



KASTAM DIRAJA MALAYSIA

CUKAI BARANG DAN PERKHIDMATAN

**GUIDE
ON
INVESTMENT BANKING**

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INTRODUCTION

1. This Industry Guide is prepared to assist you in understanding the Goods and Services Tax and its implications on banking services offered by Investment Banks (IBs).

General Operation Of Goods And Services Tax (GST)

2. The GST which is also known as Value Added Tax in other countries is a tax on final consumption of goods and services. Unlike the present sales tax system which is a single stage tax, the GST is a multi stage tax. Payment of tax is made in stages by the intermediaries in the production and distribution process. Although the tax will be paid throughout the production and distribution chain, it is ultimately passed to the final consumer. Therefore, the tax itself is not a cost to the intermediaries and does not appear as an expense item in their financial statements.

3. A person who is registered under the GST is required to charge GST on his output of taxable supply of goods or services made to his customers. He is allowed to claim as credit on any GST incurred on his purchases which are inputs to his business. His customer, if he is also in a business of making taxable supply of goods or services, in turn is allowed to claim a credit on GST paid on his input. Thus, double taxation will be avoided and only the value added at each stage is taxed.

OVERVIEW – GENERAL OPERATIONS OF THE INDUSTRY

4. In Malaysia, investment bank is responsible as a financial intermediary that performs a variety of services, primarily in raising capital and security underwriting, mergers and acquisitions, and sales and trading for both institutions and private investors. Investment bank earns profit by charging fees and commissions for providing these services and other kinds of financial and business advice. As a result, most of the services supplied are standard rated.

GST TREATMENT ON INVESTMENT BANKS (IB)

GST Treatment by Supply Types

5. IBs normally make three types of supplies namely, exempt supply, standard rated supply and zero rated supply.

(a) **Exempt supply**

A supply is exempt if the consideration of the supply is generally in the form of an interest or a spread. In normal practices, services rendered by IBs such as accepting deposits from wholesale customers, trading of money market instruments, and equity and debt capital market instruments are treated as exempt supply.

(b) **Standard Rated Supply**

Although most of the financial services are treated as exempt supplies, fee based services such as arranging, broking, underwriting, advising or any other similar activities pertaining to the provision of the financial services are treated as standard rated supplies.

(c) **Zero Rated Supply**

Services performed by IBs for customer outside Malaysia will be zero-rated if at the time when the services are performed, he is outside Malaysia. This is an export of services. Some examples of exported financial services are:

- (i) Any financial service in connection with land and goods situated outside Malaysia
- (ii) Any financial service provided to a foreigner (non-resident) and he is not in Malaysia when the services are performed, and
- (iii) Any financial service provided to a foreigner (non-resident) and he is not trading Malaysian securities.

GST TREATMENT ON INVESTMENT BANK

Corporate Finance

6. Functions of corporate finance include:

- (a) Takeover, merger, acquisitions and divestiture advisory

IBs provide advisory services on strategising, planning and takeovers, mergers, acquisitions, management buyouts and divestments; assist public and private companies in raising fund in the capital market; and act as intermediaries in underwriting stock and bond issues. The fees charged for such services are treated as a standard rated supply.

(b) Underwriting and other services

(i) IBs are also financial intermediaries in securities offerings. They verify financial data and business claims, facilitate pricing, and perform due diligence. Most underwritings are “firm commitment” underwritings in which investment banks purchase the securities from the issuer and distribute them to the public. Such services are standard rated supplies.

(ii) Besides the underwriting services, IBs offer other services which are subject to GST at a standard rate. Examples of these services are:

- Advising and preparing companies for flotation on the stock exchanges.
- Identifying potential merger partners and take-over targets for clients and advising on mergers and acquisitions and take-over transactions.
- Devising and executing strategies for capital raising activities through placement of securities, secondary issues of securities, special issues, convertible loans and other capital market instruments.
- Providing advice from corporate restructuring exercises to restructure a company’s gearing or business operations.
- Offering independent evaluation of corporate transactions and valuation of companies/business/securities and assets.

