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Transfer Pricing

Important Updates for 2021

Summary

The Finance Act 2020 was gazetted on 31 December 2020 and has been operative since 1 January 2021. Amongst others, there are several new provisions found in the Finance Act 2020 that aim to strengthen the enforcement for transfer pricing (“TP”) compliance in Malaysia. On another note, the Inland Revenue Board (“IRB”) has also updated the timeline for furnishing TP Documentation (“TPD”) in the Malaysian TP Guidelines (“MTPG”) on 29 January 2021.

The key changes that will take effect from 1 January 2021 are:



Section 113B

Introduction of **new penalty of between RM20,000 to RM100,000** for failure to submit TPD to the IRB on time.



Section 140A(3C)

Introduction of new surcharge of not more than **5% on TP adjustments** made during a TP audit. TP adjustments are adjustments made to transfer prices between related parties which the IRB does not consider to be at arms’ length.



Updated para 11.2.3 and 11.3.5 of MTPG

Period to submit TPD to IRB has been shortened from 30 days to **14 days**, and circumstances where no penalty is imposed by the IRB.



Section 140A(3A) & (3B)

The IRB is empowered to **disregard the structure** in a controlled transaction and make TP adjustments to the structure that the IRB thinks fit.

Effective from 1.1.2021

New Updates	Details	Implications								
<p>[Section 113B] Penalty for failure to submit TPD to the IRB on time</p>	<p>Where there is a prosecution and on conviction – a taxpayer is liable to a fine of between RM20,000 and RM100,000 or to imprisonment for a term up to 6 months, or both.</p> <p>Where there is no prosecution – a taxpayer may be imposed a penalty of between RM20,000 and RM100,000.</p>	<p>TPD is made mandatory for companies undertaking related party transactions (also known as "controlled transactions"). The TPD must be contemporaneous (i.e. up-to-date) and penalties shall be imposed if a taxpayer fails to furnish the contemporaneous TPD in a timely manner upon request by the IRB.</p>								
<p>[Paragraph 11.2.3 of MTPG] Timeline for submission of TPD to the IRB upon request</p>	<p>Period to submit the TPD to the IRB has been shortened from 30 days to 14 days. This requirement will apply to TP audit cases which commence on or after 1.1.2021.</p>	<p>Taxpayers who fail to submit the TPD to the IRB within 14 days upon request will be penalised under Section 113B which carries penalties of between RM20,000 and RM100,000.</p>								
<p>[Paragraph 11.3.5 of MTPG] Cases where no penalty will be imposed by the IRB during a TP audit</p>	<p>Penalties under Section 113B and/or Section 113(2) will not be imposed in cases, where:</p> <table border="1" data-bbox="670 1043 1559 1253"> <thead> <tr> <th data-bbox="670 1043 970 1129">Commencement of TP audit cases</th> <th data-bbox="970 1043 1217 1129">Submission of TPD to the IRB</th> <th data-bbox="1217 1043 1559 1129">TPD compliance</th> </tr> </thead> <tbody> <tr> <td data-bbox="670 1129 970 1193">Prior to 1.1.2021</td> <td data-bbox="970 1129 1217 1193">Within 30 days</td> <td data-bbox="1217 1129 1559 1193" rowspan="2">TPD fulfils the requirements of the TP Rules and MTPG.</td> </tr> <tr> <td data-bbox="670 1193 970 1253">On or after 1.1.2021</td> <td data-bbox="970 1193 1217 1253">Within 14 days</td> </tr> </tbody> </table>	Commencement of TP audit cases	Submission of TPD to the IRB	TPD compliance	Prior to 1.1.2021	Within 30 days	TPD fulfils the requirements of the TP Rules and MTPG.	On or after 1.1.2021	Within 14 days	<p>To avoid penalties being imposed, taxpayers must comply with the TPD requirements strictly, including:</p> <ul style="list-style-type: none"> • Preparation of contemporaneous TPD; • TPD is of good quality in accordance with the IRB's MTPG; • Upon request by the IRB, to submit the TPD to the IRB within 14 days (for TP audits that commenced from 1.1.2021 onwards).
Commencement of TP audit cases	Submission of TPD to the IRB	TPD compliance								
Prior to 1.1.2021	Within 30 days	TPD fulfils the requirements of the TP Rules and MTPG.								
On or after 1.1.2021	Within 14 days									

