
TECHNICAL

Direct Taxation

[INCOME TAX \(EXEMPTION\) \(NO.7\) ORDER 2018 \[P.U. \(A\) 386/2018\]](#)

General

In our e-CTIM TECH-DT [3/2019](#) and [113/2019](#), we highlighted the contents of [Income Tax \(Exemption\) \(No.6\) Order 2018 \[P.U. \(A\) 385/2018\]](#) (“the previous Order”) under which income tax exemption is granted to a “principal hub” (PH), the meaning of which is set out in paragraph 3 of that Order. One of the qualifying criteria under that paragraph is that the PH “*is already operating in Malaysia*”.

In this Order, exemption from income tax is granted to a PH which must meet requirements which are similar in all respects to those stated in paragraph 3 of the previous Order, except for the one mentioned above. Under paragraph 3(c) of this Order, the PH that qualifies for exemption –

“does not have an existing entity or related entity in Malaysia which carries on any qualifying services in Malaysia prior to the application referred to in subparagraph 4(3) is made;”

This Order has effect from the year of assessment (YA) 2018.

Definitions

Meanings of words used in this Order are found in paragraph 2. Among them are the following:

Word	Meaning
Core income generating activities (CIG activities)	Activities undertaken by a principal hub in relation to the provision of qualifying services or qualifying trading activities;
Qualifying trading activities	Activities undertaken by a PH other than a commodity based company, in respect of procurement and sale of raw materials, components and finished products from the PH to a <u>network company</u> within or outside Malaysia;
Principal hub (PH)	A PH as provided under paragraph 3
Qualifying services (QS)	Services specified in Schedule 1
<i>The meanings of words underlined here and below are also provided in this paragraph.</i>	

Principal hub (paragraph 3)

As stated above, a PH referred to in this Order must meet the same eligibility requirements as stated in the previous Order, except for the one mentioned above (under “General”) (Refer to our [e-CTIM TECH-DT 13/2019](#)) (See Note below).

Note:

An amendment to paragraph (3)(d) of this Order was made via [Income Tax \(Exemption\) \(No. 7\) 2018 \(Amendment\) Order 2019](#) [P.U.(A) 42/2019] (Gazette date 19/2/2019). Under this amendment, the words “which are located in 3 countries outside Malaysia” have been deleted. The amendment is deemed to have effect from YA 2018.

Exemption (paragraph 4)

A PH is exempted from payment of income tax in respect of *statutory income* derived from CIG activities in the basis period for a YA. (paragraph 4(1))

The following are some points to note from paragraph 4, relating to the exemption:

<u>Paragraph</u>	<u>Provision</u>
4(2) -	The exemption shall be for a period of 5 consecutive YAs (hereinafter referred to as "the exempt YAs"), the commencement of which period shall be determined by the Minister.
4(3) -	The application for exemption is made to the Minister through the <u>Malaysian Investment Development Authority</u> (MIDA) on or after 1/1/2018 but not later than 31/12/2020.
4(4) -	The exemption is granted subject to all conditions specified in Schedule 2 for the relevant category of PH and any other condition which may be imposed by the Minister.
4(5) -	This paragraph provides the formula for ascertaining statutory income (SI) that is exempted. The formula provided in this paragraph apply to the following:
4(5)(a)	- <u>provision of QS by the PH</u> , in the case of – (i) a PH under Category 1 of Schedule 2; (ii) a PH under Category 2 of Schedule 2; (iii) a PH under Category 3 of Schedule 2.
4(5)(b)	- <u>provision of qualifying trading activities by the PH</u> , in the case of – (i) a PH under Category 1 of Schedule 2; (ii) a PH under Category 2 of Schedule 2; (iii) a PH under Category 3 of Schedule 2.
	In each case stated above, the formula is represented by $\frac{A}{B} \times C$ The values of A, B, and C are specified in each case in the relevant paragraph .
4(6) -	SI referred to above is determined after deducting allowances under Schedule 3 of the Income Tax Act 1967 (ITA) notwithstanding that no claim for such allowances has been made.