Debt capital markets

7. IBs are also providing their corporate clients with the expertise in structuring debt financing programs via debt securities instruments, whether conventional or Islamic.
8. Some examples of services listed below are subject to GST at a standard rate:
- (a) Advising and arranging for the issuance of debt securities.
 - (b) Underwriting the issuance of debt securities.
 - (c) Subscribing the issuance of debt securities.
 - (d) Placement of debt securities.
 - (e) Agency role throughout the tenure of the debt securities.

Equity Markets/Stock broking

9. IBs assist companies in accessing the equity capital market for their financing requirements. Services offered which are subject to GST at a standard rate include:
- (a) Arranging, structuring and underwriting of an equity issuance.
 - (b) Placement of shares.
 - (c) Trading of shares.
 - (d) Advising on investment activities.
 - (e) Custody and nominee services.

Derivatives and Structured Products

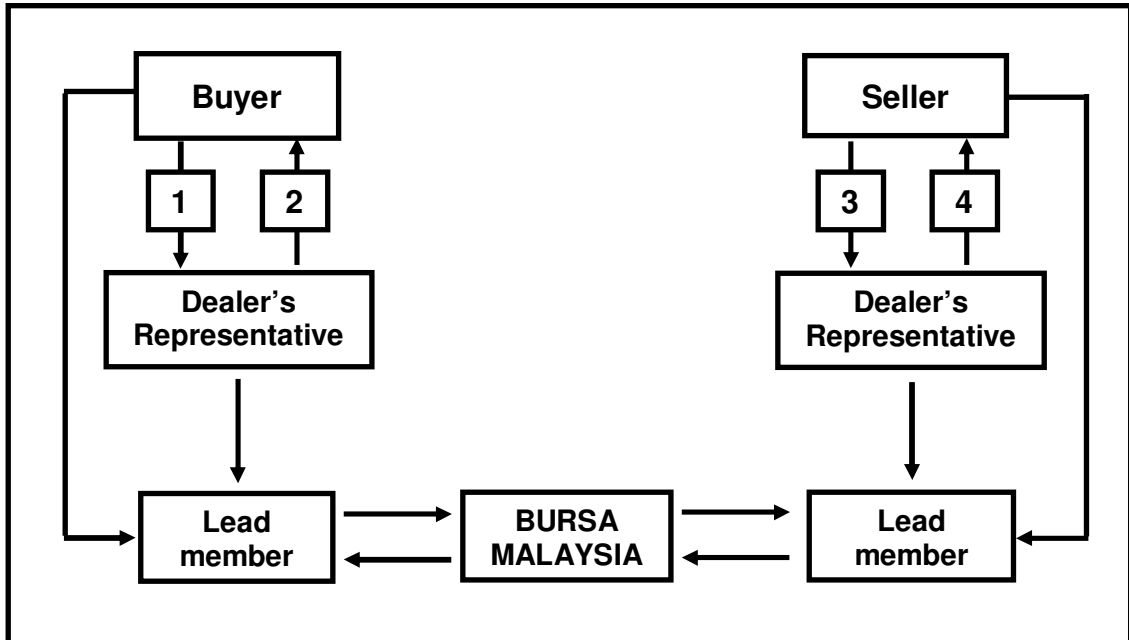
10. Services offered to cater for derivatives and structured products which are subject to GST at a standard rate are:
- (a) Advising, originating and issuing of products/structures.
 - (b) Designing products/structures with modified risk-return profiles

Treasury

11. The following services offered by IBs are exempted from GST:
- (a) Accepting deposits from wholesale customers (RM500,000 and above).

- (b) Trading of money market instruments.
- (c) Trading of debt capital market instruments.

Figure 1: The process of Dealing and Trading of shares



Description:

1. Buyer instructs dealer's representative to buy shares – exempt supply
2. Dealer's representative charges commission for buying the shares - standard rate supply
3. Seller instructs dealer's representative to sell shares – exempt supply
4. Dealer's representative charges commission for selling the shares - standard rate supply

Dealer or Futures Broker

12. If a dealer (a stock broking company) or futures broker supplies a dealing system which allows a user to insert bid and offer quotes for securities or commodities and charge the services supplied, the supply is subject to GST at a standard rate.

