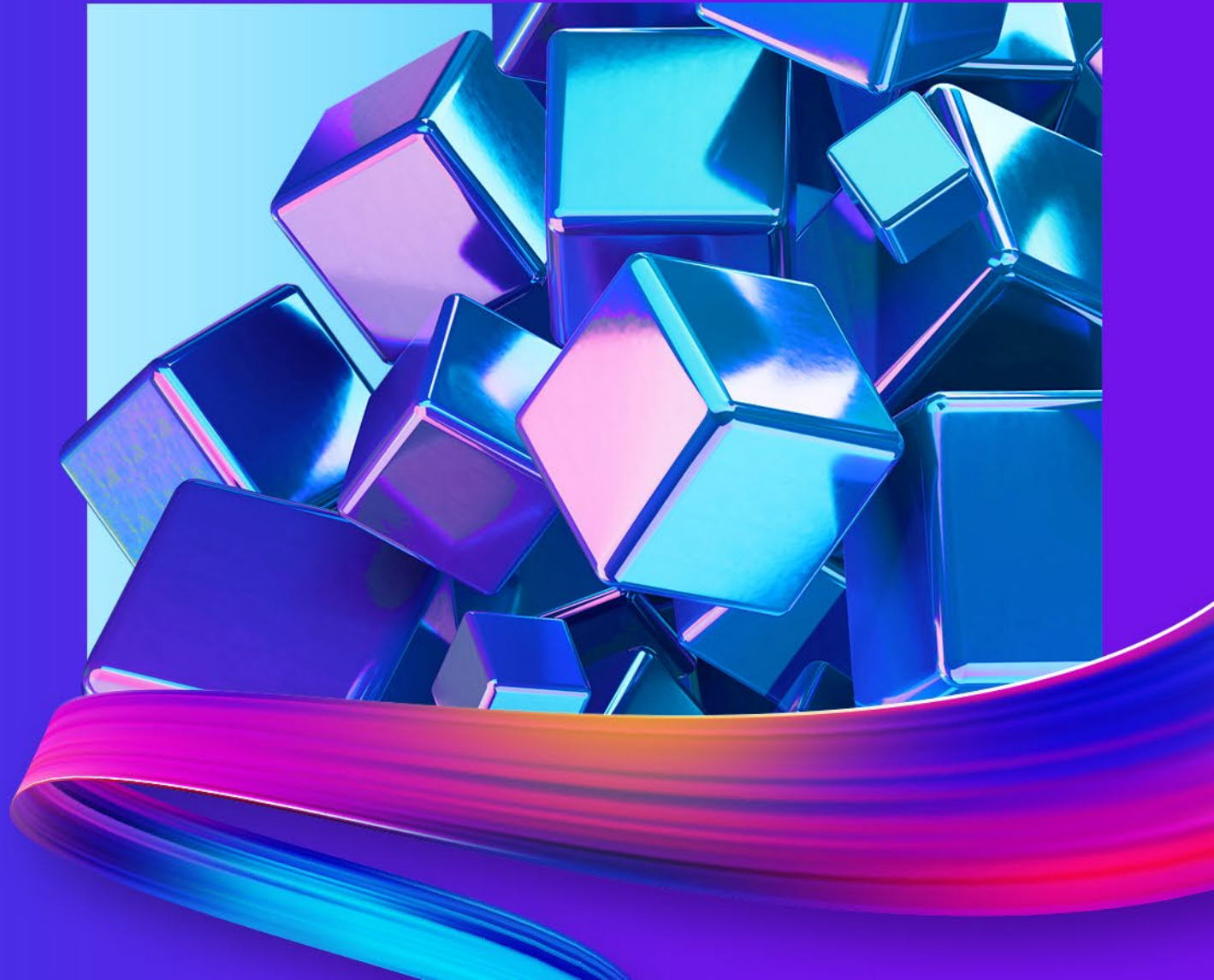




Contemporary tax issues: Malaysian TP updates and audit trends

National Budget Webinar 2023 | 12 December 2023

KPMG in Malaysia

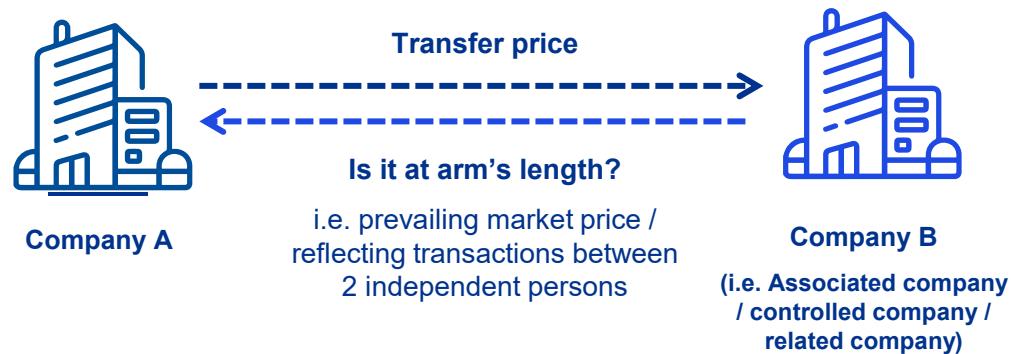


What's new in the TP landscape?



Basics of Transfer Pricing (“TP”)

What is Transfer Pricing?



Section 140A(2)

“... where a person... enters into a transaction with an associated person... for the acquisition or supply of property and services,...shall determine and apply the arm's length price...”

Applicable on Transactions Between Associated Persons (Section 140A)

Direct Control

(Person one of whom has control over the other e.g., through shareholding)

Indirect Control

(Has share capital of more than 20% and dependency on proprietary rights; influences business activities; or ability to appoint directors)

Example of Controlled Transactions

Sales or purchases of goods, services, use of intangibles (i.e. patent, know-how, trademark, copyright, etc.), financial assistance (i.e. loans, interest bearing trade credits, advance or debt and the provision of any security or guarantee), etc.

Salient points of the Income Tax (TP) Rules 2023



New definition of contemporaneous TP documentation

Prior to YA 2023

- when a person is developing or implementing any controlled transaction; and
- If there are material changes in a controlled transaction during a tax assessment year, the documentation shall be updated prior to the due date for furnishing a tax return for that year.

YA 2023

TP documentation is brought into existence **prior to the due date for furnishing the tax return (i.e., Form C).**



To date the TP documentation

