Chapter 5

Tax Incentives for Companies

Introduction

There are incentives available in Malaysia for investments in promoted products and activities in the manufacturing, agriculture, hotel and tourism industry, research and development (R&D) and training activities and specific business activities as promoted by the Malaysian government.

These incentives are contained in the Promotion of Investments Act 1986 and the Income Tax Act 1967. Generally, the incentives provide for total or partial relief from Income Tax.

A list of expenses eligible for Double Deduction is set out separately for easy reference.

Promotion of Investments Act, 1986

The main incentives covered under this Act are as follows:-

- Pioneer Status;
- Investment Tax Allowance;
- Infrastructure Allowance.

Pioneer Status

Pioneer Status is a form of tax incentive which provides for full or partial exemption from payment of Income Tax.

The profits that are exempted from tax are transferred to an exempt income account for the purpose of franking tax-exempt dividends. Redistribution by shareholder companies of such exempt dividends are also exempt from tax.

Investment Tax Allowance

Eligible projects with large capital investment and long gestation periods can consider Investment Tax Allowance as an alternative to the Pioneer Status incentive. Investment Tax Allowance is a tax incentive based on the qualifying capital expenditure incurred. Investment Tax Allowance may be applied for by any company participating or intending to participate in a promoted activity or in the production of a promoted product. Any unutilised allowance can be carried forward until it is fully utilised.

The amount of Investment Tax Allowance utilised is transferred to an exempt income account for the purpose of franking tax exempt dividends. Redistributions by shareholder companies of such exempt dividends are also exempt from tax.

Pioneer Status and Investment Tax Allowance are mutually exclusive.

A company granted either Pioneer Status or Investment Tax Allowance can enjoy partial or full exemption from payment of Income Tax depending on the type of promoted products or activities and location as follows:

i. Promoted product/activity	*Pioneer Status* 70% of the statutory income will be exempted from Income Tax for 5 years from the date of the commencement of the pioneer period as determined by the Ministry of International Trade and Industry (MITI). The remaining 30% of the statutory income will be taxed at the prevailing Income Tax rate of 28% resulting in an effective tax rate of 8.4% *Investment Tax Allowance* A company with Investment Tax Allowance will be granted an allowance of 60% in respect of the qualifying capital expenditure incurred within 5 years from the date on which the first capital expenditure is incurred. The allowance can be used to set off up to 70% of the statutory income

	in the year of assessment. The remaining 30% of the statutory income will be taxed at the prevailing Income Tax rate of 28% resulting in an effective tax rate of 8.4%.
ii. Promoted product/activity in promoted areas. Designated promoted areas are Eastern Corridor of Peninsular Malaysia, Sabah and Sarawak. The Eastern Corridor of Peninsular Malaysia covers Kelantan, Terengganu, Pahang and the district of Mersing in Johor.	*Pioneer Status* 85% of the statutory income will be exempted from Income Tax for 5 years from the date of the commencement of the pioneer period. The balance of 15% of the statutory income will be taxed at the prevailing Income Tax rate of 28%. *Investment Tax Allowance* Companies located in the designated promoted areas will be granted an allowance of 80% in respect of qualifying capital expenditure incurred from the date on which the first capital expenditure is incurred. The tax allowance can be used to set off up to 85% of the statutory income in the year of assessment. The balance 15% of the statutory income will be taxed at the prevailing Income Tax rate of 28%.
iii. Promoted product/activity for high technology companies. Additional criteria - at least 1% of gross sales be spent on local R&D. - at least 7% of total workforce are science and technical graduates	*Pioneer Status* 100% exemption from Income Tax for 5 years. *Investment Tax Allowance* An Investment Tax Allowance of 60% will be granted in respect of qualifying capital expenditure incurred within 5 years from the date on which the first capital expenditure is incurred. The allowance can be utilised to set off against 100% of the statutory income in the year of assessment
iv. Promoted product/activity of national and strategic importance including Multimedia Super Corridor (MSC) status companies and product/activity in the approved linkage programme which achieves world class status.	*Pioneer Status* 100% exemption from Income Tax for 5 years and is eligible for extension of another five years.