13. Some dealers, futures brokers or related third parties may supply electronic data services which provide subscribers with a message facility for an information

service i.e. on share price movements or financial news supplies. The supply of electronic data/information services are taxable supplies and subject to GST at a standard rate. Besides that, a dealer or futures broker may provide investment and portfolio management services, personal equity plan management services, advisory, research and valuation services and custodial services. These services are subject to GST at a standard rate.

Dealer's Representatives or Futures Broker's Representatives

14. All dealer's representatives are attached to some dealer while futures broker's representatives are attached to the futures broker before they are allowed to trade in Bursa Malaysia. For GST purposes, the dealer representatives and the dealer or futures broker representatives and the futures broker are treated as a single entity. This means that the dealer or futures broker must account GST on the brokerage commission earned by the dealer representatives or futures broker representatives even though the brokerage commission received by each dealer representative or futures broker representative is below threshold. The dealer or futures broker is required to charge and account for GST made on taxable supplies by him, dealer's representatives or futures broker's representatives and issue a tax invoice for the taxable supply.

15. On the input side, the dealer or futures broker is entitled to claim input tax on acquisition of goods and services used for making taxable supplies. This means that the dealer or futures broker can claim GST incurred on his expenses such as office rental, computer hardware and software, dealing system rental, electricity and telecommunication services.

16. Besides that, the dealer representatives or futures broker representatives may incur GST on their expenses such as telecommunication services. The dealer representatives or futures broker representatives are required to pay the GST incurred and pass on the tax invoices issued under their name to the dealer or futures broker to claim the GST incurred as input tax credit on their behalf. Having claimed the input tax credit, the dealer or future broker will then reimburse the amount of GST paid by the dealer representatives or futures broker representatives. The reimbursement is not subject to GST.

17. For intra supplies between the dealer and dealer representatives or futures broker and futures broker representatives such as dealing system rental and office rental, these supplies are disregarded for GST purposes. This means that the dealer or future broker is not required to charge GST on such supplies made to the dealer representatives or futures broker representatives.

Fixed Input Tax Recovery (FITR)

18. Generally, a mixed supplier may claim input tax in the following manner:-

- (a) Claim full input tax credit if the input is wholly attributable to a taxable supply;
- (b) Cannot claim input tax credit if the input is wholly attributable to an exempt supply; or
- (c) Apportion input tax by using the turnover method if the input (residual input) cannot be wholly attributable to either taxable or exempt supplies.

19. Supplies made by financial institutions e.g. the provision of loans or financing is an exempt supply and input tax is not claimable. However, banks and other financial institutions which provide loans or financing to businesses are allowed to claim the GST incurred on their business input. Such claim is only applicable by using Fixed Input Tax Recovery (FITR) method.

20. FITR is a method where a financial institution such as:

- (a) commercial bank;
- (b) investment bank;
- (c) Islamic bank;
- (d) development financial institutions and any other approved institution established under any Act of Parliament or State Ordinance is entitled to recover input tax based on a specific rate in percentage determined by the Minister.

21. If a financial institution is allowed to recover input tax using the FITR method, the amount of the input tax allowable is in accordance with the following formula:

$$A \times B$$

where: A is the total input tax incurred in the taxable period

and B is the fixed rate.

22. The total input tax incurred in the taxable period includes:
- (a) input tax in relation to exempt supplies i.e. loans provided to businesses and individuals;
 - (b) input tax in relation to standard rated and zero rated supplies;
 - (c) input tax in relation to other exempt supplies e.g. investment activities.
23. For Islamic banks and other financial institutions making financial supplies in accordance with the principles of Syariah, the input tax incurred on supplies relating to Syariah financing is fully claimable.

Example 1:

In January 2016, a GST registered investment bank incurs GST on the following:

- (a) *input tax in relation to exempt supplies (provision of loans to businesses) - RM36,000*
- (b) *input tax in relation to standard rated supplies(fee based services) - RM18,000*
- (c) *input tax on investment activities - RM12,000*

The bank is allowed to use the fixed input tax recovery method to claim GST incurred on his business inputs at the assumed rate of 90% in the year 2016.

