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EY Tax Alert (Special Edition)

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Enhanced Malaysia Transfer Pricing Guidelines 2024 and TP Tax Audit Framework 2024

Coverage of this alert

Malaysia TP Guidelines 2024

- Exemptions from preparing TPD
- Revised thresholds for full scope TPD
- Minimum scope TPD
- Additional considerations in TP analyses
- Low value-adding intragroup services (LVAIS)
- Business restructuring

Malaysia TP Tax Audit Framework 2024

- TP tax audit examination process
- TP penalty regime

Key highlights

- The Malaysia TP Guidelines 2024 aligns with the existing local TP regulations providing guidance and reinforcing the preparation of robust TP analyses.
- Expansion of exemption criteria in preparing TP documentation (TPD) for qualifying taxpayers.
- Thresholds distinguishing full scope and minimum scope TPDs are redefined.
- Introduction of simplified approach for low value-adding intragroup services (LVAIS).
- Emphasis on the economic value and shift in taxpayers' functional profile in business restructuring arrangements
- Introduction of a scaled TP penalty regime.

The TP landscape in Malaysia has experienced significant development in recent years as evidenced by the introduction of enhanced rules, regulatory measures and a revised penalty framework. Concurrently, there has been a notable intensification of enforcement activities concerning TP. These developments highlight an increased emphasis and scrutiny of TP practices and documentation requirements.

On 24 December 2024, the Inland Revenue Board of Malaysia (IRBM) released a new Malaysia Transfer Pricing Guidelines and a new Transfer Pricing Tax Audit Framework.

The new releases by the IRBM serve to provide clarity and educate taxpayers on TP encouraging compliance with tax laws and regulations.



Malaysia TP Guidelines 2024

Introduction

The Guidelines, which come into effect year of assessment 2023, provide further guidance on the IRBM's expectations of a comprehensive TPD. These Guidelines have been revised to ensure consistency with the existing local TP regulations and amendments made to the Transfer Pricing Rules in May 2023 (TP Rules 2023), which primarily include the following:

- a) Enhanced TPD requirements
- b) Imposition of statutory deadlines for the preparation of contemporaneous TPD (CTPD)
- c) Definition of the arm's length range
- d) Revised penalty regime

For further details on these updates, please refer to the appendix.

Key highlights include:

a) Exemption from preparing TPD

The exemption criteria from the requirement to prepare CTPD in the Guidelines have been expanded compared to those included in the preceding Guidelines. The exemptions now encompass:

- a. Individuals not carrying on a business
- b. Individuals carrying on a business (including partnerships) who only engage in domestic controlled transactions
- c. Person who entered into controlled transactions with a total amounting to not more than RM1 million
- d. Person who entered solely into domestic controlled transactions with another person where both parties:
 - i. Do not enjoy tax incentives
 - ii. Taxed at the same headline tax rate
 - iii. Do not suffer losses for two consecutive years prior to the controlled transactions

Notwithstanding the above, exempted persons are still required to comply with the arm's length principle for all controlled transactions entered into and retain all relevant documents related to the controlled transactions, including documentation to substantiate the determination of the arm's length price.



b) Revised thresholds for full scope TPD

The criteria for a person to prepare full scope TPD have been revised in comparison to the preceding Guidelines. A table outlining the relevant criteria stipulated in the previous and current Guidelines is provided below:

2012 Guidelines	2024 Guidelines
<ul style="list-style-type: none">Gross income exceeding RM25 million and total amount of related party transactions exceeding RM15 million.Provides financial assistance exceeding RM50 million.	<ul style="list-style-type: none">Gross business income of more than RM30 million and cross-border controlled transactions totaling RM10 million annually.Receives or provides controlled financial assistance of more than RM50 million annually.

c) Minimum scope TPD

Taxpayers whose controlled transactions do not fulfill the specified criteria outlined in the Guidelines are eligible to prepare a minimum scope TPD with reduced requirements.

