ Amounts paid to non-residents for services rendered in connection with the installation /operation of plant & machinery where the withholding tax provisions have not been complied with will be excluded as QCE until payment of WHT + penalty are remitted
- ❖ Amount to be deducted and the relevant penalty - a debt due to the Government

(\*) not applicable to a person where the income from all of his/her sources is fully exempt under PIA1986/Para 127(3)(b)/(3A) of ITA1967 (Eg 24 to 27 PR 10/2019)

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### Consequences of not deducting & remitting tax

#### **Note:**

- ❖ Where the withholding tax is *not due for payment and no payment or crediting is made to the non-resident payee on or before the due date of submission of the ITRF*, regardless of the withholding tax has been paid or remitted to the DGIR, a deduction is *not allowable* under paragraph 39(1)(j) of the ITA
- ❖ may file an application for relief if the payer alleges that the assessment relating to that year of assessment is excessive e.g. where a deduction is not allowed in respect of payment not due to be paid under subsection 109B on the day the return is furnished. The payer may make an application in writing to the DGIR within one year after the end of the year the payment is made.

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## DTA-PE

**Means a fixed place of business through which the business of an enterprise is wholly or partly carried on**

**Generally exist where :**

- a continuity of activity in Malaysia; and /or
- active conduct of business in Malaysia

**PE generally includes the following :**

- ❖ place of management;
- ❖ branch;
- ❖ office;( March/June 2021 Q4)
- ❖ factory;
- ❖ workshop;
- ❖ mine, quarry, oil well, gas well or other place of extraction of natural resources;
- ❖ farm, plantation or other agricultural, pastoral or forestry property;
- ❖ building site or a construction, installation or assembly project which exists for > 6 months

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## DTA-PE

**Excludes:**

- ❖ facilities used solely for storage, display or delivery of goods;
- ❖ purchasing office;
- ❖ representative office
- ❖ commission/independent agent

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## BUSINESS PRESENCE

### Trading in" and not "Trading with" Malaysia

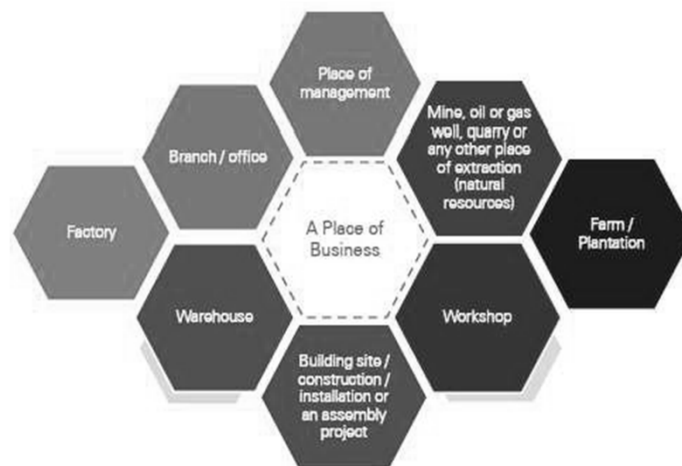
#### "Trading in"(Dependent agent)

- ❖ An active effort to solicit for orders - > final conclusion of contracts in Malaysia
- ❖ Maintenance of inventory in Malaysia and regular filling of orders for customers and delivery by its agent with the right to accept order in Malaysia
- ❖ Maintenance of inventory in Malaysia for further processing or development
- ❖ Performance of services in a contract by its personnel stationed in Malaysia

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## Business Income - Derivation

Attributable to a **place of business** in Malaysia( wef 27.12.2018)



Sarah/2010

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## Business Income - Derivation

**A person shall also be deemed to have a place of business in Malaysia if that person—**

**(i) carries on supervisory activities in connection with a building or work site, or a construction, an installation or an assembly project; or**

**(ii) has another person acting on his behalf who—**

*(a) habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification;*

*(b) habitually maintains a stock of goods or merchandise in that place of business from which such person delivers goods or merchandise; or*

*(c) regularly fills orders on his behalf.*

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## PYQ DEc22 Q4

- Amazing Inc (Amazing) is a US-based global laptop supplier operating under its house brand 'Amazing Computers' manufactured in Europe.
- As Amazing expands into the Asia Pacific region, it will not have its own manufacturing facility or any office in Malaysia. Instead, it will appoint a third-party contract manufacturer, Riba Sdn Bhd (RSB) based in Malaysia, to procure the components, assemble, and sell the finished laptops to Amazing.
- The finished products will be stored in a bonded warehouse operated by an independent logistics provider in Malaysia. As and when there are orders, the laptops would be shipped and delivered to the relevant third-party distributors in the Asia Pacific region, including Malaysia.
- A five-man sales team, housed under the payroll of RSB but acting on Amazing's behalf, will negotiate and conclude contracts with the third-party distributors in the region. For its role of housing the sales personnel for Amazing, RSB will charge an arm's length marketing service fee to Amazing.