Companies granted MSC status for qualifying MSC activities by the Multimedia Development Corporation are eligible for this incentive. Strategic projects are those with heavy capital expenditure and high technology which can generate extensive linkages to other industries.	*Investment Tax Allowance* Investment Tax Allowance of 100% in respect of qualifying capital expenditure incurred within 5 years from the date of which the first capital expenditure is incurred. The allowance can be utilised to set off against 100% of the statutory income in the year of assessment.
v. Research and Development activities	
a) Contract R&D company (A company which undertakes R&D activities for third parties)	*Pioneer Status* 100% exemption of Income Tax for 5 years. *Investment Tax Allowance* Investment Tax Allowance of 100% in respect of qualifying capital expenditure incurred within 10 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off against 70% of the statutory income. The balance of 30% of the statutory income will be taxed at the prevailing Income Tax rate.
b) R&D Company (A company which undertakes R&D activities for its related company or for any other company)	*Pioneer Status* Not applicable. *Investment Tax Allowance* An Investment Tax Allowance of 100% in respect of capital expenditure incurred within 10 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off against 70% of the statutory income. The balance of 30% of the statutory income will be taxed at the prevailing Income Tax rate.
c) In-house R&D activities (R&D activities undertaken within the company for the purpose of its own business)	*Pioneer Status* Not applicable. *Investment Tax Allowance* An allowance of 50% in respect of capital expenditure incurred within 10 years from the date of the first incurrence of capital expenditure.

	The allowance can be utilised to set off against 70% of the statutory income. The balance of 30% of the statutory income will be taxed at the prevailing Income Tax rate.
vi. Technical or Vocational Training Activities (For new company/training institute undertaking technical or vocational training activities as well as for existing companies/training institutes incurring new investment to upgrade their training equipment or to expand their training capacities)	*Investment Tax Allowance* An allowance of 100% in respect of qualifying capital expenditure incurred within 10 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off up to 70% of the statutory income. The balance of 30% will be taxed at the prevailing Income Tax rate.
vii. Environmental Protection	
a) Forest Plantation Projects	*Pioneer Status* 100% exemption of Income Tax for 10 years. *Investment Tax Allowance* Investment Tax Allowance of 100% in respect of qualifying capital expenditure incurred within 5 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off up to 100% of the statutory income.
b) Storage, treatment and disposal of toxic and hazardous wastes	*Pioneer Status* 70% exemption of Income Tax for 5 years. *Investment Tax Allowance* Investment Tax Allowance of 60% in respect of qualifying capital expenditure incurred within 5 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off up to 70% of the statutory income. The balance of 30% will be taxed at the prevailing Income Tax rate.

c) Energy Conservation (This incentive applies to applications received by 31 December 2002 and on the condition that the project is implemented within one year from the approval date.)	*Pioneer Status* 70% exemption of Income Tax for 5 years. *Investment Tax Allowance* Investment Tax Allowance of 60% in respect of qualifying capital expenditure incurred within 5 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off against 70% of the statutory income. The balance of 30% of the statutory income will be taxed at the prevailing Income Tax rate.
d) Waste Recycling Activities	*Pioneer Status* 70% exemption of Income Tax for 5 years. *Investment Tax Allowance* Investment Tax Allowance of 60% in respect of qualifying capital expenditure incurred within 5 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off against 70% of the statutory income. The balance of 30% of the statutory income will be taxed at the prevailing Income Tax rate.
e) Utilising Biomass As a New Source of Energy (This incentive applies to applications received by 31 December 2002 and on the condition that the project is implemented within one year from the approval date.)	*Pioneer Status* 70% exemption of Income Tax for 5 years. *Investment Tax Allowance* Investment Tax Allowance of 60% in respect of qualifying capital expenditure incurred within 5 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off against 70% of the statutory income. The balance of 30% of the statutory income will be taxed at the prevailing Income Tax rate.
viii) Cold Chain Facilities and Services for Food Products	*Pioneer Status* 70% exemption of Income Tax for 5 years. *Investment Tax Allowance* Investment Tax Allowance of 60% in respect of qualifying capital expenditure incurred within 5 years from the date of the first incurrence of capital expenditure.

	The allowance can be utilised to set off against 70% of the statutory income. The balance of 30% of the statutory income will be taxed at the prevailing Income Tax rate.
ix) Downstream Resource Based Industries such as rubber, oil palm and wood based industries which have export potential and which reinvest for expansion purposes.	*Pioneer Status* 70% exemption of Income Tax for 5 years. *Investment Tax Allowance* Investment Tax Allowance of 60% in respect of qualifying capital expenditure incurred within 5 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off against 70% of the statutory income. The balance of 30% of the statutory income will be taxed at the prevailing Income Tax rate.
x) Manufacture of Specific Machinery and Equipment (machine tools, plastic injection machines, material handling equipment, robotics and factory automation equipment, and parts and components of the abovementioned machinery and equipment.)	*Pioneer Status* 100% exemption of Income Tax for 10 years. *Investment Tax Allowance* Investment Tax Allowance of 100% in respect of qualifying capital expenditure incurred within 5 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set off against 100% of the statutory income.
xi) Manufacturing Related Services - Integrated logistic services - Integrated market support services - Integrated central utility facilities	*Pioneer Status* 70% exemption of Income Tax for 5 years. (85% exemption of Income Tax for 5 years for projects in the Eastern Corridor of Peninsular Malaysia, Sabah and Sarawak.) *Investment Tax Allowance* Not Applicable

Infrastructure Allowance

A company resident in Malaysia which has incurred capital expenditure on infrastructure in respect of a business or businesses in operation in a promoted area qualifies for the incentive.

