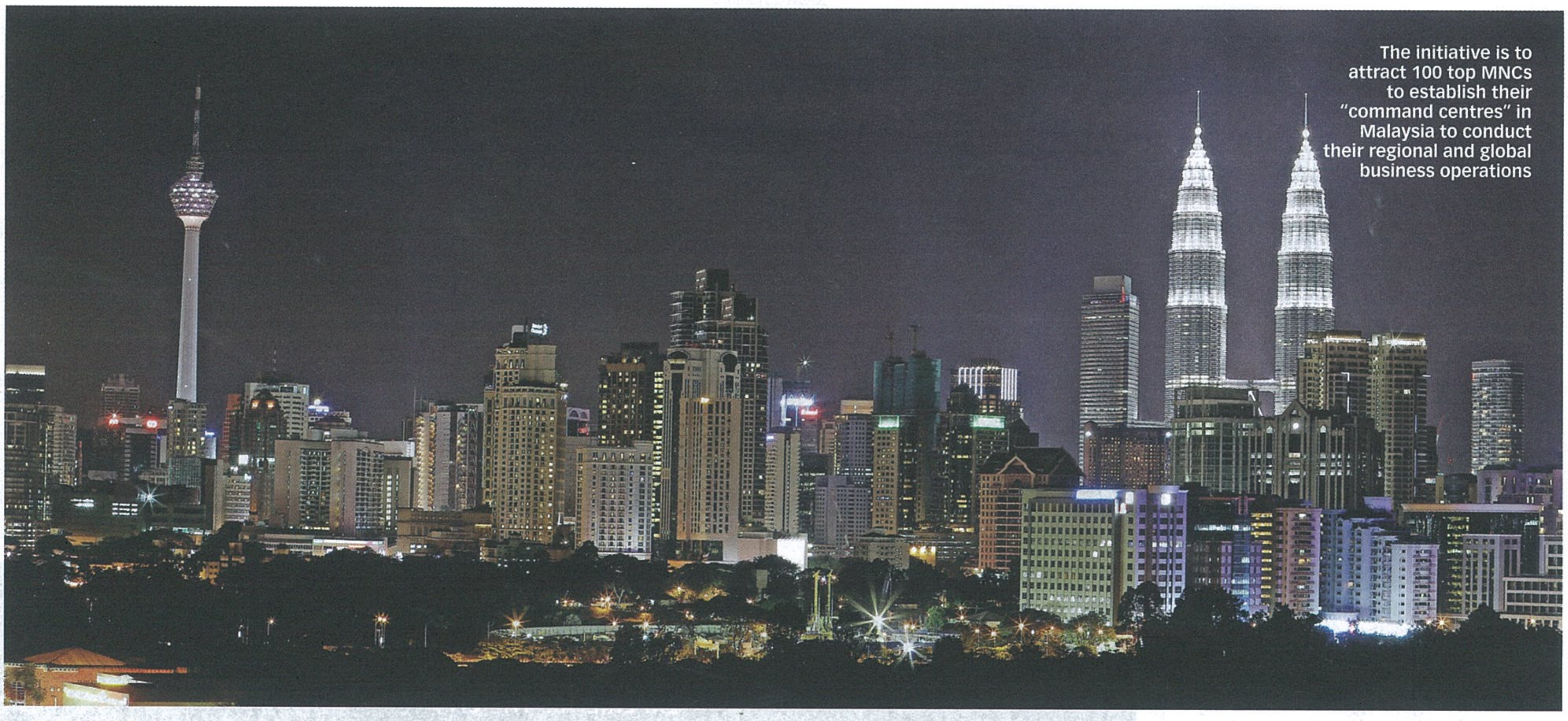

The initiative is to attract 100 top MNCs to establish their "command centres" in Malaysia to conduct their regional and global business operations

Principal hub plan needs more incentives

To compete with other regional hubs, MNCs must be given more benefits to relocate their headquarters here

Guest writer

BY LEE BOON SIEW

THE government recognises the service sector as an important contributor to economic growth as Malaysia forges ahead to become a high-income nation by 2020. Last year, the sector contributed 55% to the gross domestic product and provided eight million jobs or 61% of total employment.

The sector's structured and robust development will help the country give others like Singapore and Hong Kong, which also thrive on services, a run for their money.

The launch of the Principal Hub incentive by the Ministry of International Trade and Industry in April was met with initial enthusiasm. The incentive is to some extent an important step in transforming the country into a service-based economy.

It is part of the government's initiative to realise its ambition of attracting 100 top multinational corporations (MNCs) to relocate their headquarters here as envisaged in the Economic Transformation Programme.

