

NOTICE FOR LABUAN ENTITIES

MALAYSIA REVISES LABUAN'S CORPORATE TAX LAW AND ABOLISHES THE RM20,000 FLAT TAX RATE

The purpose of this Notice is to inform you of the amendments to the Labuan Business Activity Act 1990 ("LBATA"), gazetted under the Finance Act 2018, which comes into operation on 1 January 2019.

These changes will affect you and your clients who own Labuan entities.

So, what is it all about?

Malaysia has announced a number of changes to the LBATA and the Income Tax Act 1967 ("ITA") affecting Labuan entities. As a result of the changes, the Malaysian Government has also issued two new regulations supplementing the LBATA and the ITA namely –

- Labuan Business Activity Tax (Requirements for Labuan Business Activity) Regulations 2018; and
- Income Tax Act (Deductions Not Allowed for Payment Made to Labuan Company by Resident) Rules 2018.

Significant changes

- 1) Abolition of RM20,000 flat tax rate and maintains only 3% tax for Labuan entities carrying on trading activities. This will also require Labuan entities carrying on trading activities to have their accounts audited by an approved auditor in Labuan. Labuan entities carrying on non-trading activities will still benefit from the 0% tax rate.
- 2) Labuan entities can now on conduct –
 - (i) transactions in Ringgit Malaysia; and
 - (ii) transactions with residents of Malaysia.
- 3) For residents of Malaysia who have transactions with a Labuan entity, tax deduction on expenditure incurred by the residents is limited to –
 - (i) 67% of the amount of interest payment
 - (ii) 67% of the amount of lease rental payment
 - (iii) 3% of the amount of other payments
- 4) Royalty and other income derived from an intellectual property right if receivable as consideration for the commercial exploitation of that right will be subject to prevailing tax rate of 24% under the ITA.
- 5) Labuan entity will be required to show "economic substance", key requirements include that it must have adequate number of full time employees and must meet minimum annual operating expenditure requirement in Labuan.

When is the effective date?

To take effect on 1 January 2019.

Further guidelines and rules to be issued by the Labuan FSA and the Malaysian IRB

There will be a series of meetings in the next week or so between the Labuan industry players and Labuan FSA as well as the IRB to iron out issues and address certain matters in relation to the changes. We anticipate further guidance will be issued to reach clarity of our understanding of the new law.

Please note that our notice is intended to brief you of the key changes affecting Labuan entities. It should not be used or relied upon as a substitute for a tax advice or a basis for formulating your or your client's business decisions.

If you require further information or would like to discuss how the new changes will impact your business, please get in touch with your usual Konsultan contact or write to us at cosec@hmrkonsultan.com.

Thank you.

Yours faithfully,

Sukor Ashak
Managing Director
HMR Konsultan (Labuan) Ltd.