The information required for a minimum scope TPD is limited to the following areas:

- Worldwide group structure
- Organizational structure
- Controlled transaction
- Pricing policy

Furthermore, taxpayers who prepare minimum scope TPD are only required to include the above information for their **key controlled transactions**. For the purposes of the minimum scope TPD, key controlled transactions are defined as:

- Controlled transactions that are related to the taxpayer's principal activity, such as the acquisition or supply of raw materials for manufacturing activity.
- Controlled transactions other than those in (i), that constitute 20% or more of the operating revenue in each year of assessment.

Nevertheless, taxpayers who prepare a minimum scope TPD are still required to list all controlled transactions entered into, regardless of whether the transaction is a key controlled transaction or not.

Taxpayers who prepare minimum scope TPD are allowed to apply any method allowed by the Director General of Inland Revenue (DGIR) that is able to demonstrate compliance with the arm's length price, as long as it results in a better approximation of the arm's length price. Although a comparability analysis is not a mandatory component of a minimum scope TPD, the IRBM reserves the right to request such an analysis from taxpayers. Such request will not compromise the contemporaneous nature of the minimum scope TPD.



d) Additional considerations in TP analyses

The Guidelines provide further guidance regarding specific elements of TP analyses. Key areas include:

Pass-through costs

Pass-through costs refer to expenses incurred by an entity on behalf of a group member or an independent customer. In this capacity, the entity does not perform any value-added functions nor assumes any risks.

The Guidelines outline several criteria that must be satisfied to categorize expenses as pass-through costs. These criteria include, among others, a detailed functional analysis and supporting evidence which substantiate the entity's role as an intermediary and demonstrate that the relevant liabilities and risks in relation to the pass-through costs are assumed by the service recipients.

Furthermore, the Guidelines allow for adjustments to pass-through costs in an entity's profit margin calculation during benchmarking analysis, provided that reliable adjustments can be made to exclude such costs from the comparables, or if similar pass-through costs have been excluded from the operating margins of the comparables.

Selection criteria for potential comparables

The Guidelines require the selection of comparables that align with the economically relevant characteristics as prescribed by the TP Rules 2023. To facilitate the selection of high quality comparables, the Guidelines provide a list of qualitative and quantitative criteria to be considered.

Qualitative criteria

- Functional comparability
- Product portfolio
- Business strategies
- Geographical markets
- Business activities

Quantitative criteria

- Size criteria, such as sales (not less than 10% of tested party's revenue), assets or number of employees
- Intangible-related criteria such as ratio of intangible assets to net assets, or ratio of research and development (R&D) expenditure to sales
- Criteria related to export sales
- Criteria related to inventories
- Additional criteria to exclude third-parties in special circumstances, such as start-up companies, companies in bankruptcy, etc.

The choice and application of selection criteria as above is dependent on the facts and circumstances of each case. The above list is neither limitative nor prescriptive.



e) Low value-adding intragroup services (LVAS)

In accordance with the streamlined approach outlined in the guidelines provided by the Organisation for Economic Co-operation and Development (OECD), the Guidelines have now incorporated a simplified approach for LVAS.

LVAS are defined as services rendered by one or more multinational enterprise (MNE) group members for the benefit of other group members, which:

- a. Are of a supportive nature
- b. Are not part of the core business of the MNE Group
- c. Do not require the use or creation of unique and valuable intangibles
- d. Do not entail the service provider assuming or controlling substantial risks, nor give rise to the creation of significant risks for the service provider

The simplified approach provides a streamlined mechanism in determining the arm's length charge for LVAS, as detailed below:


- a. The service provider shall apply a profit mark-up to all costs in the pool, excluding any pass-through costs.
- b. The same mark-up shall be applied to all LVAS, regardless of the category of services.
- c. The mark-up shall be equal to 5% of all relevant costs, which may include direct, indirect and operating expenses relating to the LVAS.
- d. The mark-up under the simplified approach does not need to be justified by a benchmarking study. However, taxpayers are required to maintain complete documentation pertaining to this simplified approach.