Effective from 1.1.2021 (cont'd)

New Updates	Details	Implications
<p>[Section 140A(3C)] Surcharge on TP adjustments made during a TP audit</p>	<p>Surcharge may range from 0% to 5% on the amount of increase of income or reduction of tax deduction, arising from TP adjustments.</p>	<p>The surcharge is imposed on the amount of TP adjustment, not on the additional tax liability. Hence, non-taxable entities that are enjoying tax incentives, having tax losses, etc. have higher TP risk as compared to the years before 1 January 2021.</p>
<p>[Section 140A(3A) & (3B)] Power to disregard a structure in a controlled transaction and make TP adjustments to a structure that the IRB thinks fit</p>	<p>The IRB can make appropriate TP adjustments if it is of the view that:</p> <ol style="list-style-type: none"> a. The economic substance of a controlled transaction differs from its form; or b. The controlled transaction differs from commercially acceptable transactions undertaken by independent parties. 	<p>Business structure adopted by taxpayers which are related to each other may be scrutinized by the IRB from the commercial perspective. If the resulting controlled transactions do not reflect commercial reality, the IRB may recharacterize the transaction and make appropriate TP adjustments it thinks fit.</p>

Example

Calculations of the

- New Surcharge under Section 140A(3C)
- New Penalty under Section 113B

Parent Co
(Singapore)



Subsidiary Co
(Malaysia)



- Loss Making
- No TPD prepared

IRB's TP audit:

- TP adjustment of **RM5 mil**
- However, the company has **no** additional tax payable as it is in a tax loss position even after the TP adjustment

	Section	Penalty Regime	Surcharge or penalty
Previous regime	No provision in the law to impose surcharge or penalty for loss making entities	N/A	NIL
From 1.1.2021 onwards	S140A(3C) – Surcharge on TP adjustment	Surcharge at up to 5%	Up to RM250k
	S113B(4) – Failure to furnish TPD	Between RM20k and 100k	Up to RM100k

WHO is liable to prepare a TPD?

- Companies that undertake the controlled transactions (i.e. sales and purchases of goods, provision of services, intra-group financing arrangements and use of intangible properties).
- A **Full TPD** is required when a company has:-
 - Annual gross income **exceeding RM25 mil** and total related party transactions **exceeding RM15 mil** per annum; or
 - Provision of financial assistance exceeding **RM50 mil** for non-financial institutions.
- Otherwise, taxpayers that fall below the thresholds may opt to prepare a **Limited TPD**.



WHEN to prepare a TPD?

A TPD should be prepared and is regarded as **contemporaneous** under the following circumstances:

- At the time a person is developing or implementing any controlled transaction; and
- Annual review of the existing TPD prior to the due date for filing of tax return (i.e. Form C) for a year of assessment.

Example:

Year	Year of Assessment	TPD compliance
Year 1	2019	Preparation of a TPD with a new benchmarking analysis
Year 2	2020	Preparation of financial update of the benchmarking analysis
Year 3	2021	Preparation of financial update of the benchmarking analysis
Year 4	2022	Update of full set of TPD with a new search of benchmarking analysis

- The information contained in the TPD, in particular, the financial data and suitability of the comparable companies (entities which are used for comparison purposes in a TP study) should be **reviewed and updated every year** in order to apply the arm's length principle reliably.
- In addition, a company is required to update the full set of TPD together with a fresh search of the comparable companies through a benchmarking study **every three (3) years**.

HOW to prepare a TPD?

- A good quality TPD that complies with the MTPG shall include the following contents:

Contents of Documentation	Full TPD	Limited TPD
Group Overview / Company Background	√	√
Controlled Transactions	√	√
Pricing Policies <ul style="list-style-type: none"> • Includes a comparability study to ensure the correctness of arm's length prices 	√	√
Industry Analysis	√	×
FAR Analysis (Functions, Assets and Risks)	√	×
Selection and application of TP Method	√	×
Benchmarking Analysis	√	×
Financial Analysis	√	×



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