The allowance given is 100% on the qualifying capital expenditure incurred and it will be offset subject to a maximum of 85% of the statutory income for each year of assessment. Any unutilised allowance can be carried forward indefinitely until fully utilised. The amount of Infrastructure Allowance utilised is transferred to an exempt income account for the purpose of franking tax exempt dividends. Redistributions by shareholder companies of such exempt dividends are also exempt from tax.

The expenditure which qualifies for the allowance is the capital expenditure incurred on any construction, reconstruction, extension or improvement of any permanent structure including a bridge, jetty, port or road in respect of a business or businesses in operation in a promoted area, but excludes capital expenditure which qualifies for Investment Tax Allowance, Industrial Adjustment Allowance, Schedule 3 Allowance or Reinvestment Allowance and capital expenditure incurred on waste disposal or for the use of management, administrative or clerical staff.

Designated promoted areas are Sabah, Sarawak and the designated Eastern Corridor of Peninsular Malaysia. The Eastern Corridor covers Kelantan, Terengganu, Pahang and the district of Mersing in Johor.

This incentive applies to all applications received by 31 December 2005.

Income Tax Act, 1967

The main incentives covered under this Act are as follows:-

- Reinvestment Allowance;
- Allowance for Increased Exports of Manufactured Products or Agricultural Produce;
- Incentives for Food Production;
- Incentives for Tourism Industry;
- Malaysian International Trading Company;
- Incentives for Research and Development;
- Incentives for Approved Service Projects;
- Incentive for Technical or Vocational Training Activities;
- Incentives for Inward Reinsurance and Offshore Insurance;
- Shipping Incentives;
- Operational Headquarters Company;
- Accelerated Capital Allowance;
- Qualifying Pre-Operational Business Expenditure;
- Tax Exemption on Foreign Income;

- Taxation of Profit of an Offshore Company in Labuan.

These incentives are considered further below as applicable an industry basis of classification.

Incentives for Specific Industries or Promoted Activities
Manufacturing and Agricultural Sectors

Reinvestment Allowance

Under the Income Tax Act, 1967, a resident company which incurs capital expenditure on a factory, plant and machinery used for a qualifying project in Malaysia can claim a Reinvestment Allowance equivalent to 60% of that expenditure.

A qualifying project refers to a project undertaken by a company in expanding, modernising or automating its existing business in respect of manufacturing or processing or in diversifying its existing business or a project undertaken by a company which is participating in an industrial adjustment programme in expanding its existing business or modernising its production techniques or processes. With effect from Year of Assessment 1997, the scope of Reinvestment Allowance has been extended to agriculture companies including agro-based co-operative society and associations which undertake expansion, modernisation or diversification in selected cultivation and / or agriculture projects.

To qualify for the allowance, the company must be in operations for at least 12 months. Companies which are currently enjoying certain incentives (e.g. Pioneer Status or Investment Tax Allowance) will not qualify for Reinvestment Allowance.

Reinvestment Allowance is abated against statutory income and the utilisation of allowance is restricted to 70% of statutory income. Any unabsorbed allowance is allowed to be carried forward indefinitely. Companies that reinvest in Sabah, Sarawak and designated areas of the Eastern Corridor of Peninsular Malaysia as well as companies that achieve the level of productivity as determined by the Minister of Finance will be allowed to utilise the allowance fully against statutory income.

The Reinvestment Allowance given on a particular asset will be withdrawn if the asset is disposed of within 2 years from the date of acquisition of the asset.

Effective from Year of Assessment 1998, the allowance is granted for a period of 5 consecutive years of assessment beginning from the year of assessment in which basis period the capital expenditure was first incurred. However, as announced in the 2002 Budget in October 2001, the Reinvestment Allowance period has been extended from 5 to 15 consecutive years commencing from the year the first reinvestment is made.

The amount of Reinvestment Allowance utilised against statutory income shall be credited to a tax exempt account from which tax exempt dividends can be paid to shareholders. Redistributions of such exempt dividends by shareholder companies are also tax exempt.

Allowance for Increased Exports of Manufactured Products or Agricultural Produce

A manufacturing company or a company in the agriculture sector, resident in Malaysia, which exports manufactured products or agricultural produce is eligible to claim an Allowance for Increased Exports pursuant to the Income Tax (Allowance for Increased Exports) Rules 1999.
The allowance is computed as follows:-

- 10% of the value of increased exports of manufactured products by the company where the products exported attained at least 30% of value added;

- 15% of the value of increased exports of manufactured products by the company where the products exported attained at least 50% of value added; and

- 10% of the value of increased exports of specific agricultural produce by the company.

