



INLAND REVENUE BOARD OF MALAYSIA

GUIDELINES ON TAXATION  
OF  
ELECTRONIC COMMERCE

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# ELECTRONIC COMMERCE GUIDELINES

## 1. INTRODUCTION

- 1.1 This guideline seeks to provide some guidance on basic tax issues and income tax treatment in respect of electronic commerce (e-commerce) transactions. It should be read together with the Income Tax Act 1967 (ITA 1967), other relevant legislations and legal procedures currently in place.
- 1.2 The Inland Revenue Board of Malaysia (IRBM) adopts the principle of neutrality where both e-commerce and conventional business are subject to the same tax treatment. As such, taxpayers in similar situations and carrying out similar transactions should be subject to the same tax treatment.
- 1.3 The complex nature of e-commerce is too varied for this guideline to provide answers to specific issues.

## 2. TERMINOLOGY

For the purpose of this guideline:-

**“e-commerce”** means any commercial transactions conducted through electronic networks including the provision of information, promotion, marketing, supply, order or delivery of goods or services though payment and delivery relating to such transactions may be conducted off-line.

**“Server”** means a device (includes the computer hardware and its operating and basic application software) where e-commerce applications are sited or operated.

**“Website”** means a collection of information, which is linked together and available on the electronic networks that enable transactions to be conducted.

### **3. SCOPE OF CHARGE**

- 3.1 Generally, income tax is imposed on the income of any person accruing in or derived from Malaysia.
- 3.2 Income derived from sources outside Malaysia and which is received in Malaysia is exempt from income tax. However, for a resident company carrying on the business of banking, insurance, sea or air transport, tax is imposed on the income of that company derived from both Malaysia and outside Malaysia.
- 3.3 A non-resident person is taxed only on income that is accrued in and derived from Malaysia.

### **4. SCOPE OF TAX LIABILITY FOR BUSINESS**

- 4.1 There are no specific provisions under the ITA 1967 which address e-commerce transactions. Therefore, the general provisions and interpretations of the ITA 1967 will be applicable.
- 4.2 Income of a person accruing in or derived from Malaysia is subject to tax in Malaysia.
- 4.3 For business income, where the business operations are carried on in Malaysia, the income of the person attributable to those business operations is deemed to be derived from Malaysia. The determination of whether or not an income is derived from Malaysia is a question of fact and degree. The wider the scope and extent of the business operations in Malaysia, the greater the likelihood that the income of that operations is subject to tax in Malaysia.
- 4.4 In determining the carrying on of business operations within Malaysia, some of the factors to be considered include performance of contractual

obligations and location where contracts are formed (for example negotiations of the contract, costing of the contract, etc), services are performed, or where goods are stored and arrangement was made for delivery of the products.

4.5 In the context of e-commerce, some business activities that may be considered in determination of business operations include sourcing of content, procurement of goods, promotions, advertisement, selling, updating and maintaining the website, uploading and downloading of contents, etc.

4.6 In the case where a Double Taxation Agreement (DTA) is applicable, the test to determine whether Malaysia has taxing rights over the business income is based on the Permanent Establishment (PE) concept.

## **5. TREATMENT OF SERVER AND WEBSITE IN DETERMINING DERIVATION OF e-COMMERCE INCOME**

5.1 A website is hosted on a server which is located at a certain place. Both server and website would facilitate the performance of business activities. However, a server / website itself do not carry any meaning in determining derivation of income. Business income from e-commerce would be considered as Malaysian income if the operations test shows that the person is carrying on a business in Malaysia. Even though the server is fully automated in performing business activities, the substantial part of the business activities such as updating and maintaining the current information on the website is still managed by a human.

5.2 The examples below are illustrations in determining business operations of e-commerce based on the above factors and business activities regardless of the location of the server:

### Example 1: Trading

N Sdn. Bhd. carries on a business of selling software in Malaysia. It has a website hosted on a server located outside Malaysia. The website allows customers to identify products, answer queries on its products, order the products online and make payments for the purchase. The website also allows the downloading of the software in digitized format. Apart from these functions performed by the website, all business activities of the company, such as the procurement of software, the supply of information for the website, the storage of software, the physical delivery of software (compact disc), and the maintenance of the website are carried on in Malaysia.