Input Tax Claimable = Input Tax incurred in the taxable period x FITR rate

$$= (RM36,000 + RM18,000 + RM12,000) \times 90\%$$

$$= RM59,400$$

Example 2:

In the taxable period of January 2016, ABC islamic investment bank incurred GST on the following:

- (a) *input tax in relation to exempt supplies (provision of financing to businesses in accordance with Syariah principles) - RM15,000*
- (b) *input tax on standard rated supplies (fee based services) - RM36,000*
- (c) *input tax on investment activities - RM12,000*

For the year 2016, the bank is allowed to use a fixed rate at 90% for the purpose of claiming input tax.

$$\begin{aligned} \text{Input Tax Claimable} &= \text{Input Tax incurred in the taxable period} \times \text{FITR rate} \\ &= (\text{RM36,000} + \text{RM12,000}) \times 90\% \\ &= \text{RM43,200} \end{aligned}$$

For the taxable period of January 2016, the bank is allowed to claim input tax amounting to:

$$\text{RM43,200} + \text{RM15,000} = \text{RM58,200}$$

FREQUENTLY ASKED QUESTIONS

GST Registration

Q1: Am I eligible for group registration?

A1: You are not eligible to register for group registration because as an investment bank, you are making both taxable and exempt supplies. To be registered as a group, you must make wholly taxable supplies.

Q2: Can I use the bank account number that appears in the monthly bank statements as the GST registration number required on tax invoice?

A2: You are not allowed to use the bank's account number as your GST registration number on your tax invoice. You will be given a GST registration number when you register your business.

Q3: I am a dealer representative. Am I required to be registered?

A3: You are not required to be registered. However, your stock broker will be required to be registered if his taxable sales turnover exceeds the threshold and he has to account the GST on your brokerage commission irrespective of

whether the amount of your annual brokerage commission is above or below the threshold limit.

Q4: If my dealer representative wants to quit from my stock broking company and intends to join with another stock broking company, what must I do? What do I have to do if a new dealer representative joins my company?

A4: If your dealer representative wants to quit from your company, you must inform the Customs Department on the withdrawal of the dealer representative by filling the form GST-A. Similarly, you must inform the Customs Department if a new dealer representative joins your company.

Structured Investment Product

Q5: I structure an investment product for my client. In the process, I also supply advisory service for which the charge is embedded into the price of the structured investment product. Do I have to charge GST on my supplies?

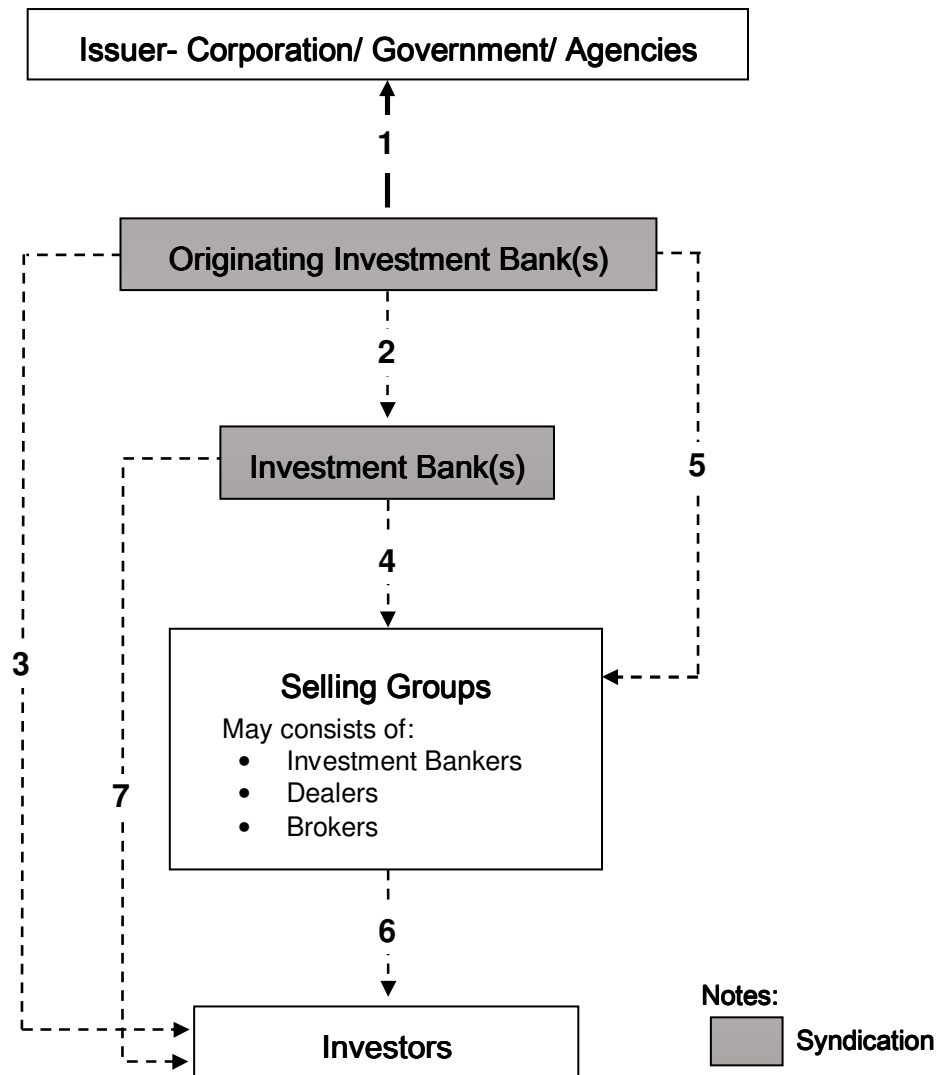
A5: Since the provision of advisory services is part of the cost in the structuring of the investment product, you are not required to apportion the advisory service. GST is not chargeable to the structured product as it is exempt.