The utilisation of the allowance is restricted to 70% of the statutory income for a year of assessment. Any unabsorbed allowance can be carried forward indefinitely.

The income exempted from tax is credited to a tax exempt account from which tax exempt dividends can be franked to the shareholders. Redistributions of such exempt dividends by shareholder companies are also tax exempt.

This incentive however does not apply to companies which are currently enjoying certain incentives under the Promotion of Investment Act 1986 (e.g. Pioneer Status or Investment Tax Allowance) or Reinvestment Allowance. Further, companies exporting certain excluded products will also not qualify for the incentive.

Incentives for Food Production

For New Project

A company which invests in a subsidiary company engaged in food production together with the subsidiary company qualifies for either one of the following two incentive packages:

Incentive Package A:

A company making investments in the subsidiary company, which is undertaking an approved food project, shall be entitled to a tax deduction equivalent to the amount of investments made (which is used for the sole purpose of financing the approved food production project) in the basis period for a year of assessment.

The subsidiary company undertaking food production will be given income tax exemption of 100% on its statutory income for 10 years commencing from the first year the company enjoys profit in which:

- losses incurred before the exemption period are allowed to be brought forward after the exemption period of 10 years;
- losses incurred during the exemption period are also allowed to be brought forward after the exemption period of 10 years; and
- dividends paid from the exempt income will be exempted in the hand of the shareholders.

OR

Incentive Package B:
Under this package, group relief is available for companies engaged in an approved food production project. The company which invests in the subsidiary company engaged in food production will be given group relief for the losses incurred by the subsidiary company before it records any profit.

The subsidiary company undertaking food production will be given income tax exemption of 100% on its statutory income for 10 years commencing from the first year the company makes profit. However,

- losses incurred during the exemption period are allowed to be carried forward for utilisation after the exemption period of 10 years; and
- dividends paid from the exempt income will be exempted in the hands of the shareholders.

Both the above incentive packages are subject to the following conditions

- the investing company should own 100% of the subsidiary company that undertakes food production;
- the eligible food products are as approved by the Ministry of Finance. Presently, the approved food products are kenaf, vegetables, fruits, herbs, spices, aquaculture and rearing of cattle, goat and sheep; and
- the food production project should commence within a period of one year from the date the incentive is approved.

Application for these incentives should be submitted to the Ministry of Agriculture before 31 December 2003 for the approval of the Minister of Finance.

Tourism Sector

Pioneer Status or Investment Tax Allowance
Hotel business and tourism related activities are promoted activities under the Promotion of Investments Act, 1986 and are eligible for Pioneer Status or Investment Tax Allowance as in the following:

- Establishment of medium and low cost hotels (up to a three-star hotel);
- Expansion/modernisation of existing hotels;
- Establishment of tourist projects;
- Expansion/modernisation of tourist projects;
- Establishment of recreational campus;

- Establishment of convention centres;

Industrial Building Allowance (IBA)

Hotels granted Pioneer Status or Investment Tax Allowance are eligible for IBA initial allowance of 10% and annual allowance of 2% on the capital expenditure on the construction or purchase of a building used in the hotel business. Effective from Year of Assessment 2002, the annual allowance will be increased from 2% to 3%. For hotels to be eligible to claim the IBA, the hotels must be registered with the Ministry of Culture, Arts and Tourism.

Other Incentives

The other incentives available for the tourism industry as provided under the Income Tax Act 1967 are:-

- Group Inclusive Tours
  Resident companies which are engaged in a tour business are exempted from tax in respect of the income derived from the business of operating group inclusive tours, provided at least 500 foreign tourists a year are brought into Malaysia. The exemption is granted at the statutory income level. Group inclusive tour means a tour package to or of Malaysia or any place within Malaysia undertaken by tourists from outside Malaysia, inclusive of transportation by air, land or sea and accommodation. The incentive is effective until Year of Assessment 2006.

- Domestic Tours
  To encourage domestic tourism, resident companies that operate domestic tour packages with at least 1,200 local tourists per year will be granted exemption in respect of the income derived from the domestic tours. The exemption is granted at the statutory income level. A domestic tour means any tour package or travel within Malaysia participated in by local tourists inclusive of transportation by air, land or sea and accommodation. This incentive is effective until Year of Assessment 2006.

- Conferences Held in Malaysia
  Effective from Year of Assessment 1997, a conference promoter resident in Malaysia will be eligible for income tax exemption on income derived from bringing at least 500 foreign participants into the country in respect of conferences held in Malaysia. Conference promoter means a company incorporated under the Companies Act 1965, or an association or organisation registered under the Societies Act 1966 performing the duties of promoting and organising conferences including the arranging of accommodation, tours and sightseeing for foreign participants.