The Principal Hub is a one-stop-shop incentive to replace the Operational Headquarters, International Procurement Centre and Regional Distribution Centre incentives. The benefits include a three-tiered corporate tax rate from zero to 10% for a period of five years which may be extended by another five years subject to the number of skilled jobs they create and their business expenditure.

This incentive is to entice reputable MNCs to establish their "command centres" in Malaysia to conduct their regional and global business operations. Essentially, core functions such as strategic decision making, risk management, finance and others will be conducted from this hub, thereby, attracting capital and skilled labour to the country.

The introduction of the incentive is timely in view of the impending implementation of the Asean Economic Community (AEC) on Dec 31 which is a bold and strategic initiative aimed at fostering regional economic integration amongst the 10 member nations. The economic potential envisaged as a result of the free flow of goods, services, investments, capital and skilled labour is likely to place Asean on the radar of many MNCs.

As such, the incentive can be seen as an additional sweetener for MNCs looking to establish or relocate their operations in Asean, particularly Malaysia.

Window of opportunity

The idea of potentially enjoying a 10-year tax holiday can be a good business case for MNCs to strategically relook their business model. For companies which already have an Asean presence, there is a window of opportunity to implement internal reorganisation to establish a control tower in Malaysia to provide strategic, business or shared services to network companies in other countries.

This entails the centralisation of key business functions or activities, risks and intangibles in Malaysia. In short, the "engine" which drives the business forward should be located here. This would be a good driver for MNCs to strategically reassess the efficiency of their global supply chain. However, time is of the essence as the deadline for submission of application to the Malaysian Investment Development Authority is April 30, 2018.

An even bolder move is for those with headquarters in renowned commercial hubs such as Hong Kong or Singapore to seriously consider whether it makes business sense to operate from Malaysia instead. With the Principal Hub package and coupled with Malaysia's cost-competitive advantage, talented multicultural and multilingual workforce, this should make the country an attractive destination for MNCs.

Whilst it is commendable the government has embarked on many roadshows locally and overseas to create awareness of this new incentive, we are not alone in this race to lure reputable MNCs.

The Singapore Economic Development Board has long been offering the Regional Headquarters or International Headquarters incentive to attract top-notch MNCs to set up base in the island republic. The Regional Headquarters incentive grants a company a concessionary tax rate of 15% for three years with the possibility of an additional two years subject to meeting certain minimum requirements.

Bigger players that can offer greater value to the Singaporean economy by committing to exceed the minimum requirements of the Regional Headquarters incentive may instead be awarded the International Headquarters incentive which offers concessionary tax rates depending on the level of economic commitment.

Thailand, on the other hand, which previously had the Regional Operating Headquarters incentive, recently launched new tax incentives to promote the establishment of the International Headquarters or International Trading Centre by MNCs in the country. Companies granted either of these incentives may enjoy full corporate income tax exemption on certain classes of income received for 15 accounting periods.

Besides tax exemption, these incentive packages also come with other tax benefits to enhance their attractiveness such as exemption from deducting withholding tax on certain types of payments made to foreign affiliates and concessionary tax rate for expatriates.

What Principal Hub incentive lacks

The Principal Hub incentive unfortunately does not offer such additional tax benefits which are of equivalent importance to MNCs apart from the corporate income tax exemption.

To give Malaysia the added advantage over other countries, additional measures should be introduced to further assist companies which have been awarded the incentive in operationalising the hub since it will be a major exercise involving relocation of key business activities and personnel.

Tax benefits for expatriates

Firstly, expatriates will be transferred to Malaysia to operate the Principal Hub. However, the benefits accorded currently do not include tax exemption for these expatriates. The government should consider introducing such exemptions to incentivise expatriates to relocate here. This is not new as it was offered under the Operational Headquarters incentive.

Secondly, regulatory authorities should be flexible in evaluating applications for the Principal Hub incentive. The door should not be closed for an applicant which fails to comply with certain quantitative conditions but nevertheless has an exciting value-adding proposition for the country.

In fact, the three-tier structure, which is based on the company's level of value creation, would allow for these flexibilities. As the applicant progresses with more activities in the country, the company can move up the tier for enhanced incentives.

However, one should be careful in evaluating the tax benefits accorded by this incentive. Recent high-profile cases involving shifting of profits to low-tax environments by MNCs has prompted tax authorities globally to pay more attention to the issue of tax avoidance to ensure corporations pay their fair share of taxes in the jurisdictions in which they operate.

The presence of economic substance is key and MNCs seeking to establish their Principal Hub in Malaysia must be mindful of the evolving tax landscape both locally and globally. Reputable names cannot afford to get caught in a costly dispute with the taxman. FocusM

It is hoped that the Principal Hub incentive will serve as the catalyst for growth in the service sector as a means to propel Malaysia to the much-aspired developed nation status by 2020.

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