Exclusion of intellectual property (IP) income (paragraph 5)

Among the important points to note are the following:

<u>Paragraph</u>	<u>Provision</u>
5(1) -	The following IP income of a PH derived from its CIG activities is to be excluded in ascertaining SI which is exempted: (a) <i>royalties and other income derived*</i> on or after 1/7/ 2018 but before 1/7/ 2021 from <i>new intellectual property rights*</i> that <i>the PH owns*</i> ; and (b) <i>royalties and other income derived</i> on or after 1/7/2021 from all <i>IP rights*</i> that <i>the PH owns*</i> . * The meanings of these terms and phrases (in italics) are explained in paragraph 5(2) .

Any IP excluded as stated above is subject to tax under the ITA.

Other Provisions

The following are brief summaries of the other provisions of this Order:

<u>Paragraph</u>	<u>Provision</u>
6 -	Sets out the tax treatment for a PH that suffered losses. The losses referred to are an adjusted loss for the basis period for a YA, ascertained in accordance with the following sections of the ITA: (1) S44(2) (2) S43(2),

which is incurred during the exempt YAs in respect of a business source consisting of the provision of QS or qualifying trading activities. Such a loss is to be disregarded from the source consisting of the provision of QS or qualifying trading activities in Malaysia and other businesses. (paragraphs 6(1) and 6(2))

Any amount of adjusted loss ascertained pursuant to S43(2) and S44(2) of the ITA in respect of a business source consisting of the provision of QS or qualifying trading activities shall be disregarded for the purposes of the ITA in the YA in which the last date of the exempt YAs of the PH falls and in the following YAs after the exempt YAs, as the case may be. (paragraph 6(3))

- 7 - Subject to conditions stated in paragraphs 7(1)(a) and (b), the Minister may extend the exempt YAs for another period of 5 YAs.

The requirements relating to the application for extension of the exempt YAs are stated in paragraphs 7(2) and 7(3).

- 8 - Empowers the Minister to withdraw the exemption granted if the PH fails to comply with any of the conditions imposed.
- 9 - The Minister may, at any time, except where the PH fails to comply with any conditions relating to the grant of exemption, allow the PH to surrender the exemption granted under this Order, by notice in writing to the Minister through MIDA.
- 10 - Lists the situations wherein this Order is not applicable (i.e. where the PH has been granted, or made claims for, incentives / exemptions listed under any of the legislations specified in this paragraph.)

Schedule 1 - Lists the QS that comes under each of the following clusters:

1. Strategic services
2. Business services
3. Shared services

Schedule 2 - Conditions for a PH which provides QS and those which provide qualifying trading activities are separately stated (Note). The [specified requirement](#) for each of the following categories are different:

Principle hub	Category 1	Category 2	Category 3
Income tax rate	0%	5%	10%

Note:

An amendment to Schedule 2 of this Order was made via [Income Tax \(Exemption\) \(No. 7\) 2018 \(Amendment\) Order 2019](#) [P.U.(A) 42/2019] (Gazette date 19/2/2019) (reported in our [e-CTIM TECH-DT 13/2019](#)). Under this amendment, the condition for a PH in respect of the location where the QS or qualifying trading activities are provided by the PH to its network companies and particulars relating to it have been deleted. The amendment is deemed to have effect from YA 2018.

Members may read the Order in full at the official website of the [Attorney General's Chambers](#).

Disclaimer

This document is meant for the members of the Chartered Tax Institute of Malaysia (CTIM) only. CTIM has taken all reasonable care in the preparation and compilation of the information contained in this e-CTIM. CTIM herein expressly disclaims all and any liability or responsibility to any person(s) for any errors or omissions in reliance whether wholly or partially, upon the whole or any part of this e-CTIM.