

FREQUENTLY ASKED QUESTIONS (FAQ) ON MATTERS ARISING FROM SECTION 140A(3C) OF THE INCOME TAX ACT 1967

Topic/ Issues	Questions	Answers
<p>Clarification on Surcharge Imposition for Loss Cases and Tax-Exempt Cases</p>	<p>1) We seek clarification on the rationale for imposing a surcharge on loss cases or tax-exempt cases as there is no loss of tax revenue in such cases.</p>	<p>1) A surcharge is imposed on a Transfer Pricing (TP) adjustment made under Section 140A of the Income Tax Act 1967 (ITA) which results in an increase in income or a reduction of any deduction or loss. When any taxpayer does not comply with the arm's length principles, a surcharge will be imposed on that adjustment regardless of whether the taxpayer is in a loss position or a tax-exempt company.</p> <p>This new move is to ensure equal tax treatment for all taxpayers that fail to comply with the arm's length principle required under section 140A of the ITA regardless of whether the TP adjustment made will result in an assessment/ additional assessment or not.</p> <p>Besides, this move is also to encourage compliance with TP legal framework after more than 10 years of its introduction in Malaysia.</p> <p>In a case where no TP adjustment is made in any year of assessment (YA) that is audited, no surcharge under Subsection 140A(3C) will be imposed for that YA.</p>

Topic/ Issues	Questions	Answers
Implementation of surcharge under Subsection 140A(3C)	<p>2) Based on the Finance Act 2020 (Act 831), subsection 140A(3C) is comes into operation from 1 January 2021. Kindly clarify how would the subsection applies in the following scenarios: -</p> <p>a) TP audit commenced after 1 January 2021 for the YAs covering prior to financial year 2021.</p> <p>b) On-going TP audit initiated prior to 1 January 2021 but concluded on or after 1 January 2021.</p>	<p>2a. Subsections 140A(3C) will only be applicable for TP audit cases that commence on or after 1.1.2021 regardless of the YAs covered in those audit exercises.</p> <p>2b. For audit cases that have been initiated prior to 1 January 2021, Subsection 140A(3C) will not be applicable, even if the audit exercise is concluded after 1 January 2021. However, if that audit resulted in a tax undercharge, the penalty under subsection 113(2) of the ITA will still apply.</p>
Mutual Exclusivity: Surcharge under Subsection 140A(3C) vs Penalty under subsection.113(2) of the ITA	<p>3) In the event there is a tax undercharge arising from a TP adjustment, please confirm whether both the surcharge and the penalty under subsection 113(2) of the ITA can be imposed:</p>	<p>IRBM confirms that the surcharge is mutually exclusive with the penalty under subsection 113(2) of the ITA. Therefore, IRBM will only impose a surcharge on any TP adjustments made under Section 140A of the ITA.</p>

Topic/ Issues	Questions	Answers
<p data-bbox="165 284 687 379">Applicability of Subsection 140A(3C) of the ITA to Companies with Tax incentives</p> <p data-bbox="165 850 383 879">Rights of Appeal</p>	<p data-bbox="714 284 1352 515">4) Is Subsection.140A(3C) of the ITA applicable to incentivise companies with 100% tax exemption? If it is applicable, the foreign direct investments (FDI) would be exposed to the risk of surcharge arising from TP adjustments which may adversely affect investors' confidence.</p> <p data-bbox="714 836 1352 999">5) Based on Subsection140A(3D) of the ITA, the surcharge shall not be treated as tax payable for the purposes of any provision of this Act except for sections 103 to 106 of the ITA.</p> <p data-bbox="775 1038 1391 1137">If taxpayers are aggrieved with the surcharge imposed, are they eligible to appeal the surcharge?</p> <p data-bbox="775 1190 786 1203">.</p>	<p data-bbox="1431 284 2069 448">In any controlled transactions, compliance with the arm's length principle is vital. Thus, any non-compliance will result in a TP adjustment which attract the imposition of a surcharge under Subsection 140A(3C) of the ITA.</p> <p data-bbox="1431 472 2069 700">A surcharge is imposed on the TP adjustment and not on the tax undercharge. As long as the audit findings warrant a TP adjustment, it doesn't matter if the company has been approved for a full tax exemption or a partial tax exemption. Therefore, even incentivise companies are exposed to the surcharge if there is any TP adjustment.</p> <p data-bbox="1431 831 2069 1059">Taxpayers who are aggrieved with the surcharge imposed can appeal to the DG for a reduction. Subsection 124(3) of the ITA has given power to the DG to abate or remit any surcharge imposed on a case-to-case basis, provided that the taxpayers have submitted reasonable justification on the appeal.</p> <p data-bbox="1431 1099 2069 1264">Since the appeal processes under Section 99 of the ITA are not applicable to surcharges, the taxpayer may make a written appeal application with justification to the LHDN offices handling their tax file.</p> <p data-bbox="1503 1326 1514 1345">+</p>

Topic/ Issues	Questions	Answers
<p>Factors in determining the surcharge rate</p>	<p>6) Please provide guidance on how the scale of the surcharge of up to 5% under Subsection 140A(3C) of the ITA will be determined. It is suggested that the criteria to be considered include the comprehensiveness and completeness of TP documentation and the degree of deviation from the arm's length range.</p> <p>7) Please confirm that the surcharge will be adjusted in line with any adjustment under a Mutual Agreement Procedure ("MAP").</p> <p>8) Kindly confirm that the surcharge applies regardless of which IRBM branch is conducting the tax audit. There are cases where the IRB branch refuses to follow the TP Guidelines because it is not a TP branch but nevertheless makes TP adjustments.</p>	<p>The general rate to be applied in imposing the surcharge is 5% on the TP adjustment made under Section 140A of the ITA. There will be no scale available as a reference. However, a lower surcharge rate will be offered for voluntary disclosure cases. Further details will be incorporated in the amended Transfer Pricing Audit Framework (TPAF).</p> <p>The surcharge rate is imposed on the amount of the TP adjustment. If there is any adjustment to be made under the MAP, the amount of the surcharge for that case will also be adjusted..</p> <p>Effective 1 January 2021, any audit conducted by IRBM branches that resulted in a TP adjustment under Section 140A of the ITA will be subject to a surcharge of not more than 5% under Subsection 140A(3C) of the ITA. All IRBM branches should follow the processes and procedures as determined under the Malaysia Transfer Pricing (MTPGL) and Transfer Pricing Tax Audit Framework.</p>