Taxpayers are now required to **indicate the completion date of the TP documentation** to satisfy the contemporaneous requirement, which is prepared **prior / at the point of submission of Form C.**

Failure to Comply



Penalty of RM20,000 to RM100,000



Imprisonment of six (6) months.



Tapered Arm's Length Range

The arm's length range is now defined from **37.5th** percentile to **62.5th** percentile of the benchmarking results.

On top of the tapered arm's length range, it is legislated that IRB can now adjust the taxpayers' results to the median point of the arm's length range in the event of TP audit (see illustration)

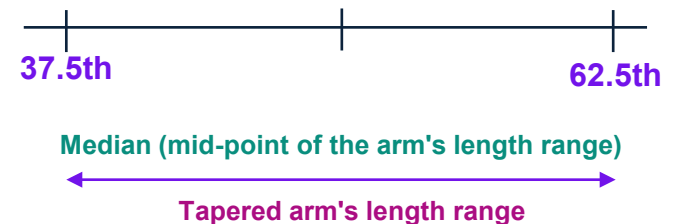


Illustration of the tapered arm's length range

Set of comparable:

Net Operating Margin ("OM")	Company A	Company B	Company C	Company D	Company E
	4.0%	5.0%	6.5%	7.0%	8.0%

Benchmarking range of results:

Prior to YA2023

Range	Net OM
Minimum	4.0%
25 th percentile	5.0%
Median	6.5%
75 th percentile	7.0%
Maximum	8.0%

Arm's length
range

YA2023

Range	Net OM
Minimum	4.0%
37.5 th percentile	5.8%
Median	6.3%
62.5 th percentile	6.8%
Maximum	8.0%

Salient points of the Income Tax (TP) Rules 2023



Change in content of TP documentation

Taxpayers are now required to prepare a localized master file (i.e., **Schedule 1**) as part of contemporaneous TP documentation.

There are also other information that are required (i.e., **Schedule 2** and **Schedule 3**) which makes the TP documentation for YA 2023 rather extensive and voluminous.

Schedule 1

Multinational Enterprise (“MNE”) Group Information

Schedule 2

Business Information

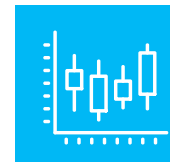
Schedule 3

Cost Contribution Arrangement



Indication of non-applicability

Taxpayers are now required to indicate **if any of the prescribed information** under the documentation requirement is not applicable.



