

NOTICE FOR LABUAN ENTITIES

AN UPDATE AND DEADLINE ON ECONOMIC SUBSTANCE REQUIREMENTS FOR LABUAN ENTITIES

The purpose of this Notice is to update you on matters in connection with the changes to the Labuan Business Activity Tax Act 1990 ("LBATA") and the subsequent Labuan Business Activity Tax Act (Requirements for Labuan Business Activity) Regulations 2018 ("Labuan ESR" or the "regulations") as previously [notified](#)¹, are now in effect, in terms of –

- application of the preferential tax rate of 3% for trading activities and 0% for non-trading activities;
- economic substance requirements; and
- the deadline to comply by 31st December 2019.

To recap, the Labuan ESR sets out the requirements for Labuan entities in terms of economic substance. These regulations list down "Labuan entities carrying on Labuan business activities" which are in-scope, must meet the minimum number of full-time employees and an amount of annual operating expenditure ("OPEX") as specified in the [Schedule](#)².

Pure equity and non-pure equity holding now included in the list. Status of trading entities still uncertain

Labuan FSA released their latest pronouncement on 11th December 2019, extending the scope to include entities that carry on "**pure equity holding**" and "**non-pure equity holding**" business activities. For entities that carrying on non-pure equity holding activity (business activity that derives other passive income e.g. interest and rental income) are required to have at least 2 full-time employees and meet the minimum of RM50,000 (approx. USD12,500) annual OPEX in Labuan. Whereas, pure equity holding entities (business activity that derives income from dividends and capital gains only) will only need to meet the management and control requirement, and the minimum of RM50,000 annual OPEX in Labuan.

Notably, Labuan FSA and the regulations are ambiguous on the status of Labuan entities carrying on non-licensed trading activities whether they fall within the scope of substance. At this point, we are unable to determine if such entities are required to comply with the substance requirements. Further industry consultation is ongoing with Labuan FSA with respect to this issue.

Indicative direction on economic substance requirements for all Labuan entities

It is now expected that all Labuan entities are to comply with the economic substance requirements by the deadline. Entities that deem non-compliant will be taxed at the higher tax rate of 24% under the soon to be enacted Labuan Business Activity Tax (Amendment) Bill 2019.

Actions now required

In the absence of any final guidelines from Labuan FSA, despite several high-level meetings and industry consultations held with them throughout the course of 2019, we can only advise that you or your clients to comply with the substance requirements pursuant to Labuan ESR in view of maintaining the preferential tax rates of 3% (for trading activities) or 0% (for non-trading activities).

For **non-licensed entities**, we advise that you or your clients to undertake –

(1) Exercise of management and control and meet the RM50K OPEX in Labuan

- by holding board and members' meetings, at least twice yearly, in Labuan to reflect that the entity undertakes its decision makings in, from and through Labuan;

¹ Notice for Labuan Entities (Ref: HMRKLB00119) 11th January 2019

² Labuan Business Activity Tax Act (Requirements for Labuan Business Activity) Regulations 2018 (P.U. (A) 392) – please scroll down for English version

- to reflect that its operational activities are being carried out physically in Labuan i.e. certain administrative activities like maintaining bookkeepers, payroll services, issuance of invoices/receipts, insurance policies, virtual office facility, etc. which may be outsourced to us.

or

(2) Full physical presence in Labuan

- to employ a minimum of 2 full-time employees (one with managerial position and one non-managerial/clerical, either on permanent or on contract basis);
- to establish an office premise to run your business operation;

By having the above in place, the entity should comply with the minimum Labuan ESR.

For **licensed activities**, your entities will have to comply with the Labuan ESR. We understand that most of the licensed entities will already meet the substance requirements with little effort due to the licensing conditions imposed separately.

This is, however, not a “one-size-fits-all” solution for compliance. We are positioning ourselves to meet the demand in order to provide solutions, tailored to your or your client’s needs. Outsourcing of certain activities such as human resources, nominee services, administrative and office premises will be made available by us to your or your client’s entities in order to keep the cost of meeting the substance requirements low, reasonable and controlled. We urge that you get in touch with us for further consultation.

Further guidance to be issued by Labuan FSA

We anticipate that Labuan FSA will publish further pronouncements, if not their final codes or guidelines, as to address the industry’s several key questions on the substance matters which are still left unanswered and unrefined in their applications.

Please note that this notice is intended to update you with the revised changes affecting all Labuan entities. It should not be used or relied upon as a substitute for advice or a basis for formulating your or your client’s business decisions as to the tax and/or the economic substance requirements.

We urge that you contact us if you require further information or would like to discuss how the revised changes will impact your or your client’s business. Please contact us for more details and further consultation.

Thank you.

Yours faithfully,

Sukor Ashak
Managing Director
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