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## Business Income - Derivation

Dec 22 Q2(b)

### (b) Amazing Inc (Amazing)

#### (i) What constitutes a 'place of business' in Malaysia

Under the tax legislation, a person is deemed to derive income from a business in Malaysia if that income can be associated with the existence of a place of business in Malaysia.

A place of business is defined to include a place of management, branch, office, warehouse, etc. In addition, a person is deemed to have a place of business in Malaysia if the person carries on supervisory activities in connection with a building or work site, or a construction, an installation or an assembly project.

Additionally, a place of business can exist if the person has another person acting on their behalf who habitually concludes contracts, or plays the principal role leading to the conclusion of contracts which are routinely concluded without material modification; habitually maintains stock of goods in that place of business of the person from which such person delivers goods; or regularly fills orders on behalf of the person.

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#### (ii) Place of business analysis – Amazing

In determining whether Amazing has a place of business in Malaysia, the fact pattern of the activities undertaken by Amazing in Malaysia would need to be analysed:

Contract manufacturing activities – the appointment of a contract manufacturer in Malaysia, i.e. Ribe Sdn Bhd (RSB), in itself should not result in it having a place of business in Malaysia.

Use of warehouse to store finished laptops – Amazing will appoint an independent logistics provider to store the finished laptops in Malaysia. While a warehouse can be said to trigger a place of business, the use of a warehouse operated by an independent logistics provider where such a warehouse is not at the disposal of Amazing should not by itself constitute a place of business for Amazing.

Presence of a marketing and sales team in Malaysia – Amazing has five sales personnel based in Malaysia, housed under the payroll of RSB. The sales team is acting on behalf of Amazing to negotiate and conclude contracts with its distributors. This would result in Amazing having a place of business in Malaysia. This is notwithstanding that RSB is charging arm's length marketing fees for the provision of the sales personnel.

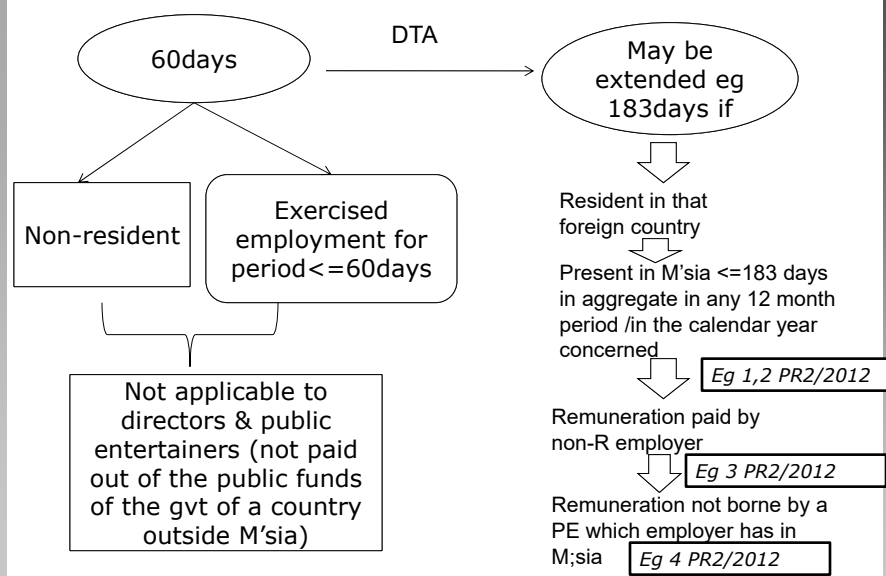
Maintenance of goods for delivery to distributors/sales team in Malaysia – based on the guidelines issued by the Inland Revenue Board (IRB), the foreign principal will be deemed to have a place of business if the agent also conducts sales related activities in addition to regularly delivering or regularly filling orders out of the stocks of goods belonging to the principal.

As Amazing maintains stocks in Malaysia with RSB providing the marketing and selling activities, this would likely trigger Amazing having a place of business in Malaysia.

While some of the activities undertaken by Amazing or through RSB or an independent logistics provider may not individually constitute a place of business, the sum total of all the activities of Amazing in Malaysia (i.e. the presence of sales personnel negotiating and concluding contracts on behalf of Amazing, the maintenance of stocks in Malaysia for delivery coupled with sales related activities) constitutes complementary functions which are part of a cohesive business operation. Consequently, on balance, Amazing is likely to be regarded as having a place of business in Malaysia.

