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## EY Tax Alert (Special Edition)

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# Foreign-sourced income (FSI) exemption orders gazetted

### Coverage of this Alert

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- ▶ Key points of Income Tax (Exemption) (No. 5) Order 2022, which applies to all sources of income of individuals
- ▶ Key points of Income Tax (Exemption) (No. 6) Order 2022, which applies to the dividend income of companies, limited liability partnerships (LLPs) and individuals earning dividend income in relation to a partnership business

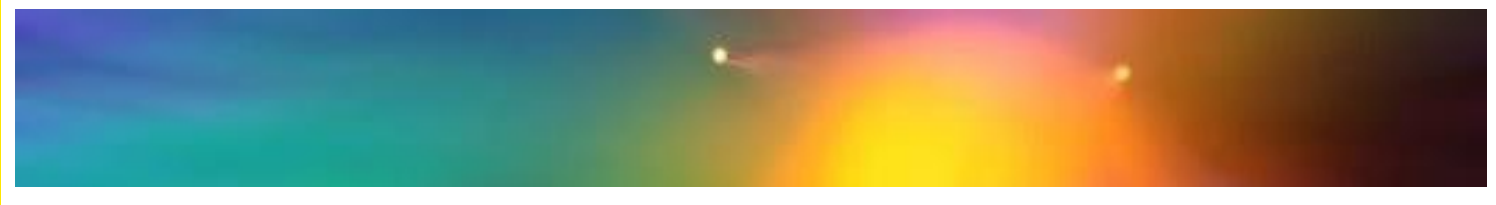
Pursuant to the Finance Act 2021, the income tax exemption on FSI received by any person (other than a resident company carrying on the business of banking, insurance or sea or air transport) was removed for all Malaysian-resident taxpayers from 1 January 2022. A flat income tax rate of 3% would apply on the gross amount of FSI received in Malaysia from 1 January 2022 to 30 June 2022. From 1 July 2022 onwards, the prevailing tax rate of the taxpayer would apply.

As highlighted in an earlier alert, on 30 December 2021, the Ministry of Finance (MoF) issued a press release stating that certain types of FSI of resident taxpayers will continue to be exempt from tax, subject to conditions (see *Special Tax Alert No. 1/2022*). To legislate the above, the following Orders were gazetted on 19 July 2022 and are effective from 1 January 2022 to 31 December 2026:

- ▶ Income Tax (Exemption) (No. 5) Order 2022 [P.U.(A) 234]
- ▶ Income Tax (Exemption) (No. 6) Order 2022 [P.U.(A) 235]

Both Orders provide that:

- ▶ “Income received in Malaysia from outside Malaysia” means income arising from outside Malaysia which is brought into Malaysia.
- ▶ Any deduction in relation to the exempted FSI shall be disregarded for the purpose of ascertaining the chargeable income of the qualifying individual / person
- ▶ The exemption granted does not absolve the qualifying individual / person from any requirement to submit any return, statement of accounts or any other information as required under the Income Tax Act 1967 (ITA)



## **Key points of Income Tax (Exemption) (No. 5) Order 2022, which applies to all sources of income of individuals**

The Order exempts a qualifying individual<sup>1</sup> from the payment of income tax in respect of gross income from all sources of income under Section 4<sup>2</sup> of the ITA (excluding income from a partnership business in Malaysia) which is received in Malaysia from outside Malaysia.

The exemption is on condition that the FSI has been subjected to tax “of a similar character to income tax” under the laws of the foreign jurisdiction where the income arose. To satisfy this condition, the qualifying individual is required to comply with conditions imposed by the MoF, which will be specified in guidelines to be issued in due course by the Inland Revenue Board (IRB).

## **Key points of Income Tax (Exemption) (No. 6) Order 2022, which applies to the dividend income of companies, limited liability partnerships (LLPs) and individuals earning dividend income in relation to a partnership business**

The Order exempts a “qualifying person” from the payment of income tax in respect of dividend income which is received in Malaysia from outside Malaysia.

“Qualifying person” in this context means a person resident in Malaysia who is:

- (a) An individual who has dividend income received in Malaysia from outside Malaysia in relation to a partnership business in Malaysia,
- (b) An LLP which is registered under the Limited Liability Partnerships Act 2012, or
- (c) A company which is incorporated or registered under the Companies Act 2016

The exemption available to the “qualifying person” is subject to the following conditions:

- ▶ The dividend income has been subjected to tax “of a similar character to income tax” under the laws of the foreign jurisdiction where the income arose, and
- ▶ The highest rate of tax “of a similar character to income tax” charged under the laws of the foreign jurisdiction where the income arose was not less than 15%.

Similarly, to satisfy the above conditions, the qualifying person is required to comply with the conditions imposed by the MoF which will be specified in guidelines to be issued by the IRB. Further guidance is also

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<sup>1</sup> “Qualifying individual” means an individual resident in Malaysia who has income received in Malaysia from outside Malaysia.

<sup>2</sup> The sources of income under Section 4 of the ITA refer to:

- (a) Gains or profits from a business, for whatever period of time carried on
- (b) Gains or profits from an employment
- (c) Dividends, interest or discounts
- (d) Rents, royalties or premiums
- (e) Pensions, annuities or other periodical payments not falling under any of those listed above
- (f) Gains or profits not falling under any of those listed above

expected on whether the 15% tax rate mentioned above refers to the prevailing tax rate in the foreign jurisdiction at the time the dividend was declared, at the time the dividend is received in Malaysia or at some other date.