Use of latest data available

Taxpayers shall determine the arm’s length price **using the latest data available** at the point of preparation of TP Documentation.



Selection of most appropriate TP method

Taxpayers are **not required to follow** the hierarchy in selecting the most appropriate TP method.

What is the new content of contemporaneous TP documentation?

Schedule 1

Multinational Enterprise (“MNE”) Group Information

- ✓ Worldwide organizational structure
- ✓ Product and services , geographic markets, supply chain, functional analysis, etc.
- ✓ Intangible properties
- ✓ Financial activities
- ✓ Financial and tax positions

Similar to Master File and relevant to the MNE’s group business in Malaysia

Schedule 2

Business Information

- ✓ Organizational structure
- ✓ Nature of the business, industry and market conditions
- ✓ Related party transactions (“RPTs”)
- ✓ Details of pricing policy of RPTs
- ✓ Assumption, strategies and information regarding pricing policy
- ✓ Functional, asset and risk (“FAR”) analysis
- ✓ Comparability analysis
- ✓ Selection and application of TP methodologies

The information required is extensive and voluminous

Schedule 3

Cost Contribution Arrangement (“CCA”)

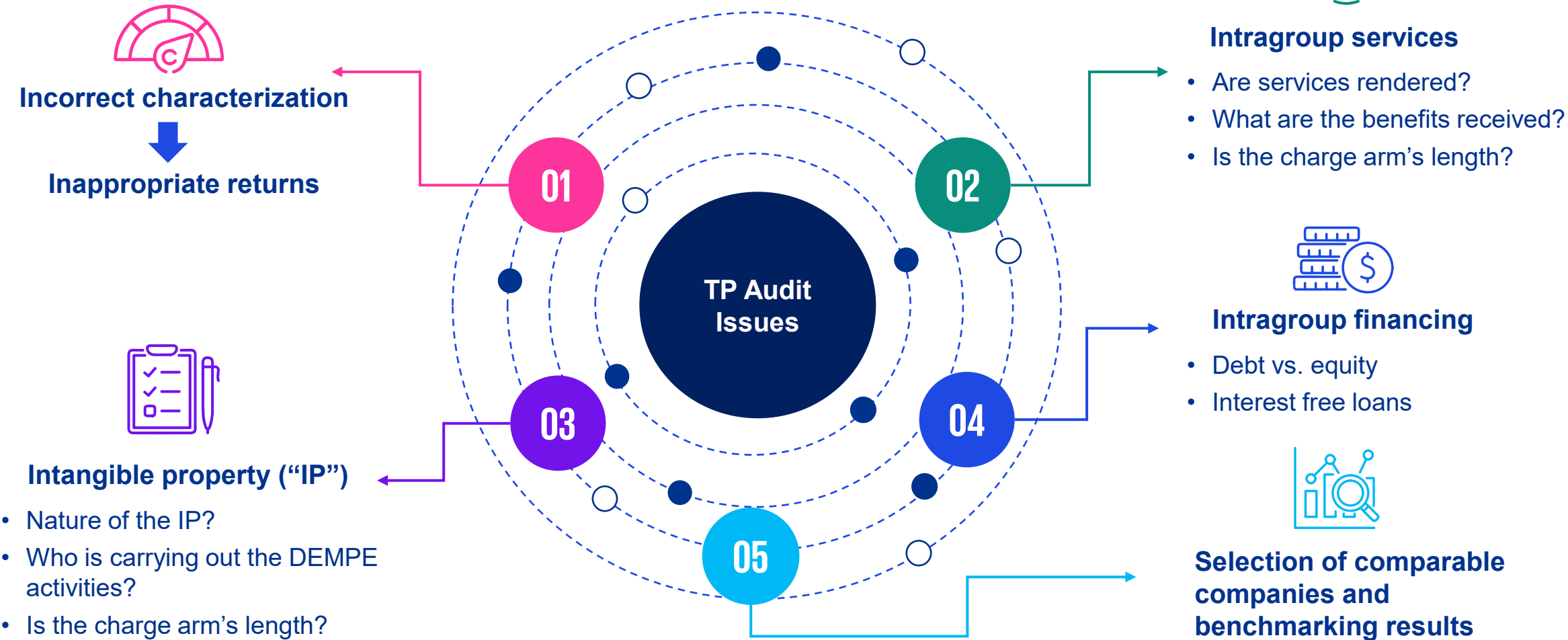
- ✓ Agreements
- ✓ List and identity of participants
- ✓ Scope of activities
- ✓ Duration
- ✓ Total amount
- ✓ Allocation of task and responsibilities

