Deloitte Tax Challenge 2015

Team Category – Preliminary Stage

Suggested Answer

Part I – Group Tax Efficiency

Ref	Model Answer
i)	The following measures can be considered:

i) <u>Management Fee</u>
PASB should charge management fees to its subsidiaries at arm's length rate including the loss making entity which benefited from the services received.

<u>Loan Interest</u>
Where <u>PASB</u> obtain the loan, the interest cost is not tax deductible unless PASB enters into a back to back loan agreement with PCSB to recharge the finance cost

Where <u>PISB</u> obtain the loan, PISB is unable to claim a tax deduction on the interest cost as it has yet to commence its business activity

Where <u>PCSB</u> obtain the loan, PCSB is able to claim a tax deduction on the interest cost against its business income given that it is wholly and exclusively incurred in the course of producing its construction business income.

Conclusion : In view of the above, the loan can either by secured by PASB or PCSB.

ii) The following actions should be taken to enable both PCSB and PSSB qualify for group relief:

- to increase PASB's stake of ordinary shares in PCSB from 69.5% to 70%.
- to change PCSB's financial year end from 30 June to 31 December.
- to change PSSB's paid up share capital from RM2.4 million to more than RM2.5 million.

Part II – Tax Incentive

PISB may wish to consider applying for the BioNexus tax incentive. Tax incentives are available for companies involved in the biotechnology industry that have obtained approval of the BioNexus status from the Malaysia Biotechnology Corporations Sdn Bhd. The details of these incentives are as follows:

- An exemption from tax on 100% statutory income for (a) a period of ten consecutive years of assessment from the first year the company derived statutory income from the new business; or (b) for a period of five consecutive years of assessment from the first year the company derived statutory income from the existing business and expansion project; or (c) an exemption of 100% statutory income derived from a new business or an expansion project that is equivalent to an allowance of 100% qualifying expenditure incurred for a period of five years.

- Entitled to a concessionary tax rate of 20% on statutory income from qualifying activities for ten years upon the expiry of the tax exemption period.
- Tax exemption on dividends distributed by a BioNexus Status company.
- Exemption of import duty and sales tax on imported raw materials/components and machinery and equipment.
- Double deduction on expenditure incurred for Research & Development activity.
- Double deduction on expenditure incurred for the promotion of exports.
- With effect from 2 September 2006, qualifying buildings used solely for the purpose of biotechnology activities will be eligible for Industrial Building Allowance to be claimed over a period of 10 years.
- A company or an individual (that carry on business) investing in a BioNexus Status company is eligible for a tax deduction equivalent to the total investment made in seed capital or early stage financing.

Additional points to note regarding tax incentives received under the BioNexus status:-

- Depending on the choice of incentive selected (PS or ITA), there will be different criteria for eligibility and requirements that apply.
- Additionally, a company granted with the BioNexus status is also eligible for the BioNexus commercialization fund which provides for a facility of RM500,000 to RM3,000,000 per company.
- Generally, incentive granted for BioNexus status company is more superior that the normal tax incentive (i.e. tax exemption up to 70% of statutory income for 5 years or investment tax allowance of 60% to be set up against 70% of the company's statutory income for 5 years).

What distinguishes the BioNexus incentive from other incentive is:-

- the commercialisation fund which allows PISB to gain access to the RM500,000 to RM3,000,000 commercialisation fund.
- taking into account Dr Pym's intention of bringing in other shareholders, the tax deduction on total investments is an important consideration
- the background of the case provides that there will be heavy plant and machinery brought in to the refinery, so import duty exemption will be needed.
- IBA for buildings carrying out biotechnology activities.
- Since there will be future research and development carried out by PISB, double deduction may also be claimed on any research and development activity.

- Teams to indicate whether ITA or Pioneer Status is suitable. For this case, it will be ITA.

c) **Part III – Withholding Tax**

i) Based on Article 5(4)(c) of the double tax agreement between Malaysia and Australia, an enterprise shall deem to have a permanent establishment (PE) in Malaysia if it furnishes consultancy services in Malaysia through its employees, but only where those activities continue for a period or periods aggregating more than 3 months within any 12 month period.

Given the employees of NI has rendered the consultancy services in Malaysia for 4 months, NI is considered to have a PE in Malaysia.

ii) Below are the withholding tax (WT) applicability, rate and its reasons:

Description of Expenses	**Explanation**
• Local labor and material cost	Not subject to WHT as WHT is not applicable to goods
• Leasing of heavy plant & machinery	Subject to 10% WHT under Section 109B. Treaty rate – N/A
• Consultancy service • Training in Malaysia • Reimbursement of airfare	13% WT under Section 107A is applicable on these expenses due to NI has a PE in Malaysia.
• Supply of spare parts	No WT as it is only applicable on services rendered in Malaysia
• Royalty	10% WT under Section 109 is applicable. Malaysia-Singapore treaty rate – 8%
• Offshore services	No WT is the service is performed outside Malaysia