



TaXavvy

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MIDA Guidelines on Tax Incentives for Principal Hub 3.0 and Global Trading Centre



Principal Hub 3.0

Following the announcement in Budget 2021, the Malaysian Investment Development Authority (MIDA) has recently released details of the Principal Hub (PH) incentive 3.0.

The PH incentive was first introduced in 2015 to replace the International Procurement Centres (IPC), Regional Distribution Centres (RDC) and Operational Headquarters (OHQ) incentive schemes.

A PH is a locally incorporated company that uses Malaysia as a base for conducting its regional or global businesses and operations to manage, control, and support its key functions including management of risks, decision making, strategic business activities, finance, management and human resource. A PH can be located closer to customers and supply chains to improve operational efficiency, promote product/service quality and speed to market at a lower cost. The PH structure also enables MNCs to better share resources between groups of companies. The PH structure and qualifying services are set out below:

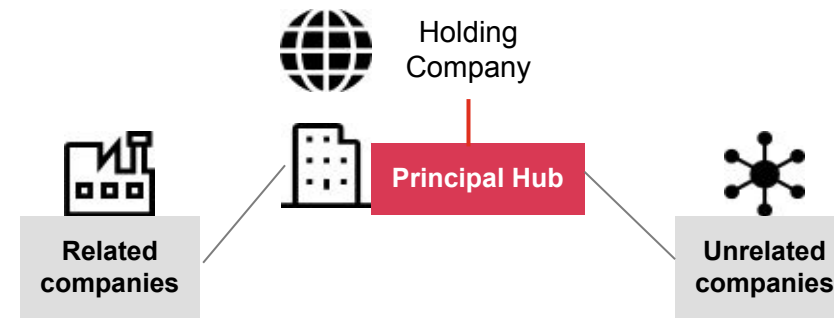


Table 1: Qualifying services

Strategic Services	Business Services	Shared Services
<ul style="list-style-type: none"> Regional P&L / Business Unit Management Strategic Business Planning & Corporate Development Corporate Finance Advisory Services Brand Management IP Management Senior-level Talent Acquisition & Management, etc 	<ul style="list-style-type: none"> Bid & Tender Management Treasury & Fund Management Research, Development & Innovation Technical Support & Consultancy Information Management & Processing Economic / Investment Research Analysis 	<ul style="list-style-type: none"> Project Management Sales & Marketing Business Development Logistic Services, etc. Corporate Training & Human Resource Management Finance & Accounting



Evolution of PH incentive

Since its introduction in 2015, the PH incentive has been enhanced at intervals to further strengthen Malaysia's competitiveness as the preferred headquarters hub for MNCs in Asia Pacific.



Highlights of the PH incentive journey

PH 2.0 (2019)

Enhanced tax incentive

Existing incentive was improved by granting:

New companies	Up to 0% tax rate for 10 years based on the level of commitments
Existing companies	Concessionary 10% tax rate on overall statutory income derived from activities in Malaysia for 5 years

PH 1.0 (2015)

Launching of the new PH incentive scheme

New companies	Preferential tax rates of 0%, 5% or 10% for Tier 1, 2 and 3 companies respectively for a period of 5 years (extendable for a second 5-year period)
Existing companies	Tax exemption on value-added income up to 5 years (extendable for a second 5-year period for companies without incentive)

PH 3.0 (2021)

Relaxation of conditions for PH incentive and introduction of Global Trading Centre (GTC) incentive

The Malaysian Investment Development Authority (MIDA) has recently published the Guidelines for PH 3.0 and GTC incentives.

Approved Investments for Principal Hubs (2015-2020)

Malaysia has seen a sturdy growth in companies setting up their regional headquarters in the country whereby a total of **38 PH projects** have been approved. The total approved investments amounted to **RM47.8 billion** and **3,282 high value jobs** were created. (Source: MIDA's website as at 28 September 2021)

MIDA's Guidelines for PH Incentive 3.0

MIDA has recently issued the Guidelines for PH Incentive 3.0 (PH 3.0 Guidelines).

