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PR No. 2/2016 – Venture Capital Tax Incentives

The Inland Revenue Board ["IRB"] has recently issued the Public Ruling ["PR"] No. 2/2016 – Venture Capital Tax Incentives to provide explanation on the tax incentives available in relation to the venture capital industry in Malaysia.

Salient points of the abovementioned PR include:-

- i. Venture Capital Industry in Malaysia
 - Venture capital is financial capital provided by individuals, companies or venture capital companies ["VCC"] to high potential and high risk growth start-up companies at early stage.
 - A VCC is a company incorporated under the Companies Act 1965 to obtain funds from investors (equity capital) or loan capital, which are invested in the venture company ["VC"] in the form of seed capital, start-up or early stage financing.
 - A venture capital management corporation ["VCMC"] manages on behalf of a VCC the investments in securities of a VC in different business strategies, i.e. seed capital, start-up or early stage financing.

Hyperlinks

- [Moore Stephens Malaysia](#)
- [Moore Stephens International](#)
- [Inland Revenue Board](#)

- [PR No. 2/2016](#)

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- A VC is a company incorporated under the Companies Act 1965, which is:-
 - resident in Malaysia for a basis year of assessment; and
 - involved in utilizing the seed capital financing, start-up financing or early stage financing for:-
 - products or activities promoted under the Promotion of Investments Act 1986 where a VC has been granted tax incentives such as pioneer status or investment tax allowance;
 - technology-based activities listed in Appendix A of the Venture Capital Tax Incentives Guidelines issued by the Securities Commission ["SC"] (*Note*);
 - products or activities which have been developed under the Industrial Research and Development Grant Scheme, granted by the Minister of Science, Technology and Innovation; or
 - products or activities which have been developed under the MSC Research and Development Grant Scheme granted by Multimedia Development Corporation.

- ii. Tax Exemption Incentive for a VCC Investing in a VC
 - A VCC is exempted from the payment of tax in respect of the statutory income:-
 - from all sources of income excluding interest income arising from savings or fixed deposits and profits from *syariah*-based deposits; and
 - for a period of 10 years of assessment or the life of the fund established for the purpose of investing in a VC whichever is the lesser ["the period of exemption"].
 - To qualify for the exemption above, the VCC shall for each year of assessment for the period of exemption, obtain a certification from the SC confirming that:-
 - the VCC has invested at least 70% of its invested funds in a VC or where the investment is in the form of seed capital at least 50% of its invested funds;
 - the VCC has not invested in a VC which is its related company at the point of the first investment; and
 - the VCC has provided an early stage financing to a VC which is involved in activities which are not listed as technology-based business activities, from seed capital or start-up stage, where such early stage financing is provided as:-
 - additional capital expenditure or additional working capital to increase production capacity, marketing or product development; or
 - an interim financing for the purpose of being listed on the official list of a stock exchange.
 - Loss from disposal of shares
 - Where a VCC incurs a loss from the disposal of shares in a VC in the basis period for any year of assessment within the exempt period, such loss shall be carried forward to the post-exempt period.

Hyperlinks

iii. Tax Deduction Incentive for an Individual or a Company Investing in a VC

- An individual or a company, including a VCC would be entitled to claim a deduction in ascertaining the adjusted income for a basis period for a year of assessment of an amount equivalent to the value of the investment in shares (cost of investment) in a VC if the individual or company, including a VCC:-
 - is a resident in Malaysia;
 - has a business source; and
 - invested in a VC at start-up, seed capital and early stage financing for products and activities as mentioned in item (i) above.
- The investment made shall be deemed to be incurred on the date the investment is disposed of as certified by the SC. Therefore, the tax deduction is given at the time the investment is disposed of and not at the time the investment is made.
- To qualify for the deduction, the company or individual shall obtain certification from the SC confirming that:-
 - the investment was in the form of the holding of shares which at the time of acquisition are not listed for quotation in the official list of a stock exchange;
 - the investment, in relation to a company, was not made in a VC which is its related company at the point of first investment;
 - the investment was made for seed capital financing, start-up financing or early stage financing;
 - it had provided early stage financing to a VC which is involved in activities which are not listed as technology-based activities, from the seed capital or start-up stage, where such early stage financing was provided as:-
 - additional capital expenditure or additional working capital to increase production capacity, marketing or product development; or
 - interim financing for the purpose of being listed on the official list of a stock exchange;
 - the investment was made at least 2 years prior to the date of its disposal.

iv. Mutually Exclusive

- A VCC that has applied for tax exemption under item (ii) above and received certification from the SC is not entitled to apply for a tax deduction under item (iii) above for the whole period of exemption.

v. Tax Incentive for a VCMC

- A VCMC that is registered with the SC will be exempted from the payment of income tax in respect of the statutory income from the share of profits received by it from a VCC on any investment made by the VCC as stipulated in the agreement between the VCMC and VCC.

