



Case study

EarthCo Sdn. Bhd. (EarthCo) is a privately-owned agriculture company incorporated in Malaysia. The company operates in three key divisions: (1) developing new varieties of core agricultural products (e.g., tea and cocoa) that are more robust (e.g., being drought tolerant) to the impacts of climate change via genetic engineering (2) developing eco-friendly pesticides and fertilizers using adjacent technologies, and (3) working with farmers to develop more sustainable agricultural practices.

EarthCo has a core team of scientists based in Malaysia, who leads a global network of both direct employees as well as independent contractors. EarthCo maintains a large secondary research team in Country X as well as additional smaller teams with local expertise in Countries Y and Z. The research leaders (leading the team of scientists) from Malaysia make frequent trips to all these other research facilities but most frequently to Country X's facility which includes a laboratory and farms owned by EarthCo.

Whilst growth has been strong in recent years, the company has struggled with its supply chain. EarthCo has struggled to find reliable third-party logistics solutions to deliver its products to its global customers. Increasing prices, inconsistent reliability and long delays have all had negative impacts on profits as well as brand reputation.

The Chief Financial Officer (CFO) of EarthCo has asked you to help them with a feasibility study on how best to overcome their recent supply chain issues. The company's management team is considering building an in-house logistics and warehousing function. EarthCo's management team likes the idea of having complete control over the cost structure, and building the function out of a new internal organization. However, they have also had informal discussions with a few mid-sized logistics companies that may be open to acquisition. Given these two potential routes to addressing their supply chain issues, the management team is keen to understand all the associated tax impacts that would come with such a change. That said, while your focus is on tax, you have also been asked to consider non-tax related matters that may impact the planning for EarthCo's new logistics unit.

Other information

- ▶ The company does not grow any of its own food products. Instead, it works with unrelated farmers to grow the EarthCo developed varieties which are then purchased by EarthCo. EarthCo currently uses third party logistics companies for transport and warehousing but is considering developing in-house logistics as they are facing substantial fee increases in shipping and warehousing.



- ▶ EarthCo primarily sells its products to third party retailers in major markets across the world.
- ▶ The company has substantial sales to countries without tax treaties with Malaysia and is trying to navigate what impact the current and future operating models may have on withholding tax implications.
- ▶ The company has expressed an interest in basing their new logistics team in Country A due to its central location to the countries where they work with the largest number of farms. However, EarthCo currently does not have any operations in Country A. While the actual number of employees in Country A may be quite small, they will own substantial fixed assets in Country A.
- ▶ The company's growth has been driven by substantial R&D investment and so, while revenues are strong, margins are relatively small. As a result, the company is mindful that investing in an internal logistics organization may result in net operations losses in the near term.
- ▶ Both potential acquisition targets have long-term contracts with other customers that would have to be honoured, as well as geographical footprints far beyond EarthCo's.
- ▶ The CFO has also read about the changes in the international tax and regulatory landscape. She indicates that she does not have a full grasp of them. She does not understand the OECD Base Erosion Profit Shifting (BEPS) model and the emphasis on BEPS 2.0. She would like to understand what the impact is and the most relevant matters to focus on.

Requirement:

The CFO of EarthCo has requested for a meeting with you to discuss the issues raised.

Prepare a presentation on the issues raised by the CFO, covering:

- a) The specific matters on which the CFO would like your advice
- b) Any other matters which you think are relevant
- c) How Young Tax Professionals (YTPs) may be able to help



EY | Building a better working world

EY exists to build a better working world, helping create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation are available via ey.com/privacy. EY member firms do not practice law where prohibited by local laws. For more information about our organization, please visit ey.com.

© 2023 Ernst & Young Tax Consultants Sdn. Bhd.
All Rights Reserved.

APAC no. 07009914
ED None.

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, legal or other professional advice. Please refer to your advisors for specific advice.

ey.com/en_my