Detailed information on the CCA activity

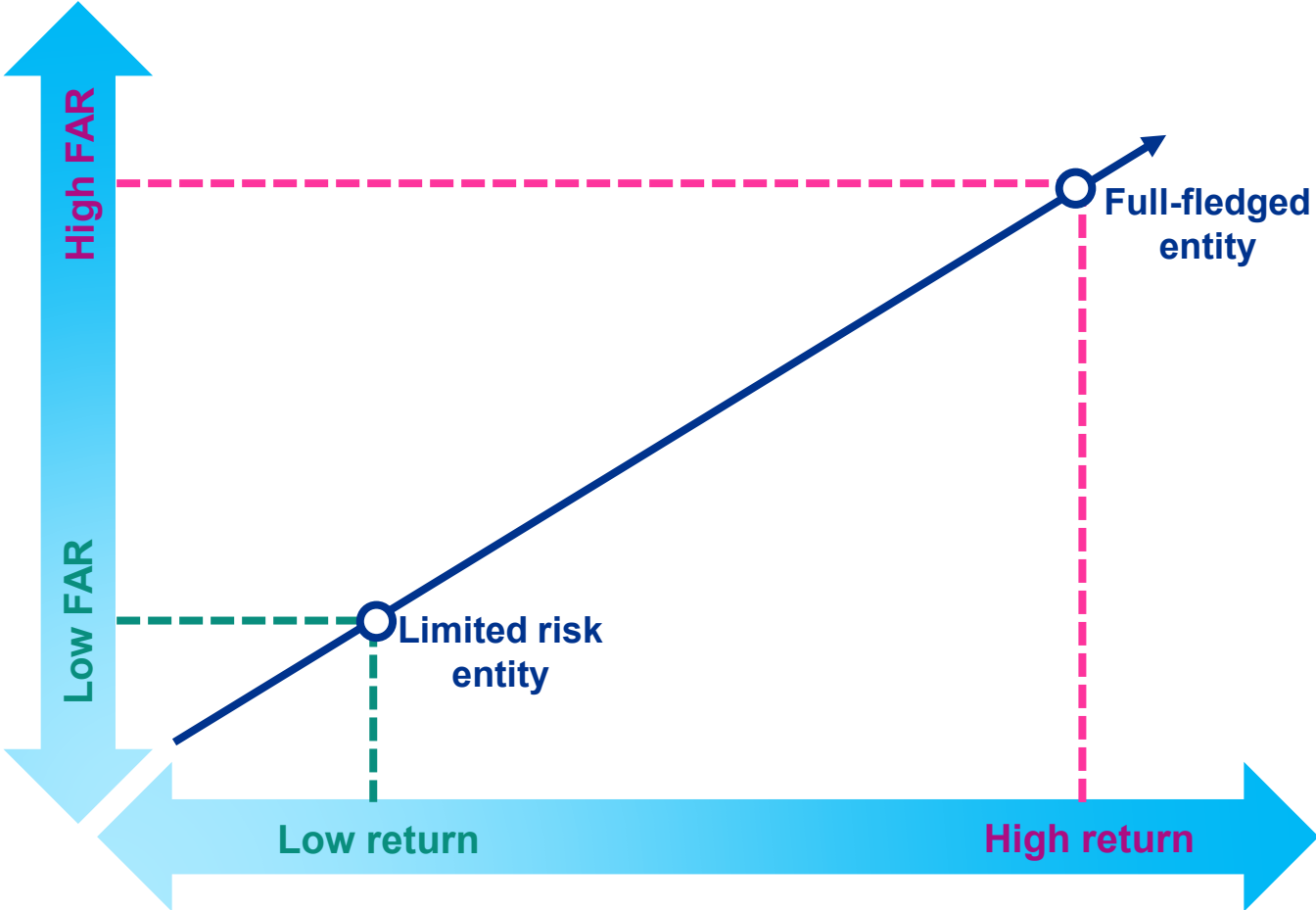
Issues in TP Audits



Issues in TP Audits



TP Audit: Incorrect characterization leads to inappropriate return



Entity characterisation

Limited risk

- Performs functions solely based on the instructions from principals
- Uses assets only to a minor degree
- Does not bear significant risks
- Earns a lower but fixed return

Full-fledged

- Acts as entrepreneur
- Owns brands or intangible assets
- Bears major risks
- Earns residual profit/ loss

TP Audit: Intragroup Services

Types of services usually provided within a group of companies

 Management services

 Business consultancy

 Support services (accounting, tax, public relations, personnel, IT, etc.)