This simplified approach is applicable to Malaysian service providers. For Malaysian service recipients, only payments made to LVAS providers that have adopted the OECD's simplified approach within their respective jurisdictions will be considered compliant with the arm's length principle. Where these criteria are not satisfied, taxpayers are required to perform comparability analysis to demonstrate that the payments made are compliant with the arm's length principle.

f) Business restructuring

The IRBM has expounded its viewpoint on the application of the arm's length principle for business restructuring exercises performed by MNEs. Emphasis is placed on the following (but not limited to):

- a. Alignment of the shift in functional profile and characterization of the taxpayer to its profitability levels
- b. Assessment of the options realistically available when a taxpayer considers undertaking a business restructuring exercise

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- c. Substantiating the economic nature of the arrangements pre- and post-restructuring of the parties involved in the business restructuring exercise

TP Tax Audit Framework 2024 (TPTAF)

Introduction

Effective	: 24 December 2024
Reference (but not limited to)	: <ul style="list-style-type: none">▪ Section 113B of the Income Tax Act (ITA) 1967▪ Section 132 of the ITA▪ Section 139 of the ITA▪ Section 140A of the ITA▪ TP Rules 2012 [P.U.(A)132/2012]▪ TP Rules 2023 [P.U.(A)165/2023]▪ Malaysia TP Guidelines 2024

The TPTAF 2024 (which supersedes the former TP Audit Framework 2019) administers the adherence and compliance of controlled transactions with the arm's length principle. The responsibilities and obligations of the IRBM, the taxpayer and the tax agents are spelled out ensuring that TP audit examinations are performed effectively and efficiently. The TPTAF 2024 also provides clarity on some key areas, for example, the TP audit examination procedures, the TP penalty regime and appeal processes.

Key highlights include:

a) TP tax audit examination process

- A TP tax audit examination covers six years of assessment and may be extended to seven years of assessment depending on the audit findings.
- The IRBM has broadened its basis and parameters in the selection of taxpayers for TP tax audit examinations, which include:
 - Risk assessment of the taxpayer's controlled transactions
 - Business restructuring activities of the taxpayer and its group
 - Information received from third-party sources and exchange of information from foreign tax authorities



- The IRBM clarifies that the TP tax audit examination case needs to be completed within 450 calendar days from the audit commencement date. Audit commencement date is established as below:
 - Formal notification by the IRBM in determining the commencement date; or
 - Date of the physical field audit visit; or
 - Any other date pre-agreed between the IRBM and the taxpayer.

However, the IRBM may notify if an extension of time is required to conclude the audit examination.

- In cases involving offsetting adjustments for the taxpayer's local counterparty, a separate application must be made by the relevant counterparty and the IRBM shall perform a separate audit examination on the counterparty.

b) TP penalty regime

In the event of a TP adjustment arising from an understatement or omission of income, a TP surcharge may be imposed in accordance with subsection 140A(3C) of the ITA as detailed below.

Category	Description
TP audit examination	<ul style="list-style-type: none"> ▪ TP surcharge rate of up to 5% on TP adjustment ▪ The TP surcharge may still be imposed even if no assessment/additional assessment is raised
Voluntary disclosure (VD)	<ul style="list-style-type: none"> ▪ TP surcharge rate ranging from 0% to 4% on TP adjustment, subject to fulfilling the IRBM's VD criteria ▪ Taxpayer may apply for a VD post the submission deadline of the income tax return form but before the audit examination commences

In accordance with Section 113B of the ITA, the following monetary penalties or imprisonment, or both may be imposed where:

- Failure to submit TPD within 14 days from the date of the IRBM's written notice.
- Non-compliance with the TPD requirements under P.U.(A) 165/2023 and the Malaysia TP Guidelines 2024.



Period of delay (post the initial 14 days' timeframe)	Penalty (applicable for each year of assessment under audit)
Up to 7 days	Monetary penalty of RM20,000
More than 7 days up to 14 days	Monetary penalty of RM40,000
More than 14 days up to 21 days	Monetary penalty of RM60,000
More than 21 days up to 28 days	Monetary penalty of RM80,000
More than 28 days	Monetary penalty of RM100,000
No response from the taxpayer post 14 days from the IRBM's written notice	Prosecution may be instituted (not more than 6 months imprisonment)

Note:

- Penalty concession may apply for taxpayers who has an accounting period beginning before 29 May 2023 [Gazette order date of P.U.(A) 165/2023]
- The TP penalties above will be imposed at the final stage of the audit process.