The PH 3.0 Guidelines is available on MIDA's website www.mida.gov.my (Forms and Guidelines > Services Sector > Regional Operations > Principal Hub).

Under Budget 2021, the Government has proposed the following in order to encourage further establishment of PH in Malaysia:

- The application period for the PH incentive for companies undertaking qualifying services be extended until 31 December 2022 (previously 31 December 2020).
- The minimum condition on the number of high value jobs, annual operating expenditure and the number of key posts for renewal of the PH incentive for the second 5-year period be relaxed.

Following the above, MIDA has issued the new PH 3.0 Guidelines. The PH 3.0 Guidelines is effective for applications received by MIDA from 1 January 2021 to 31 December 2022.

Highlights of PH 3.0 Guidelines

- **Preferential tax rate** - Approved PH companies enjoy preferential tax rate on services income derived from qualifying activities based on the level of commitment by the company as follows:

	New Company				Existing Company
	Tier 1		Tier 2		
Period of incentive (block years)	5 years (initial)	+5 years (renewable)	5 years (initial)	+5 years (renewable)	5 years
Tax rate	0%		5%		10%

- **Removal of trading activities** - The incentives pertaining to trading activities (previously covered under PH 2.0) have been removed from the scope of PH 3.0. The incentives in relation to trading will now be streamlined under a specific incentive, i.e. the new GTC incentive.
- **Relaxation of conditions** - The conditions for renewal of the PH incentive for the second 5-year period have been updated. Key conditions of the PH 3.0 incentives are set out in the following pages (comparison to PH 2.0 are indicated, where applicable):

Category 1 - New companies	Tier 1	Tier 2
Incentive	Preferential tax rate of 0% for 5 + 5 years on statutory income from qualifying services	Preferential tax rate of 5% for 5 + 5 years on statutory income from qualifying services
Paid-up capital	More than RM2.5 million	More than RM2.5 million
Serving / business control of no. of network companies <u>Network companies</u> are defined as follows: <ul style="list-style-type: none"> - Related companies or entities within the same group including subsidiaries, branches and joint ventures. - Non-related companies which have a contractual agreement of at least 2 years with the PH company or its ultimate holding company with regards to the PH company's business or supply chain. 	10 <i>(15, under PH 2.0)</i> (including 4 related companies)	7 <i>(10, under PH 2.0)</i> (including 3 related companies)
Annual operating expenditure (Note)	<ul style="list-style-type: none"> • First 5 years: RM10 million • Second 5 years (renewable): RM13 million <i>(commitment from end of Year 5 + 30%, under PH 2.0)</i> 	<ul style="list-style-type: none"> • First 5 years: RM5 million • Second 5 years (renewable): RM7 million <i>(commitment from end of Year 5 + 30%, under PH 2.0)</i>
Number of high value jobs (inclusive of key posts) (basic monthly salary of at least RM5,000)	<ul style="list-style-type: none"> • First 5 years: 50 • Second 5 years (renewable): 60 <i>(commitment from end of Year 5 + 20%, under PH 2.0)</i> 	<ul style="list-style-type: none"> • First 5 years: 30 • Second 5 years (renewable): 36 <i>(commitment from end of Year 5 + 20%, under PH 2.0)</i>
Number of key posts (basic monthly salary of at least RM25,000)	<ul style="list-style-type: none"> • First 5 years: 5 • Second 5 years (renewable): 5 <i>(commitment from end of Year 5 + 20%, under PH 2.0)</i> 	<ul style="list-style-type: none"> • First 5 years: 4 • Second 5 years (renewable): 4 <i>(commitment from end of Year 5 + 20%, under PH 2.0)</i>
Qualifying Services	Regional P&L / Business Unit Management, Strategic Business Planning & Corporate Development + 2 other qualifying services under Strategic Services, Business Services or Shared Services as specified in Table 1.	