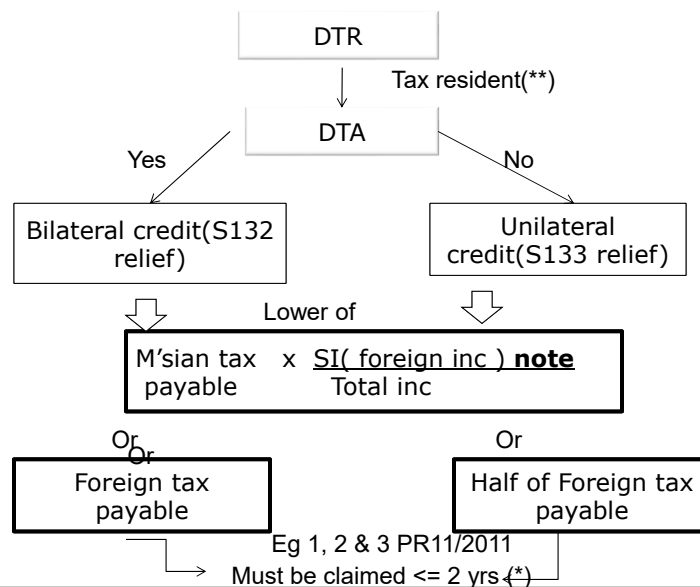
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## Exemption of employment income



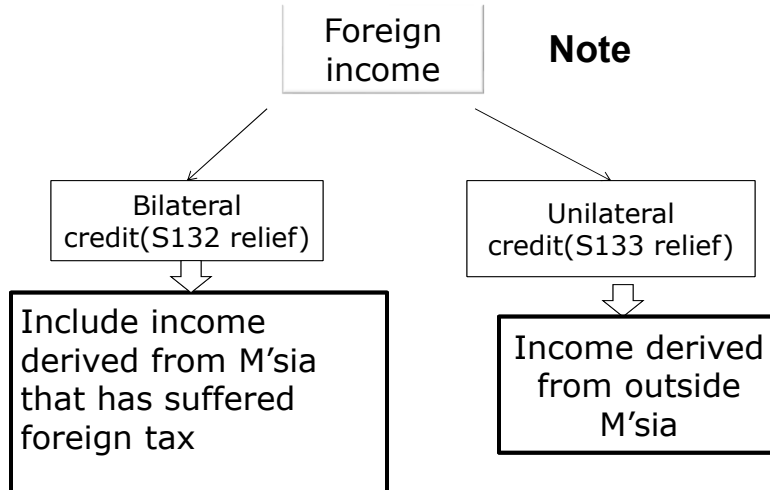
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## Double Taxation Relief(DTR)



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## Double Taxation Relief(DTR)



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## Bilateral Relief

**March/June 2021 Q4**

- ❖ (c) Explain whether Nasib Baik Sdn Bhd is eligible for double tax relief in relation to the Philippines withholding tax suffered, and, assuming it is eligible, compute the relief available.

Nasib Baik Sdn Bhd (NBSB), a company with a paid-up ordinary share capital of RM3 million, is in the business of providing cyber security analytical services to its clients.

For the financial year ended 31 March 2021, NBSB was contracted by a client in the Philippines to provide these services. Most of the analytical services were performed from its office in Kuala Lumpur, Malaysia. In addition, two consultants travelled to the Philippines to validate and explain the findings. This trip lasted three days.

The service fee of RM200,000 receivable by NBSB was subject to withholding tax of RM20,000 in the Philippines.

NBSB's gross revenue for the year was RM3,000,000 and its statutory/aggregate/total income was RM250,000.

The Philippines have signed a double tax treaty with Malaysia.

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## Bilateral Relief

### (c) Nasib Baik Sdn Bhd (NBSB)

In respect of the Philippines contract, as the performance of the services was mainly carried out from its office in Kuala Lumpur, Malaysia, the income was derived from Malaysia, and should therefore be subject to Malaysian Income tax.

However, it was also subject to withholding tax in the Philippines. As the Philippines have concluded double tax treaties with Malaysia, it is possible to claim bilateral tax relief in relation to the foreign tax suffered. For the purpose of bilateral relief, foreign income includes income derived from Malaysia charged to foreign tax.

The bilateral relief is calculated based on the lower of the Malaysian tax attributable to the foreign income or the foreign tax suffered.

#### Computation of bilateral relief

Aggregate/total income	RM250,000
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Income tax at 24%	RM60,000
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Less: Bilateral relief

Attributable Malaysian tax on the Philippines contract

= Gross income from Philippines/total gross income x statutory income

=  $200,000/3,000,000 \times 250,000$  = SI of foreign source

= 16,667 x 24%

= RM4,000

Foreign tax suffered = RM20,000

Whichever is lower, i.e. RM4,000

$16,667/25000 \times 60000$   
= 4000