- Trade Exhibitions Held in Malaysia
  Effective from Year of Assessment 2002, income derived from the organisation of international trade exhibitions held in Malaysia will be eligible for income tax exemption subject to the following conditions:
  - the international exhibition is approved by MATRADE; and
  - the organiser of the international trade exhibition brings in at least 500 foreign visitors per year.

- Chartering Services of Luxury Yachts
  Effective for applications received by the Ministry of Finance from 20 October 2001, income derived by the company in providing chartering services of luxury yachts be granted income tax exemption of 100% for a period of 5 years.

The profits that are exempted from tax under the above incentives are transferred to an exempt income account for the purpose of franking tax-exempt dividends by companies. Redistributions by shareholder companies of such exempt dividends are also exempt from tax.

Promotional Expenditure

Hotels and tour operators are eligible for double deduction on certain overseas promotional expenditure. The expenses qualifying for such double deduction are those incurred on:-

- Publicity and advertisements in any mass media outside Malaysia;
- Publication of brochures, magazines and guidebooks, including delivery costs that are not charged to the overseas customers;
- Market research into new markets overseas, subject to the prior approval of the Minister of Culture, Arts and Tourism;
- Fares in respect of travel overseas for the purposes of negotiating or securing a contract for advertising or participating in trade fairs, conferences or forums approved by the Minister of Culture, Arts and Tourism. Such expenses are subject to a maximum of RM300 per day for accommodation and RM150 per day for sustenance for the duration of the stay overseas;
- Holding of overseas trade fairs, conferences or forums approved by the Minister of Culture, Arts and Tourism; and
- Maintenance of sales offices overseas for the purposes of promoting tourism to Malaysia.

Trading Sector

Malaysian International Trading Company (MITC)

An approved MITC can apply for a tax exemption equivalent to 10% of increased export sales for a period of 5 years provided the following conditions are fulfilled:-

- Not more than 20% of the company’s annual sales are derived from trading in commodities;
- The company uses local services for export such as banking, finance, insurance, local ports and airports.

To qualify as an approved MITC, the company must apply to the MATRADE and satisfy the following conditions:-

- Locally incorporated;
- At least 60% of issued share capital is owned by Malaysians;
- Achieve an annual sales turnover of more than RM10 million;
- Export manufactured goods, especially those from Malaysian small and medium scale companies.

Research & Development (R & D) Activities

In view of the importance of R&D to the economic development of the country, companies undertaking R&D activities are eligible for incentives under the Promotion of Investments Act 1986 as well as incentives under the Income Tax Act 1967.

Pioneer Status or Investment Tax Allowance

- An approved research company carrying out R&D projects for its holding/affiliate/associate companies is eligible for an Investment Tax Allowance in respect of capital expenditure incurred to undertake the R&D activity as provided under the Promotion of Investments Act 1986. The holding/affiliate/associate companies using the services of this R&D company will not enjoy double deduction on the services;

- A contract research and development company carrying out R&D projects for companies other than its related companies is eligible for Pioneer Status or Investment Tax Allowance as provided under the Promotion of Investment Act 1986. A related company refers to a company in whose issued share capital is at least 20% directly or indirectly owned by the other company. The companies using the services of the Contract R&D company can also enjoy double deduction in respect of these services;

- A company carrying out in-house R&D is given an Investment Tax Allowance of 50% on qualifying capital expenditure for a period of 10 years. The allowance is abated to a maximum of 70% of statutory income for each year of assessment.

Expenses of a revenue nature incurred on scientific research by a person and which are related to his business and which is directly undertaken by him or on his behalf, are eligible for a deduction. Revenue expenditure incurred for approved research is eligible for a double deduction.

Among the other incentives under the Income Tax Act 1967 to promote R&D activities are:-

- Plant and machinery used in approved research-related programmes/projects are eligible for capital allowances;

- A building allowance in the form of an initial allowance of 10% and an annual allowance of 3% can be claimed for buildings used for approved research programmes/projects;

- Accumulated losses of approved research companies and institutes can be carried forward for utilisation after the exemption period;
- A double deduction is given for contributions in cash by individuals or organisations to approved research institutes;
- A double deduction is allowed for revenue expenses incurred by companies on approved research projects or for companies which undertake to use the facilities and services of approved research companies or institutes;

Approved Service Projects

Incentives For Approved Service Projects (ASP)
An approved service project means a project in the service sector in relation to transportation, communications, utilities or any other sub sector as approved by the Minister of Finance.

The incentives for approved service projects which are mutually exclusive, given under the Income Tax Act, 1967 are as follows:-

- Income Tax exemption which is comparable to Pioneer Status; or
- Investment Allowance which is comparable to Investment Tax Allowance.