Note: Under PH 3.0, a fixed number (i.e. value in RM and number of jobs) is prescribed for the renewal conditions. This provides a "ceiling" as compared to the approach under PH 2.0 where the conditions are based on prescribed incremental rates on values from the end of year 5. For example, under PH 2.0, if a Tier 2 PH company incurred annual operating expenditure of RM7 million by end of year 5, the said PH company is required to commit to an annual operating expenditure of RM9.1 million during the second 5 years (RM7 million + 30% of RM7 million) whereas under PH 3.0, the annual operating expenditure commitment for the second 5 years is fixed at RM7 million.

Category 2 - Existing Manufacturing/Services Company

Incentive	Preferential tax rate of 10% for 5 years on statutory income from qualifying services
Serving / business control of no. of network companies	7 (including 3 related companies) <i>(10 including 5 related companies, under PH2.0)</i>
Annual operating expenditure (Note)	RM10 million <i>(the higher of RM10 mil or average operating expenditure for the past 3 years + 30%, under PH 2.0)</i>
Number of high value jobs (inclusive of key posts) (basic monthly salary of RM5,000)	30 <i>(the higher of 30 or existing number of high value jobs + 30%, under PH 2.0)</i>
Number of key posts (basic monthly salary of at least RM25,000)	5
Qualifying Services	Regional P&L/Business Unit Management, Strategic Business Planning & Corporate Development + 2 other qualifying services under Strategic Services, Business Services or Shared Services as specified in Table 1.
Structured Internship Programme/ Training Scheme introduced by the Government	Conduct Structured Internship Programmes / equivalent Training Schemes to train at least one (1) graduate every year
Structured Training Programme	At least 10% of local workforce from the entire workforce to undergo a structured training program for upgrading of skills in related qualifying services

Note: Annual operating expenditure is defined as expenses incurred in carrying out the PH's day-to-day operations excluding cost of goods sold / cost of services and expenses that are not directly related to the core income generating activities of the PH such as depreciation and interest on borrowings. It will be based on the operating expenditure which is reflected in the company's audited financial statement (excluding interest, depreciation and other expenses which are not incurred for the production of services income).



Non-compliance with conditions

An approved PH company must comply with the stipulated conditions throughout the incentive period. Where in any year of assessment during the incentive period, the approved PH company fails to comply with the stipulated conditions, the company may not enjoy the preferential tax rate for that year of assessment.

Non-fiscal benefits

Facilities which will be accorded to an approved PH company include:

- *Flexible ownership* - No local equity / ownership condition
- *Access to foreign talents* - Expatriate posts based on the requirements of the applicant's business plan subject to the current policy on expatriates
- *Foreign exchange administrative (FEA) flexibilities* - Can be considered to support PH companies in ensuring business efficiency and competitiveness. Applications are to be submitted to Bank Negara Malaysia.



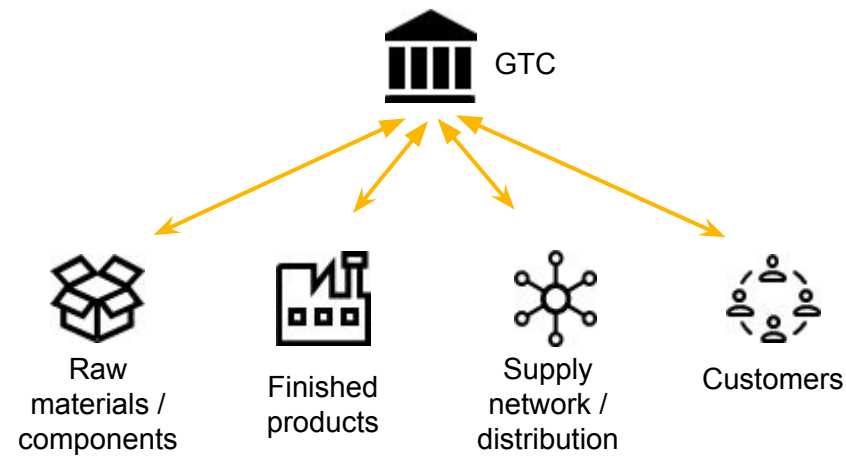
MIDA's Guidelines for Global Trading Centre (GTC) Incentive

The GTC incentive was announced in Budget 2021 to promote the establishment of companies undertaking global trading businesses in Malaysia. The tax incentive in relation to trading activities which was previously covered under PH 2.0 is now covered under the GTC incentive.