Securities Syndication

Q6: I enlist the support of other investment banks to sell securities, thus forming a security syndicate. In addition to that, each member of my syndicate have their own selling groups, consisting of other investment bankers, dealers and brokers that sell to their own investors. How should I account for the GST?

A6: As the originating bank, you are accountable for the GST on the fee based services related to the syndication. Therefore, you should charge GST at a standard rate on any fee based service which you make to your customer. Briefly, the GST treatment can be illustrated in the following diagram:-

Figure 2: Securities Syndication



Explanation on GST treatment:

No.	Transactions	GST
1	Originating Investment Bank(s) charges arranger fee to issuer for the syndication service.	Standard Rate
2	Originating Investment Bank(s) sell securities to Investment Bank(s) and receive commission.	Sell securities - Exempt Commission – Standard Rate

3	Originating Investment Bank(s) may sell securities directly to investors and receive commission.	Sell securities – Exempt Commission – Standard Rate
4	Investment bank(s) sell securities to Selling Group (SGs); receive commission from Originating Investment Bank(s) and pays brokerage fee to (SGs).	Sell securities - Exempt Brokerage and Commission – Standard Rate
5	Originating Investment Bank(s) may sell securities directly to Selling Groups (SGs) and pay brokerage fee.	Sell securities - Exempt Brokerage – Standard Rate
6	SGs sell securities directly to investors, charges brokerage fee and receive commission.	Sell securities - Exempt Brokerage and Commission – Standard Rate
7	Investment Bank(s) may sell securities directly to investor and earn full commission from Originating Investment Bank(s)	Sell securities - Exempt Commission – Standard Rate

Loan Syndication

Q7: I am the arranger of a syndicated loan. I provide the loan of RM100 million and receive an arranger fee of RM50,000. How do I charge GST?

A7: Since the provision of a loan is a provision of credit, it is an exempt supply. However, you are required to account GST on RM50,000.00, since arranger fee is taxable.

Example 3: Mixed Supply

Loan Amount:

RM100 million

Arranger Fee: *RM 50,000.00*

GST @ 6%: (RM50,000 x 6%) RM 3,000.00

Q8: I am the mandated arranger as well as the administrative agent of a syndicated loan facility. The other participating banks' roles in the syndicates' composition is shown in Table 1. What is the GST treatment on the supply of these participating banks?