Income Tax Exemption
Generally, companies undertaking ASP's are eligible for an exemption of 70% of the statutory income for 5 years. However, companies undertaking ASP's in Sabah, Sarawak and the designated Eastern Corridor of Peninsular Malaysia will be eligible for an exemption of 85% of the statutory income for 5 years. Companies undertaking ASP's of national and strategic importance will be eligible for 100% exemption of statutory income for 10 years.

The profits that are exempted from tax are transferred to an exempt income account for the purpose of franking tax exempt dividends. Redistributions by shareholder companies of such exempt dividends are also exempt from tax.

Investment Allowance (IA)
Alternatively, companies undertaking ASP's are eligible for IA of 60% on the qualifying capital expenditure incurred within 5 years from the date the capital expenditure is first incurred. The allowance can be used to set off against up to 70% of the statutory income. However, companies undertaking ASP's in Sabah, Sarawak and the designated Eastern Corridor of Peninsular Malaysia will be granted IA of 80% on the qualifying expenditure incurred within 5 years from the date the capital expenditure is first incurred. The allowance can be utilised to set off against 85% of the statutory income. Companies undertaking ASP's of national and strategic importance will be granted IA of 100% on the qualifying capital expenditure incurred within 5 years from the date the capital expenditure is first incurred. The allowance can be utilised to set off against 100% of the statutory income. Any unutilised allowance can be carried forward to subsequent years until it is fully utilised.

The amount of IA utilised is transferred to an exempt income account for the purpose of franking tax exempt dividends. Redistributions by shareholder companies of such exempt dividends are also exempt from tax.

Buildings or structures used for the operation of an approved service project are eligible for the IBA initial allowance of 10% and annual allowance of 3% on the capital expenditure incurred on the buildings or structures.

Tax Exemption on the Value of Increased Exports for Selected Service Sectors

Effective from Year of Assessment 2002, companies in selected services sectors comprising legal, accounting, engineering consultancy, architecture, marketing, business consultancy, office services, construction management, building management, plantation management, private health and education, publishing, and Information and Communication Technology (ICT), can apply for tax exemption on statutory income equivalent to 50% of the value of increased exports.

Technical or Vocational Training Activities

In order to upgrade skills and improve productivity, incentives are available under the Promotion of Investments Act 1986 as well as under the Income Tax Act, 1967 for companies undertaking training activities.

Investment Tax Allowance (ITA)

A company or training institute undertaking technical or vocation training activities is eligible for a 100% ITA in respect of qualifying capital expenditure incurred within 10 years from the date of the first incurrence of capital expenditure. The allowance can be utilised to set-off up to 70% of the statutory income. The incentive is also available to existing companies or training institutes incurring new investment to upgrade their training equipment or expand their training capacities.

Industrial Building Allowance

A special allowance will be given at a rate of 10% of the qualifying expenditure over a period of 10 years for buildings constructed or purchased for the use in industrial, technical or vocational training and education as approved by the Minister of Education.

Double Deduction for Expenses on Training

Double deductions for expenses on training will be considered only for companies which do not contribute to the Human Resource Development Fund. The trainees must be Malaysian citizens who are full-time employees of the company.

Other relevant conditions are:

- Training must be undertaken in approved training institutions or government training institutions;

- For manufacturing companies already in production, this includes expenses incurred on training programmes specifically approved by Malaysian Industrial Development Authority (MIDA) for the purpose of upgrading/developing craft, supervisory skills, technical skills, productivity and quality improvements;

- For new manufacturing companies which have yet to commence production, expenses incurred on training programmes approved by MIDA for the purpose of acquiring/developing craft or technical skills which can contribute to future production;

- Training incurred to improve the employment prospect of any certified handicapped person who is not an employee of the company.

Special Treatment for Gifts of Used Machinery
The donation of used machinery as gifts to technical or vocational training institutions is deemed to result in the donor having disposed of the machinery at nil value for capital allowances purposes. Any unutilised capital allowance in respect of the machinery will be given full deduction in the year of assessment in which the machinery is donated.

Single Deduction on Pre-operating Training Expenses
A single deduction is given for pre-operating training expenses incurred by any company.

Single Deduction for Contributions in Cash
A single deduction is given for contributions in cash to a technical or vocational training institute established and maintained by the Government or statutory body.

Insurance Sector

Incentives for Inward Reinsurance and Offshore Insurance
Income Tax payable on profits from inward reinsurance and offshore insurance is levied at only 5% instead of the normal 28%. This applies to all insurers, whether or not tax resident in Malaysia including Malaysian branches of foreign insurance companies to the extent permitted.

In respect of a resident insurance company, the chargeable income of the inward reinsurance and offshore insurance net of tax is credited to an exempt account for franking tax exempt dividends. Redistributions by shareholder companies of such exempt dividends are also exempt from tax.

Shipping Sector

Shipping Incentives
The statutory income of a resident person derived from the following businesses is exempt from tax:-

- Transporting passengers or cargo by sea on board a Malaysian ship.