Income from selling of the software is deemed to be derived from Malaysia due to the substantial business operations in Malaysia regardless of the location of the server.

### Example 2: Services

AA Sdn. Bhd. operating in Malaysia is engaged in the provision of consultancy services. It has a website hosted on a server located outside Malaysia. The website supplies details of its services, answers enquiries, enable communications with its clients/potential clients, and accept payments for services rendered. The company obtains consultancy projects from overseas clients through the website. The business activities relating to the consultancy services, including collecting and analysing data, undertaking research, preparing reports, etc., is done in Malaysia.

The income derived from the consultancy services is deemed to be derived from Malaysia due to the substantial business operations in Malaysia regardless of the location of the server.

### Example 3: Manufacturing

ZA Sdn. Bhd. is a manufacturer of car accessories, which has its principal place of business in Malaysia. It has a website hosted on a server located outside Malaysia. Through the website, customers obtain details of the company's products and prices, negotiate with the company for purchases, order goods, and make payments. The company's business activities in Malaysia include preparing information for the website, answering enquiries from customers, procuring supplies for its manufacturing operations, manufacturing its products, storing, and making delivery arrangements for the finished products.

Income from manufacturing is deemed to be derived from Malaysia pursuant to sub-sub section 12(1)(b) ITA 1967.

## 6 EXAMINATION OF BUSINESS MODELS

There are several basic models identified in this guideline to provide guidance as to whether or not income from e-commerce is derived from Malaysia and would be subject to Malaysian tax. The models are set out below:

### 6.1 A resident person having business operations in Malaysia sets up a website in Malaysia.

#### 6.1.1 Assumptions

- a) The business can either be manufacturing, trading or provision of services in Malaysia.
- b) Products can either be tangible or intangible.
- c) Website is hosted on a server in Malaysia.
- d) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is possible for intangible products (i.e. software, music, videos, images, digital books or other digital products), while tangible

products are delivered through normal physical delivery channels.

- e) The business activities include sourcing for contents/ procurement of goods, promotions and advertisement, selling, arranging for delivery of the products, and maintaining the current information on the website in Malaysia.

6.1.2 As business operations of the person are substantially carried on in Malaysia, business income from e-commerce is deemed to be derived from Malaysia and thus, subject to income tax in Malaysia.

## **6.2 A resident person having business operations in Malaysia sets up a website outside Malaysia.**

### 6.2.1 Assumptions

- a) The business can either be manufacturing, trading or provision of services in Malaysia.
- b) Products can either be tangible or intangible.
- c) Website is hosted on a server outside Malaysia.
- d) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is possible for intangible products (i.e. software, music, videos, images, digital books or other digital products), while tangible products are delivered through normal physical delivery channels.
- e) The business activities include sourcing for contents/ procurement of goods, promotions and advertisement, selling, and arranging for delivery of the products in Malaysia.
- f) The activities in relation to maintaining the website such as developing the website, uploading and updating information on

the website can be performed either in Malaysia or outside Malaysia.

6.2.2 As business operations of the person are substantially carried on in Malaysia, business income from e-commerce is deemed to be derived from Malaysia and thus, subject to income tax in Malaysia. Even if the activities to maintain the website are performed outside Malaysia, the business operations are considered to be carried on in Malaysia. Thus all profits, including those from sales via the website outside Malaysia is deemed to be derived from Malaysia and subject to tax in Malaysia.

### **6.3 A resident company having business operations in Malaysia sets up a website and branch outside Malaysia.**

#### 6.3.1 Assumptions

- a) The business can either be manufacturing, trading or provision of services in Malaysia.
- b) Products can either be tangible or intangible.
- c) Website is hosted on a server outside Malaysia.
- d) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is possible for intangible products (i.e. software, music, videos, images, digital books or other digital products), while tangible products are delivered through normal physical delivery channels.
- e) The business activities include sourcing for contents/ procurement of goods, promotions, advertising, selling and arranging for delivery of the products.
- f) The company operates a branch outside Malaysia. Activities of the branch are marketing and selling of the company's products

and maintaining the current information on the website as well as fulfilling the orders and making arrangement for the delivery of the products.