The Guidelines for the GTC incentive is available on MIDA's website www.mida.gov.my (Forms and Guidelines > Services Sector > Regional Operations > Global Trading Centre).

How GTC works

By definition, a GTC is a locally incorporated company that uses Malaysia as its international trading base for undertaking strategic sourcing, procurement and distribution of raw materials, components and finished products to its related and unrelated companies in Malaysia and abroad, depicted as follows:



Benefits to investors

A company approved with the GTC incentive may enjoy a concessionary corporate tax rate of 10% for a period of 5 years. The incentive period may be extended for another period of 5 years.

Eligible applicants may submit an application to MIDA from 1 January 2021 until 31 December 2022.

Qualifying conditions for the GTC incentive

The following are the salient conditions from the Guidelines:

Qualifying person	<ul style="list-style-type: none"> • A company newly incorporated under the Companies Act 2016 • Resident in Malaysia
Paid-up capital	RM1.0 million <i>(minimum paid-up capital was >RM2.5 million under PH 2.0 which covered both trading and services)</i>
Annual sales turnover from qualifying activities	RM300 million <i>(annual sales in relation to trading was RM500 million, under PH 2.0)</i>
Annual operating expenditure from qualifying activities (Note)	RM1.5 million
Number of high value jobs with basic monthly salary of at least RM5,000 <i>(min 50% to comprise of Malaysians)</i>	15
Location	Must operate in a Licensed Manufacturing Warehouse (LMW), Free Zone (FZ) and/or Bonded Warehouse
Usage of Malaysian ports and airports	Mandatory

Note: Defined as expenses incurred in carrying out the day-to-day operation of the GTC which are related to the core income generating activities of the GTC. For the purpose of compliance of condition, it will be based on the operating expenditure which is reflected in the company's audited financial statement (excluding interest, depreciation and other expenses which are not incurred for the production of income from qualifying activity).

Non-compliance with conditions

An approved GTC must comply with the stipulated conditions throughout the incentive period. Where in any year of assessment during the incentive period, the company fails to comply with the stipulated conditions, the company may not enjoy the preferential tax rate for that year of assessment.

Key takeaways

The release of the details of the PH 3.0 and GTC incentives is timely as MNCs need to adapt business and operating structures during the current times with the rapid change in global and business landscapes. Below are some concluding points:

- **Positioning Malaysia as the preferred global/regional hub** - The extension of the application period to 31 December 2022 and relaxation of conditions of the incentives demonstrate the Government's commitment to attract and retain MNCs to locate key strategic functions in Malaysia.
- **Streamlined incentive regimes and targeted conditions** - The shifting of trading activities to a specific incentive, i.e. the GTC incentive, streamlines the PH 2.0 incentive into two separate categories, i.e. service-based and trading-based activities. With a dedicated GTC incentive, more targeted qualifying conditions have been formulated by the Government.
- **Transitional considerations** - For companies which are currently enjoying the PH incentive on its trading income (first 5-year period), the PH 3.0 Guidelines does not currently specify which are the renewal conditions that will be applicable for the renewal (second 5-year period), i.e. whether it will be based on conditions under the PH 3.0 Guidelines or PH 2.0 Guidelines. Subject to clarification from the authorities, companies currently enjoying the PH 2.0 incentive with trading income (first 5-year period) will likely continue to fall under the conditions based on PH 2.0 Guidelines for the renewal of its second 5-year tax incentive period. In other words, the conditions based on the PH 2.0 Guidelines will be grandfathered on such companies. This assumption is made on the basis that the business model which was presented during the application and approval for the first 5-year period was based on a combination of both qualifying service and trading activities.



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