 Distribution and commission services

 Leasing

 Treasury

 Staff secondments

Whether the services were actually performed

Substance test

Benefit test


Whether the service recipients receive any benefit from the intragroup services

Arm's Length Test

Whether pricing mechanism applied by service provider is in compliance with the arm's length principle

TP Audit: Intangible Properties


THE DEMPE Analysis

Functional analysis
Who performed the DEMPE functions?

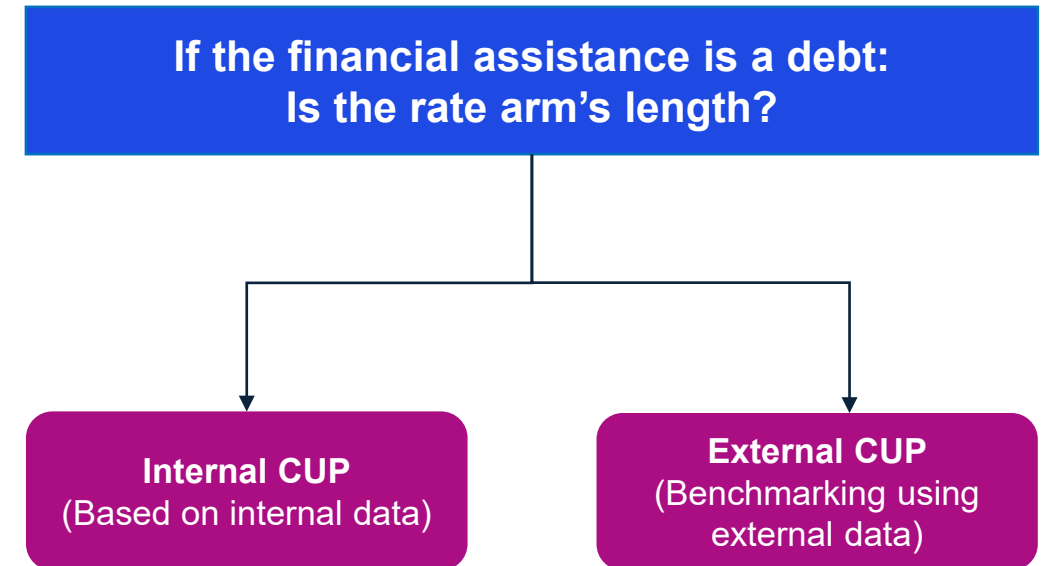
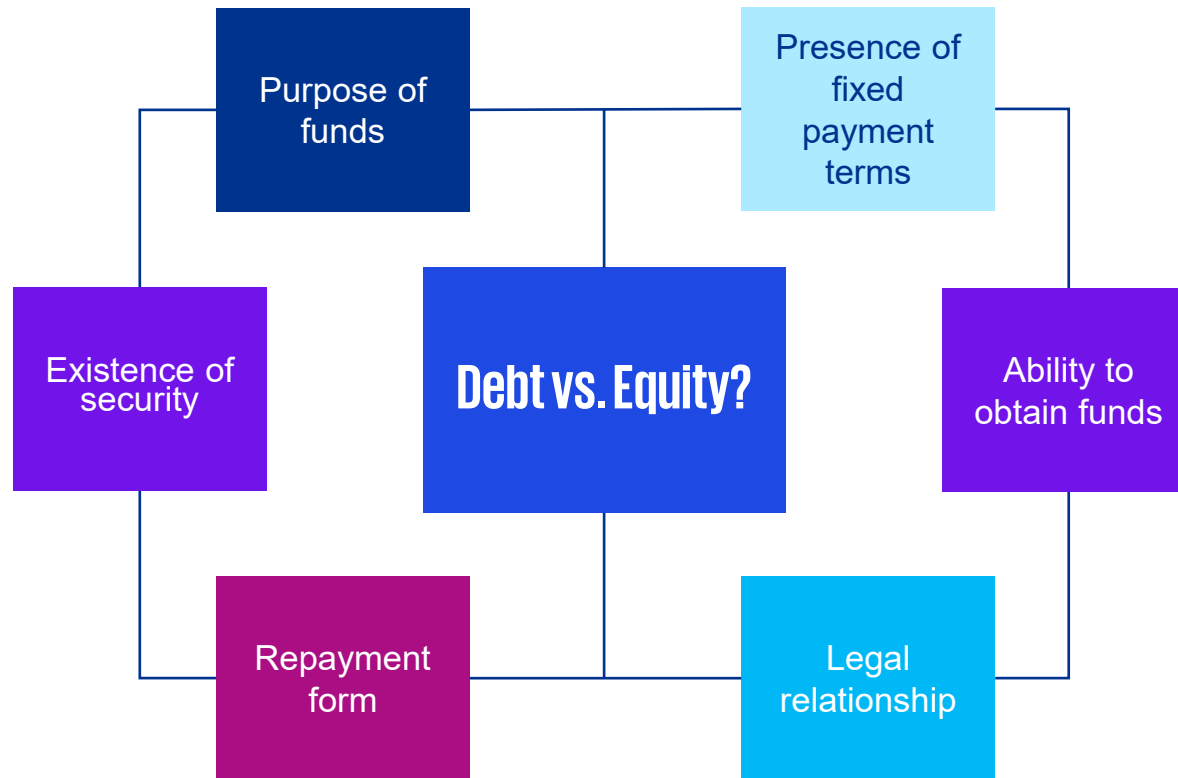