6.3.2 As the substantial business activities are carried on in Malaysia, business operations is thus in Malaysia. Income of the company derived from its operations in Malaysia is liable to tax in Malaysia whilst income derived from sales via the website that are attributable to the business operations of the branch outside Malaysia are deemed not to be income derived from Malaysia.

#### **6.4 A resident person having business operations outside Malaysia sets up a website in Malaysia.**

##### 6.4.1 Assumptions

- a) The business can either be manufacturing, trading or services.
- b) Products can either be tangible or intangible.
- c) Website is hosted on a server in Malaysia.
- d) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is possible for intangible products (i.e. software, computer games, music, videos, images, digital books or other digital products), while tangible products are delivered through normal physical delivery channels.
- e) The business activities include sourcing for contents/ procurement of goods, promotions and advertisement, selling, arranging for delivery of the products, and maintaining the current information on the website outside Malaysia.

6.4.2 As business operations of the person are carried on outside Malaysia, business income from e-commerce is not subject to

income tax in Malaysia. A website hosted on a server in Malaysia without business operations in Malaysia, would not amount to the carrying on of a business in Malaysia.

## **6.5 A resident person having business operations outside Malaysia sets up a website outside Malaysia.**

### 6.5.1 Assumptions

- a) The business can either be manufacturing, trading or services.
- b) Products can either be tangible or intangible.
- c) Website is hosted on a server outside Malaysia.
- d) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is possible for intangible products (i.e. software, music, videos, images, digital books, magazine or other digital products), while tangible products are delivered through normal physical delivery channels.
- e) The business activities include sourcing for contents, promotions and advertisement, selling, servicing, arranging for delivery of the products, providing technical support of the website and maintaining the current information on the website outside Malaysia.

6.5.2 As business operations of the person are carried on outside Malaysia, that income from e-commerce would not be considered as derived from Malaysia, and thus not subject to income tax in Malaysia.

## **6.6 A non-resident person having business operations in Malaysia sets up a website in Malaysia.**

### 6.6.1 Assumptions

- a) The business can either be manufacturing, trading or services.
- b) Products can either be tangible or intangible (eg: online distributor).
- c) Website is hosted on a server in Malaysia.
- d) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is possible for intangible products (i.e. software, music, videos, images, architecture design, digital books or other digital products), while tangible products are delivered through normal physical delivery channels.
- e) Business activities carried on in Malaysia include selling, marketing, servicing, delivering the products and providing technical support of the website.

6.6.2 As the business operations are carried on in Malaysia, the income generated from e-commerce is deemed to be derived from Malaysia and subject to tax in Malaysia.

## **6.7 A non-resident person having business operations in Malaysia sets up a website outside Malaysia.**

### 6.7.1 Assumptions

- a) The business can either be manufacturing, trading or services.
- b) Products can either be tangible or intangible.
- c) Website is hosted on a server outside Malaysia.
- d) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is

possible for intangible products (i.e. software, music, videos, images, digital books or other digital products), while tangible products are delivered through normal physical delivery channels.

- e) Business activities carried on in Malaysia include selling, marketing, servicing, delivering the products and providing technical support of the website.

6.7.2 As the business operations are carried on in Malaysia, the income generated from e-commerce is deemed to be derived from Malaysia and subject to tax in Malaysia.

## **6.8 A non-resident person having business operations outside Malaysia sets up a website in Malaysia.**

### 6.8.1 Assumptions

- a) The business can either be manufacturing, trading or services.
- b) Products can either be tangible or intangible.
- c) Website is hosted on a server in Malaysia.
- d) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is possible for intangible products (i.e. software, music, videos, images, digital books or other digital products), while tangible products are delivered through normal physical delivery channels.
- e) Business activities carried on outside Malaysia include selling, marketing, servicing, delivering the products and providing technical support of the website.

6.8.2 As the business operations are carried on outside Malaysia, the income generated from e-commerce is deemed not to be derived from Malaysia and thus not subject to tax in Malaysia.