It is noted that the above definition of “qualifying person” does not appear to include, for example, a unit trust or a company which is incorporated under the Labuan Companies Act 1990 which has elected to be taxed under the ITA, which means that such taxpayers would technically not qualify for the exemption. Further clarification will be sought from the authorities in this regard. It is also possible that further details will be made available in the IRB’s guidelines.

The Order also stipulates that the exemption will not apply to a person carrying on the business of banking, insurance or sea or air transport.

## Contact details

### Principal Tax

**Yeo Eng Ping (EY Asia-Pacific Tax Leader)**

eng-ping.yeo@my.ey.com

+603 7495 8288

**Amarjeet Singh (EY Asean Tax Leader)**

amarjeet.singh@my.ey.com

+603 7495 8383

**Farah Rosley (Malaysia Tax Leader and Malaysia Global Compliance and Reporting Leader)**

farah.rosley@my.ey.com

+603 7495 8254

### People Advisory Services

**Tan Lay Keng (EY Asia-Pacific People Advisory Services Leader)**

lay-keng.tan@my.ey.com

+603 7495 8283

**Christopher Lim (EY Asean Immigration Leader and Malaysia People Advisory Services Leader)**

christopher.lim@my.ey.com

+603 7495 8378

**Irene Ang**

irene.ang@my.ey.com

+603 7495 8306

### Business Tax Services

**Robert Yoon (EY Asia-Pacific Fixed Assets Services Leader)**

*(based in Johor)*

robert.yoon@my.ey.com

+603 7495 8332

**Wong Chow Yang**

chow-yang.wong@my.ey.com

+603 7495 8349

**Bernard Yap**

bernard.yap@my.ey.com

+603 7495 8291

**Chan Vai Fong**

vai-fong.chan@my.ey.com

+603 7495 8317

**Chua Siong Chee**

siong-chee.chua@my.ey.com

+603 7495 8410

### Global Compliance and Reporting

**Julian Wong (EY Asean Global Compliance and Reporting Leader and EY Asean Managed Services Leader)**

julian.wong@my.ey.com

+603 7495 8347

**Farah Rosley (Malaysia Tax Leader and Malaysia Global Compliance and Reporting Leader)**

farah.rosley@my.ey.com

+603 7495 8254

**Janice Wong (EY Asean Japan Business Services (JBS) Tax Leader)**

janice.wong@my.ey.com

+603 7495 8223

**Asaithamby Perumal**

asaithamby.perumal@my.ey.com

+603 7495 8248

**Julie Thong**

julie.thong@my.ey.com

+603 7495 8415

**Liew Ai Leng**

ai-leng.liew@my.ey.com

+603 7495 8308

**Linda Kuang**

*(based in Kuching)*

linda.kuang@my.ey.com

+6082 752 660

**Mark Liow**

*(based in Penang)*

mark.liow@my.ey.com

+604 688 1899

**Jaclyn Tan (Payroll Operate Services)**

jaclyn.tan@my.ey.com

+603 7495 8404

## Contact details

### International Tax and Transaction Services

**Yeo Eng Ping**

eng-ping.yeo@my.ey.com  
+603 7495 8288

**Amarjeet Singh**

amarjeet.singh@my.ey.com  
+603 7495 8383

**Sockalingam Murugesan (EY Asean Transfer Pricing Leader and Malaysia Transfer Pricing Leader)**

sockalingam.murugesan@my.ey.com  
+603 7495 8224

**Anil Kumar Puri**

anil-kumar.puri@my.ey.com  
+603 7495 8413

**Andrew Loh**

andrew.loh@my.ey.com  
+603 7495 8313

**Chua Meng Hui**

*(based in Kota Kinabalu)*  
meng-hui.chua@my.ey.com  
+603 7495 8261

**Sharon Yong**

sharon.yong@my.ey.com  
+603 7495 8478

**Derek Chan**

derek.chan@my.ey.com  
+603 7495 8336

**Florence Tan**

florence.tan@my.ey.com  
+603 7495 8585

**Shalini R Chandrarajah**

shalini.chandrarajah@my.ey.com  
+603 7495 8281

### International Tax and Transaction Services (cont'd)

**Gary Ling (Transfer Pricing)**

gary.ling@my.ey.com  
+603 7495 8388

**Hisham Halim (Transfer Pricing)**

hisham.halim@my.ey.com  
+603 7495 8536

**Vinay Nichani (Transfer Pricing)**

vinay.nichani@my.ey.com  
+603 7495 8433

### Indirect Tax

**Yeoh Cheng Guan**

cheng-guan.yeoh@my.ey.com  
+603 7495 8408

**Aaron Bromley**

aaron.bromley@my.ey.com  
+603 7495 8314

**Jalbir Singh Riar**

jalbir.singh-riar@my.ey.com  
+603 7495 8329

### Financial Services

**Koh Leh Kien**

leh-kien.koh@my.ey.com  
+603 7495 8221

**Bernard Yap**

bernard.yap@my.ey.com  
+603 7495 8291

**Gary Ling (Transfer Pricing)**

gary.ling@my.ey.com  
+603 7495 8388

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