- The said VCC must have obtained certification from the SC for the tax incentive mentioned in item (ii) or item (iii) above.
- vi. Application for Certification of Investment for Tax Exemption and Tax Deduction in a VC
- Applications for annual certification for the purposes of tax exemption and tax deduction must be made to the SC by submitting the relevant forms and documentation.

Note: For further information on the Venture Capital Tax Incentives Industries, kindly refer to our Tax Flash – May 2014 issue.

Tax Exemption for Income from Investment Made Through Investment Account Platform

Pursuant to the Income Tax (Exemption) (No. 3) Order 2016, income tax exemption is granted in respect of profits from an investment received by a qualified person (i.e. an individual who is resident in Malaysia) within the period of 3 consecutive years of assessment starting from the first year of assessment the profits are received by the qualified person.

Among others, the conditions for tax exemption are:-

- the investment is made within the period of 3 years starting from 1st April 2016 to 31st March 2019;
- the investment is made through investment account platform established by a licensed Islamic bank or prescribed institution and operated by a person recognised by Bank Negara Malaysia in accordance to *Shariah* principles;
- the investment is to finance any venture or project in Malaysia in any industry or sector undertaken by a small and medium enterprise [“SME”] that fulfills the following criteria:-
 - a sole proprietor who is a Malaysian citizen and his business is registered under the Registration of Business Act 1956;
 - a limited liability partnership registered under the Limited Liability Partnership Act 2012 in which at least 51% of its capital contribution is contributed by Malaysian citizen;
 - a partnership registered under the Registration of Businesses Act 1956 in which at least 51% of its capital contribution is contributed by Malaysian citizen; or
 - a company incorporated under the Companies Act 1965 in which at least 51% of its issued ordinary share capital is directly owned by Malaysian citizen.
- the qualified person obtains a confirmation from the person who operates the investment account platform on the profits received from the venture or project in respect of which the investment is made and furnishes the confirmation to the Director General of Inland Revenue.

Hyperlinks

➤ [Tax Flash – May 2014](#)

➤ [Income Tax \(Exemption\) \(No. 3\) Order 2016](#)

The exemption given to a qualified person may be withdrawn if the SME undertaking the venture or project is no longer a SME or no longer fulfills the criteria specified above.

For the purpose of the above Order:-

“investment account platform” means a multibank platform which enables the channeling of funds by an individual through an investment account as defined under subsection 2(1) of the Islamic Financial Service Act 2013.

“SME” has the meaning assigned to it under Section 2 of the SME Corporation Malaysia Act 1995.

The above Order is deemed to have come into operation on 1st April 2016.

IRB’s Clarification on Reduction of Penalty for Voluntary Disclosure and Waiver of Tax Increase for Settlement of Tax Arrears

The IRB has earlier issued media release dated 10th February 2016 and Operational Guidelines No. 1/2016 on reduction of penalty for voluntary disclosure and waiver of tax increase for settlement of tax arrears. Following the briefing attended by the professional bodies, the IRB has issued a media release dated 14th April 2016 to provide clarifications on issues raised as follows:-

- i. Letter of Undertaking
 - The IRB has amended some wordings in the letter of undertaking to facilitate the taxpayers in signing the letter.
- ii. Reduction of Penalty for Transfer Pricing Audit Cases
 - The request for further reduction of penalty rates for transfer pricing audit cases will not be considered.
- iii. Audit Cases (Assessments Raised) Prior to 1st January 2016
 - The IRB has confirmed that the offer for reduction/waiver of penalty also applies to audit cases where assessments have been raised prior to 1st January 2016.

Note: For further information on the above, kindly refer to our Tax Flash – March 2016 issue.

Hyperlinks

➤ [IRB’s Media Release dated 14th April 2016](#)

➤ [Tax Flash – March 2016](#)

IRB's Clarification on Tax Treatment of Online Business

The IRB has recently issued a media release dated 23rd May 2016 to clarify on the tax treatment of online business.

The IRB clarifies that the income tax treatment of online business is the same as that for the offline/conventional business where income from a business shall be assessed to tax after taking into account the deduction for expenses allowable and reliefs. The chargeable income of an individual derived from the online business will be assessed to tax at the rates of 0% to 28% whereas for a company, the tax rates will be 19% and 24% (effective year of assessment 2016).

The IRB has earlier issued the Guidelines on Taxation of Electronic Commerce on 1st January 2013 which serves to provide some guidance on basic tax issues and tax treatment in respect of electronic commerce transactions. In addition, IRB has also published tax brochure on e-Commerce annually for public's reference in conducting their tax affairs.

Note: For further information on the Guideline on Taxation of Electronic Commerce, kindly refer to our Tax Flash – April 2013 issue.

Hyperlinks

➤ [IRB's Media Release dated 23rd May 2016](#)

➤ [Tax Flash – April 2013](#)

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