A8: The GST treatment is shown in the Table 1 below:-

Table 1: Example of a Syndicated Loan Structure

Participating Banks' Role	Services	Fee/Income	GST Treatment
1. Mandated Arranger (Lead manager/ Administrative agent)	1. Originate, structure and syndicate the transaction	1. Syndication fee	Standard rate
	2. Provide portion of the loan to the syndicate.	2. Loan	Exempt
	3. Receives portion of the interest on the loan from borrower.	3. Interest	Exempt
2. Joint Manager/ Co-Manager	1. Member of the syndicate receiving a portion of the syndication's fee.	1. Syndication fee	Standard rate
	2. Provide portion of the loan to the syndicate.	2. Loan	Exempt
	3. Receive interest on	3. Interest	Exempt

	the loan.		
3. Book Runner	1. Issues invitations to participate in the syndication, disseminates information to banks and informs the borrower about the progress of the syndication.	1. Book Runner fee	Standard rate
	2. Provide portion of the loan to the syndicate.	2. Loan	Exempt
	3. Receive interest on the loan.	3. Interest	Exempt
4. Participants only	1. Provide portion of the loan to the syndicate.	1. Loan	Exempt
	2. Receive interest on the loan.	2. Interest	Exempt

Q9: Sometimes an application fee on a non-syndicated loan may be termed as “acceptance fee” or “review fee” and it is charged upon approval of the loan. What is the GST treatment on this fee?

A9: Irrespective of the term you use for the fee, the application fee is subject to GST at a standard rate.

Q10: I charged processing fee when a non-syndicated loan application is approved. Is there GST on processing fee if the loan is declined?

A10: GST is chargeable at a standard rate even though the loan is declined.

Corporate Financing

Q11: Debt assignment is the assignment of debt for a consideration. In this assignment, the debt factor will charge service fee. What is the GST treatment on the service fee?

A11: The service fee on the debt assignment is subject to GST at a standard rate.

Q12: Is there GST for late payment penalties?

A12: If you impose a penalty because your clients did not pay by the due date, the penalty is not subject to GST.

Securities Services

Q13: Many securities transactions are effected by electronic means. Is the supply through a dealing system that matches and sell deals subject to GST?

A13: The trading of securities is an exempt supply. However, the rental of the dealing system is a taxable supply and therefore is subject to GST at a standard rate.

Initial Public Offering (IPO)

Q14: What is the GST treatment on fees paid in an IPO exercise?

A14: Fee based services relating to IPO exercise is standard rated even though you may have progress billings. The GST is due when the billing is made or payment received. This may include any kind of additional costs on report preparation, administrative and maintenance on corporate governance.

Q15: My supply in an IPO exercise is basically related to the new securities of a public company in which I am also the company's underwriter. What is the GST treatment if I sell the new securities in large blocks to institutional or retail buyers?

A15: The sale and purchase of securities to an institution is an exempt supply and therefore it is not subject to GST. GST is not chargeable even though you resell the securities to a retail purchaser. However, if there is any brokerage fee or commission, it is subject to GST at a standard rate.

Acquisition through Borrowings

Q16: A leveraged buyout is essentially a strategy involving the acquisition of another company using borrowed money through bonds or loans in order to meet the cost of the acquisition. Often, the assets of the company being acquired will be used as collateral in addition to the assets of the acquiring company. Is collateral subject to GST?

A16: Collateral is a form of security to ensure settlement of the loans. Hence, it is not subject to GST.

Takeover

Q17: A friendly takeover occurs with the consent of the management of the target company and consists of a straight buyout of the company. In this kind of takeover, the shareholders either receive cash or an agreed-upon number of shares of the acquiring company's shares. What is the GST treatment?

A17: Cash payment and shares buyout is not subject to GST.

Stock Lending

Q18: I lend shares to another entity (borrower) for it to complete some shares transaction. The borrower will return the same number of shares to me at a later agreed date. In this transaction I charged the borrower some fees. Is the fee subject to GST?

A18: The fee you charged the borrower is subject to GST at a standard rate. However, the lending of shares is not subject to GST.

Q19: Where stocks are loaned, the borrower has the legal title of the shares and received the dividend until these shares are returned. What is the GST treatment on the dividend received by the borrower?