Appendix

Alignment between Guidelines and existing local TP regulations

a) Enhanced TPD requirements

In alignment with the information requirements mandated by the TP Rules 2023, the Guidelines provides that a CTPD should contain the following records and documents:

- a. Information of the MNE Group as specified under Schedule 1 of the TP Rules 2023. Where an MNE Group has prepared a master file that includes all information required, such a file can be submitted as a replacement for Schedule 1.
- b. Information of the person's business as required under Schedule 2 of the Rules.
- c. Information and documentation as specified under Schedule 3 of the Rules regarding cost contribution arrangements (CCA) (if applicable).
- d. Information and documents related to specific transactions.
- e. Index to the documents.
- f. The completion date of the CTPD.
- g. Any documents that serve as a foundation, provide support or were referred to during the development of the TP analysis, including documentation for comparable searches.
- h. Any other relevant information, data, or documents that can be used to determine the arm's length price of the controlled transactions, including the effects of any material changes to the business conditions during the basis period. In this context, material changes refer to significant changes that would have an impact on the tested party's functional analysis or TP analysis. Material changes include changes to the operational and economic conditions that will significantly affect the controlled transactions under consideration.



b) Imposition of statutory deadlines for the preparation of CTPD

In accordance with the TP Rules 2023, taxpayers are required to prepare CTPD before the **due date of furnishing a return in the basis period for a year of assessment in which a controlled transaction is entered into**. The CTPD should be completed and dated prior to the submission of tax return for a relevant year of assessment.

However, it is not necessary for taxpayers to submit the CTPD when filing the tax return forms. Instead, the documentation should be made available and **furnished within 14 days upon request by the IRBM**.

c) Definition of the arm's length range

The provisions relating to the arm's length range and arm's length price have been refined to align with the TP Rules 2023. Specifically, the arm's length range is now defined as "a range of figures or a single figure falling between the **value of 37.5 percentile to 62.5 percentile of the data set** and acceptable by the DGIR...", with the median defined as the **mid-point of the arm's length range**.

However, the TP Rules 2023 permit the DGIR to make adjustments to the median or any other point above the median within the arm's length range if it is believed that:

- The comparables have a lesser degree of comparability; or
- There are any comparability defects that cannot be identified, quantified or adjusted accordingly.

Furthermore, the Guidelines also specify that if a price (or interest rate) of a controlled transaction is asserted to be at arm's length based on comparables that do not share similar economically relevant characteristics to the tested party, the DGIR is authorized to adjust the transaction to reflect an arm's length price or interest rate for that transaction.



d) Revised penalty regime

The penalty provisions outlined in the Guidelines have been updated to incorporate the revised penalty framework which were introduced subsequent to the release of the preceding Guidelines.

Below is a comparative overview of the penalty regime as specified in the previous and current Guidelines.

2012 Guidelines	2024 Guidelines
<ul style="list-style-type: none"> ▪ DGIR empowered to make adjustments if income reported is not at arm's length (Subsection 140A(3) of the ITA) ▪ Inconsistency in facts presented between TPD and actual conduct could result in fines between RM1,000 and RM10,000 and a special penalty of double the undercharged tax (Section 113(1)(b) of the ITA) ▪ Provision of incorrect information affecting the chargeability of tax could result in penalties equal to undercharged tax, if no prosecution was made (Section 113(2)(b) of the ITA) 	<ul style="list-style-type: none"> ▪ DGIR can make adjustments if income reported is not at arm's length, and disregard or recharacterize transactions with differing economic substance or structures not adopted by independent parties (Subsections 140A(3), (3A) and (3B) of the ITA) ▪ Surcharge up to 5% of TP adjustment imposed regardless of tax payable (Section 140A(3C) of the ITA) ▪ Failure to furnish CTPD within 14 days of IRBM notice can result in fines between RM20,000 and RM100,000, imprisonment up to six months, or both (Section 113B(1) of the ITA) ▪ Penalties for not furnishing CTPD without prosecution range from RM20,000 to RM100,000 per year of assessment (Section 113B(4) of the ITA) ▪ Insufficient record keeping for seven years, including CTPD, may lead to fines between RM300 and RM10,000, imprisonment up to one year, or both (Section 119A of the ITA).

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