Benefit test
Did the taxpayer receive economic benefits?



Arm's length test
Is the rate at arm's length?

TP Audit: Intragroup Financial Assistance



TP Audit: Selection of Comparables and Benchmarking Results



- Uncontrolled transaction is lesser degree of comparability
- Comparability defect in the comparability analysis



Adjust the price of RPTs to median or any point above median

01



Quality of comparables

Differences in business activities and lack of publicly available information

Comparable companies that are loss making

02



Financial performance

03



Location

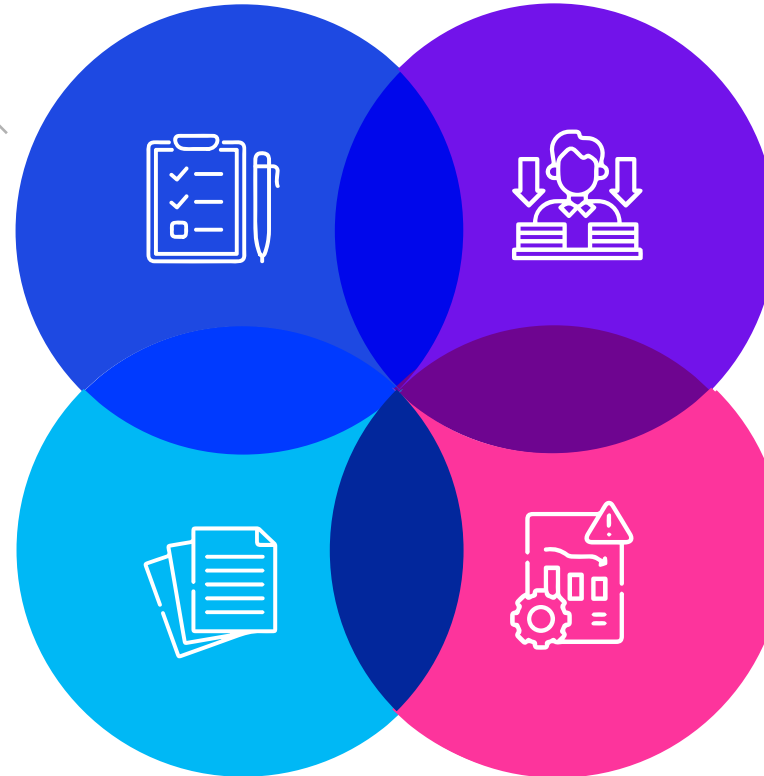
Comparable companies from other countries or region

Key Takeaway



Key takeaways

Mark TP documentation on your priority list



Burden to prove the arm's length nature of RPTs

The TP documentation for YA 2023 will be extensive and voluminous

Maintain robust supporting documents to minimize TP audit risk



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