A19: The dividend received is not subject to GST.

Swaps

Q20: When is the tax point in an interest rate swaps i.e. when the banks and other financial institutions exchange fixed interest rate on their debts?

A20: An interest rate swap is an exempt supply. Therefore, the issue of tax point does not arise.

Q21: Is the GST treatment on interest rate swaps similar to currency swaps?

A21: The GST treatment will be similar since currency swap is also an exempt supply.

Preparatory Services

Q22: I provide preparatory services to my nominee companies. What is the GST treatment on these preparatory services?

A22: Preparatory services such as preparing and filling of documents in a rights issue are subject to GST at a standard rate.

Stock broking

Q23: My client is a Singaporean. He trades shares on Bursa Malaysia. Do I charge GST on brokerage commission?

A23: You are required to charge GST on the brokerage commission even though your client is not a Malaysian.

Q24: I purchase 10 lots of shares from Hong Kong stock market through my stock broking company in Johor and I have been charged commission twice for the services rendered that is, commission charged by the stock broking company and their parent company in Kuala Lumpur. Do I have to pay GST on the commissions charged for such purpose?

A24: Your payment for both commissions will not be charged GST because it is zero-rated.

Q25: I intend to buy 20 lots of a foreign-listed company's call warrants which are also listed at Bursa Malaysia. Do I have to pay GST on commission for such dealing?

A25: You have to pay GST on the commission charged.

Input tax recovery

Q26: Can an IB claim input tax incurred in respect of medical and hospitalization benefits of its employees?

A26: The bank is not entitled to claim the input tax incurred since medical and hospitalization benefits for the employees are blocked.

Q27: Can an IB claim the input tax incurred in relation to entertainment to existing clients?

A27: The bank may claim the input tax incurred since entertainment to existing clients is not blocked.

Q28: As a dealer's representative or futures broker's representative, I incur GST on telecommunication services when I call my clients through my mobile phone. Can my lead member claim the GST incurred on my behalf?

A28: Your lead member cannot claim the GST incurred on telephone service made by you when you call your clients through your mobile telephone. However, GST paid on your fixed line telephone which is registered under your name is allowed to be claimed as your input tax credit (ITC).

Q29: As a dealer's representative or futures broker's representative, I sometimes incur parking charges on the car which I use to meet up with my clients. Can the stockbroking company claim the GST incurred on my behalf?

A29: Your stockbroking company can claim the GST incurred provided that parking charges incurred is related to the meeting with your client.

Q30: As an investment bank, I sometimes provide margin financing to my clients besides charging brokerage commission. How do I claim the GST incurred on my expenses?

A30: As margin financing is an exempt supply, you are required to apportion and claim the GST incurred on making taxable supplies.

Bad Debts

Q31: After paying upfront the value of a share transaction which includes the share price, commission, stamp duty and GST on commission to my lead member eight months earlier, as a dealer's representative I still have not received any payment from my client. My lead member then proceeded to treat the unpaid dues as bad debts. Can my lead member claim the GST that I have paid on commission?

A31: Your lead member can claim GST in full provided that your lead member has satisfied all of the requirements of bad debts relief. However, when your lead member subsequently recovers the bad debts, the lead member shall pay the GST recovered to the dealer's representative.

Q32: After I have claimed the GST due to the unpaid account, one of my clients pays me. Do I have to pay GST back to the government?

A32: You have to pay back the amount of GST which your client has paid to the government.

FEEDBACK OR COMMENTS

24. Any feedback or comments will be greatly appreciated. Please email your feedback or comments to either Mohd Hisham B. Mohd Nor (m_hisham.nor@customs.gov.my) or Aminul Izmeer B. Mohd Sohaimi (izmeer.msohaimi@customs.gov.my).

FURTHER INFORMATION AND ASSISTANCE

25. Further information can be obtained from:

- (a) GST Website: www.gst.customs.gov.my
- (b) GST Hotline: 03-88822111
- (c) Customs Call Centre:
 - Tel : 03-78067200/ 1-300-888-500
 - Fax : 03-78067599
 - E-mail : ccc@customs.gov.my