- Letting out on charter a Malaysian ship owned by him on a voyage or time charter basis.

“Malaysian ship” means a sea-going ship registered as such under the Merchant Shipping Ordinance, 1952, other than a ferry, barge, tug-boat, supply vessel, crew boat, lighter, dredger, fishing boat or other similar vessel. Under Section 11(1) of the Merchant Shipping Ordinance, 1952, a ship which is owned by a Malaysian citizen or a corporation must meet certain conditions including the following:-

- The principal place of business of the corporation is in Malaysia;

- The majority voting rights of the corporation are held by Malaysian citizens free from any trusts or obligations in favour of a non-Malaysian;

- The majority of the directors of the corporation are Malaysian citizens.

A person who is carrying on a business in respect of which its income is tax exempt as mentioned above is required to maintain a separate account of the income derived from each Malaysian ship from that business.

The exempt income from the Malaysian ship can be credited to an exempt account for the purpose of franking tax exempt dividends.

Where such dividends are received by a shareholder who is a company, any payment of dividends by that company to its shareholders is exempt from tax.

Effective from 20 October 2001, rental income received by non-residents from the rental of ISO containers to Malaysian shipping companies will be exempt from tax.

Regional Activities

Special incentives (fiscal and non-fiscal) are available to companies which undertake regional activities from Malaysia. Depending on the type of regional activities, the companies can consider applying for the following:

- Operational Headquarters Company (OHC) status; or

- International Procurement Centre (IPC) status.

Companies granted either the OHC or IPC status can be 100% foreign owned.

Operational Headquarters Company

The qualifying income of an approved Operational Headquarters Company (OHC) derived from the provision of certain services is taxed at a concessionary rate of 10%. The profit after the 10% concessionary tax is credited to an exempt account for franking tax exempt dividends. Redistributions of such exempt dividends by corporate shareholders are also tax exempt.

Income qualifying for the concessionary tax rate covers the provision of services by the OHC to offices outside Malaysia or to related companies outside Malaysia.

Qualifying services include:-

- General management and administration;
- Business planning and co-ordination;
- Procurement of raw materials, components and finished products;
- Technical support and maintenance;
- Marketing control and sales promotion planning;
- Training and personnel management;
- Data/information management and processing;
- Treasury and fund management services; including provision of credit facilities, the funds of which can be obtained from outside or within Malaysia. Where such funds are obtained from within Malaysia the amount shall not exceed RM10 million;
- Research and development work;
- Corporate financial advisory services.

Other non-fiscal incentives enjoyed by an OHC include the following:-

- Expatriate posts which will be approved for a period of 3 to 5 years based on expertise, skill requirements and needs of the company;
- The ability to borrow freely from domestic sources in foreign currency, without the approval of the Central Bank, for treasury and fund management operations for their related companies outside Malaysia;
- The ability to borrow freely from domestic sources in Malaysian Ringgit (RM) up to a maximum of RM10 million for use in Malaysia (borrowing in excess of RM10 million requires prior approval from the Central Bank);
- The ability to invest freely in foreign securities and to lend to related companies outside Malaysia as long as the domestic borrowing in RM is within the RM10 million limit and the remittances are made in foreign currency equivalent;
- The ability to open one foreign currency account or one multi-currency account with any of the designated banks to retain export proceeds in foreign currency;
- The ability to open foreign currency accounts with the designated banks in Malaysia, including the offshore banks in Labuan, or overseas banks for crediting foreign currency receivables other than export proceeds.

Foreign sourced income received by an OHC (e.g. dividends and interest) is not subject to Malaysian tax.

International Procurement Centre

International Procurement Centres (IPCs) are regional organisations established by manufacturing companies to economise on the cost of services and purchase of raw materials, components and finished products. The following incentives are enjoyed by IPCs:-

- Approval of expatriates' posts based on the requirements of the IPC;
- Maintenance of one or more foreign currency accounts with any licensed commercial bank to retain their export proceeds without any limit imposed;
- Participation in foreign exchange forward contracts with any licensed commercial bank to sell forward export proceeds based on projected sales;
- Exemption from the requirements of the Ministry of Domestic Trade and Consumer Affairs with regards to foreign equity ownership on wholesale and retail trade; and
- Permission to bring raw materials, components or finished products without payment of custom duties into Free Zones or Licensed Manufacturing Warehouses for repacking, cargo consolidation and integration before distribution to the final consumers.

To qualify as an approved IPC, a company must apply to the Ministry of International Trade and Industry and satisfy the following conditions:-

- Locally incorporated with minimum paid-up capital of RM500,000;
- A minimum annual business expenditure of RM1.5 million; and
- Incremental usage of Malaysian ports and airports.