**6.9 A non-resident company having business operations outside Malaysia sets up a website outside Malaysia and branch in Malaysia.**

6.9.1 Assumptions

- a) The business can either be manufacturing, trading or services.
- b) Products can either be tangible or intangible.
- c) The company operates a branch in Malaysia. Activities of the branch are selling, marketing, servicing and delivering the products.
- d) Website is hosted on a server outside Malaysia.
- e) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is possible for intangible products (i.e. software, music, videos, images, digital books or other digital products), while tangible products are delivered through normal physical delivery channels.
- f) The business activities include sourcing for contents/ procurement of goods, promotions and advertisement, selling, arranging for delivery of the products, and maintaining the current information on the website outside Malaysia.

6.9.2 Income from business operations carried on outside Malaysia is deemed not to be derived from Malaysia and thus not subject to tax in Malaysia whilst, income including e-commerce income that are attributable to the business operations of the branch in Malaysia is deemed to be derived from Malaysia.

## **6.10 A non-resident company having business operations outside Malaysia sets up a website and branch in Malaysia.**

### 6.10.1 Assumptions

- a) The business can either be manufacturing, trading or services.
- b) Products can either be tangible or intangible.
- c) Website is hosted on a server in Malaysia.
- d) The website allows customers to identify products or services, answer queries on its products or services, order the products online and make payments for the purchase. Online delivery is possible for intangible products (i.e. software, music, videos, images, digital books or other digital products), while tangible products are delivered through normal physical delivery channels.
- e) The company operates a branch in Malaysia. Activities of the branch are selling, marketing, servicing, delivering the products and providing technical support of the website.

6.10.2 As the business operations are carried on outside Malaysia, the income is deemed not to be derived from Malaysia and thus not subject to tax in Malaysia. Whilst, income derived from the branch in Malaysia is liable to tax in Malaysia.

## **7. WITHHOLDING TAX ON ROYALTY**

7.1 Where income from e-commerce of a non-resident is deemed not to be business income derived from Malaysia because the business operations is not carried on in Malaysia (refer to above model under paragraph 6.8, 6.9 and 6.10), payments to the non-resident in the nature of royalty and deemed to be derived from Malaysia is subject to withholding tax.

7.2 The term 'royalty' defined under the ITA 1967 includes payments for the use of or the right to use copyrights, know-how or information concerning technical, industrial, commercial or scientific knowledge, experience or skill to a non-resident. Where the definition of royalty provided in a DTA differs from that of the ITA 1967, the DTA definition shall prevail.

7.2.1 Payment for the use of, or the right to use copyrights of intangible products such as

- (a) Downloading of a digital product to a customer's hard disk or similar media.
- (b) Licensing arrangements to reproduce, modify and adapt, the absence of which would constitute an infringement of copyright.

In the above example, if the payment is for the use of, or the right to use copyrights, the income constitutes royalty. On the other hand if the payment is for the purchase of the product, the transaction would not result in royalty income.

7.2.2 Payment for the use of, or the right to use know-how (intangible products).

Example 4:

Any form of electronic supply of know-how (i.e. undivulged technical knowledge, information, experience or technique that is necessary for the industrial reproduction of a product or process) which take the form of technical data, samples or patterns, or details of processing or production methods for which payment is made constitutes "royalty".

In the above example, a distinction should be made between contracts for the supply of existing knowledge or experience which can be used by the customer to produce an outcome and contracts where the supplier applies his knowledge and experience to create a result for the customer. The former refers to a contract for the supply of know-how (royalty) and the latter refers to a contract for the provision of services (technical fee).

- 7.2.3 Payment for the use of, or the right to use information concerning technical, industrial, commercial or scientific knowledge, experience or skill.

Example 5:

Any electronic use or the right to use the above information which may include access to unpublished knowledge or information gained through scientific, technical etc. experience. This may include supply of information on markets or fashion trends, information concerning future technological advances or access to unpublished information contained in a database. Payment for these constitutes royalty.

- 7.3 Royalty is deemed to be derived from Malaysia if the payer is a resident, the government, a state government or a local authority. If the royalty payment is charged as an outgoing or as an expense against any business in Malaysia, it is also deemed derived from Malaysia.

## **8. ISSUES OF DOUBLE TAXATION AND TAX TREATIES**

- 8.1 Where income from e-commerce by a resident person is subject to tax both in Malaysia and the foreign country, provision for relief is available in

the ITA 1967 and the relevant Double Taxation Agreement (DTA) entered into by the Government of Malaysia and the foreign country.

8.2 In the above model as described in paragraph 6.2, where a resident person having business operations in Malaysia and sets up a website on a server outside Malaysia, there could be an issue of double taxation on the income arising from e-commerce. In such case, relief from double taxation may be sought under the DTA between Malaysia and the foreign country.

### 8.3 Relief Provisions

#### (a) **Non DTA context**

In the absence of a DTA, a unilateral tax credit may be allowed by virtue of section 133 of the ITA 1967 in accordance with Schedule 7 of the ITA 1967.

#### (b) **DTA context**

Where a DTA is available, a bilateral tax credit may be allowed by virtue of section 132 of the ITA 1967 in accordance with Schedule 7 of the ITA 1967. The elimination of double taxation is subject to the terms and provisions as stipulated in the DTA.

### 8.4 Permanent Establishment (PE)

8.4.1 Under a DTA, the allocation of taxing rights over business income between countries that are a partner to a tax treaty is based on the PE concept.

8.4.2 PE is defined as a “fixed place of business through which the business of an enterprise is wholly or partly carried on”. This definition contains the following conditions:

- (a) the existence of a “place of business”, i.e. a facility such as premises or, in certain instances, machinery or equipment, and
- (b) the place of business must be “fixed”, i.e. it must be established at a distinct place with a certain degree of permanence and
- (c) the carrying on of the business usually by personnel of the enterprise through the fixed place of business.

8.4.3 In the above model as described in paragraph 6.8, the issue of PE may arise. In this paragraph, if the server constitutes a PE under the applicable DTA, then the income arising from e-commerce through the server will be considered as Malaysian source income and liable to tax in Malaysia.

8.4.4 As provided in the Organisation for Economic Co-operation and Development (OECD) Commentary, a server at the disposal of a business (i.e. owned or rented by it) can only constitute a PE of the business if the activities conducted through the server are not regarded as preparatory or auxiliary. The Commentary also states that a PE may be constituted even if no personnel of the business are required at the server’s location for the operation of the server.

8.4.5 Examples of activities which would generally be regarded as auxiliary include:

- (a) providing a communication link-much like a telephone line – between suppliers and customers
- (b) advertising of goods or services
- (c) gathering market data
- (d) supplying information

8.4.6 The general view is that computer equipment, such as a server, could constitute a permanent establishment where the functions performed at the server represent a significant and essential part of the enterprise's business activities.

Examples of functions which may be considered to be significant and an essential part of the enterprise's business activities are conclusion of the contract with the customer, the processing of the payment and the delivery of products. However, such functions should be considered in light of the nature of the enterprise's business.

**Note:**

All enquires with regards to this guideline can be forwarded to:

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Inland Revenue Board  
Level 17, Menara Hasil  
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Cyber 8, Cyberjaya  
63000 Selangor

Tel. No. 03-83138888

Date : 01 January 2013

## Summary of Positions Taken by the Authorities Under Various Scenarios

	Business Operation		Website Hosted		e-Commerce Income Deemed Derived from Malaysia? (Example ref)
	In Malaysia	In Overseas	In Malaysia	In Overseas	
	√		√		Yes [6.1]
R E S I D E N T	√			√	Yes [6.2]
	√	Branch		√	No. [6.3]- Income of the company from operations in Malaysia taxable in Malaysia whilst income derived from sales via the website that are attributable to the business operations of the branch outside Malaysia not deemed to be derived from Malaysia.
		√	√		No [6.4]
		√		√	No [6.5]
N O N  R E S I D E N T	√		√		Yes [6.6]
	√			√	Yes [6.7]
		√	√		No [6.8]
	Branch	√		√	Yes. Income including e-commerce income that are attributable to the business operations of the branch in Malaysia. [6.9]
	Branch	√	√		No. Whilst Income from the branch liable to tax in Malaysia [6.10]
<ul style="list-style-type: none"> <li>● Business -either manufacturing / trading /services</li> <li>● Products- either tangible / intangible</li> <li>● Website-identify / queries / order / payment / online delivery</li> <li>● Tangible products-deliver by normal physical channel</li> <li>● Business activities include sourcing of contents / procurement of goods / promotion and advertisement / selling / arranging for delivery of products / maintaining website</li> </ul>					