Other Incentives

Accelerated Capital Allowance

A manufacturing company which reinvests in the manufacture of promoted products and a company in the agriculture sector that reinvests in promoted agricultural activities and food products, is eligible to apply for Accelerated Capital Allowance after the expiry of the Reinvestment Allowance period.

For agricultural activities, these include cultivation of rice, maize, vegetables, tubers, livestock, aquatic products and any other activities approved by the Ministry of Finance.

This incentive is also applicable for all capital expenditure on related machinery and equipment incurred by:

- Companies which are themselves waste generators and wish to establish facilities to store, treat and dispose of their waste, either on-site or off-site;
- Companies which conserve their own energy consumption;
- Companies undertaking waste recycling activities.

For the above, the Accelerated Capital Allowance is to be utilised within 3 years, i.e. an initial allowance of 40% in the first year and an annual allowance of 20%.

Qualifying Pre-operational Business Expenditure

A resident company is eligible to claim qualifying pre-operational business expenditure incurred in connection with a proposal by that company to undertake investment in a business venture approved by the Minister of Finance in a country outside Malaysia.

The expenses that qualify are those incurred on:-

- Conduct of feasibility studies;
- Conduct of market research or the obtaining of marketing information;
- Overseas travelling expenses for the purposes of conducting a feasibility studies or market surveys; and
- Accommodation and sustenance expenses for the duration of the overseas trip up to a maximum of RM400 per day.

Tax Exemption on Foreign Income

All income arising from sources outside Malaysia and received in Malaysia by a resident company (other than a company carrying on the business of banking, insurance, shipping and air transport) or a unit trust will be exempted from Income Tax.

The income so exempted shall be available for distribution as tax exempt dividends to shareholders/ unit holders. A corporate shareholder/unit holder receiving such a dividend can in turn redistribute tax exempt dividends to its shareholders.

Taxation of Profit of an Offshore Company in Labuan

Offshore Companies in Labuan are taxed at 3% of their offshore trading profits as shown in the audited accounts, subject to a maximum limit of RM20,000. Profits from offshore non-trading activities carried on by Offshore Companies are not subject to tax. Further details are provided in Chapter 11.

Expenses Eligible For Double Deduction

Double Deduction for Promotion of Exports

Certain expenses incurred by resident companies for the purpose of seeking opportunities for the export of products manufactured in Malaysia are eligible for a double deduction against taxable income. The expenses that qualify are those incurred on:-

- Publicity and advertisements in any media outside Malaysia;
- Supply of free samples abroad including delivery costs;
- Export market research or the obtaining of export marketing information;
- Preparation of tenders for supply of goods overseas;
- Supply of technical information abroad;
- Exhibits and/or participation required in trade or industrial exhibitions held locally or abroad approved by the Ministry of International Trade and Industry (MITI);
- Fares in respect of travel overseas by employees of companies for business; and accommodation expenses up to RM300 per day and sustenance expenses up to RM150 per day;
- Maintaining sales offices and warehouses overseas for the promotion of exports from Malaysia;
- Professional fees incurred in packaging design subject to conditions that the product is of export quality and the company uses local professional services;
- Services rendered for public relations work connected with exports; and
- Participation in virtual trade shows and trade portals.

For companies enjoying Pioneer Status, such expenses incurred during the pioneer period shall be accumulated and given deductions against the companies' post-pioneer business income.

Double Deduction for Promotion of Export of Services

- Export Market Research;
- Preparation of tenders for the supply of services overseas;
- Supply of technical information abroad;

- Fares in respect of travel overseas by employees of companies for business; and accommodation expenses up to RM300 per day and sustenance expenses up to RM150 per day;

- Cost of maintaining office overseas for purpose of promotion of services;

- Publicity and advertisements in any media outside Malaysia for the promotion of the export of services;

- Feasibility studies for overseas projects identified for the purpose of tender;

- Participation in trade or industrial exhibitions in the country or overseas; and

- Participation in exhibitions held in Malaysian Permanent Trade and Exhibition Centres Overseas.

Others

The following types of expenses are given a double deduction in the year in which they are incurred:-

- Insurance premium paid for import and export of cargo insured with any insurance company incorporated in Malaysia;

- Approved research and development expenditure;

- Cash contributions to approved research institutes;

- Payments for the use of services of approved research companies or institutes;

- Remuneration in respect of employment of handicapped employees;

- Qualifying expenditure incurred on local advertising of Malaysian branded products;

- Expenditure incurred on overseas advertising of Malaysian branded products provided the brand is registered in overseas;

- Freight charges incurred by all manufacturers for the shipment of their manufactured goods from Sabah or Sarawak to any port in Peninsular Malaysia;

- Freight charges incurred by certain manufacturers who export rattan and wood-based products (excluding sawn timber and veneer); and

- Professional fees paid to brand management companies, which promote Malaysian brand names.