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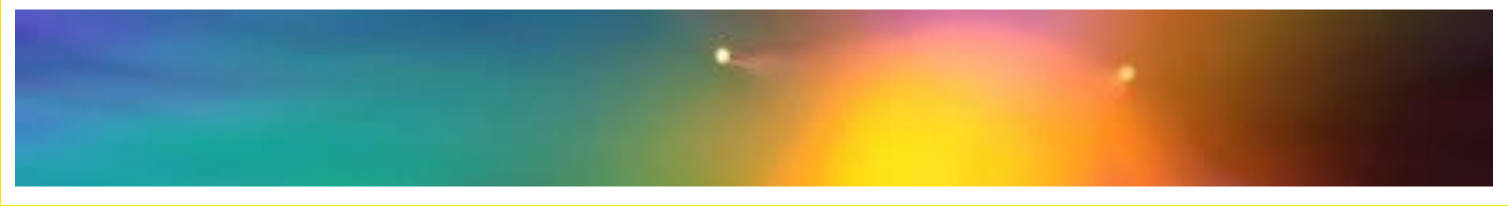
Malaysian developments

Practice Note No. 2/2020: Claiming capital allowance on the development cost for customized computer software under the Income Tax Rules 2019

In Budget 2018, the Government proposed that expenditure incurred on consultation fees, licensing and incidental fees for the development of customized software would qualify for capital allowance (CA) claims, effective from the year of assessment (YA) 2018 (see *Special Tax Alert: Highlights of 2018 Budget – Part I*).

The proposal was subsequently legislated via the Income Tax (Capital Allowance) (Development Cost for Customised Computer Software) Rules 2019 [P.U.(A) 274] ("Rules"). The Rules provide that a Malaysian resident who has incurred development cost for customized computer software (i.e. consultation fee, payment for rights of software ownership and incidental fee relating to the development of customized computer software) in the basis period for a YA would qualify for CA claims at the rate of 20% initial allowance (IA) and 20% annual allowance (AA), from YA 2018 (see *Tax Alert No. 19/2019*).



The Inland Revenue Board (IRB) has now issued a two-page Practice Note No. 2/2020 (PN) dated 16 March 2020, titled "Claiming Capital Allowance on the Development Cost for Customised Computer Software under the Income Tax Rules 2019" to provide further guidance on the application of the Rules.

The PN clarifies that the "development cost for customized computer software" refers to expenditure incurred in the production of new software or the improvement of existing software, used for business purposes. The costs consist of the following:

(a) Consultation fees*

Consultation fees incurred for the development of software specifically for the purpose of developing a new software system, as well as modification or modernization of existing software. Consultation fees related to the initial procedure or planning stages (e.g. feasibility study or preliminary study) are excluded and will not qualify for capital allowances.

(b) Payments for the rights of software ownership*

Payments for the right to use the software exclusively

(c) Incidental fees*

Payments incurred to enable the use of the software in the business and are capitalized (e.g. costs relating to changes / updates to software requirements)

*The PN highlights that these payments to non-residents may be subject to withholding tax under Section 109 or 109B of the Income Tax Act 1967 (ITA), depending on the relevant facts.

In addition to the above, the PN stipulates that CA can be claimed from the YA in which the customized computer software is capable of being used for the purpose of the business.

The following examples have been provided in the PN:

YA the development cost is incurred	YA the customized computer software is capable of being used in business	Tax treatment
Example 1 2018, 2019 and 2020	2020	▸ Cost incurred from YA 2018 is qualifying expenditure. ▸ CA can be claimed from YA 2020.
Example 2 2017, 2018 and 2019	2019	▸ Cost incurred from YA 2018 is qualifying expenditure. ▸ Cost incurred before YA 2018 is disregarded. ▸ CA can be claimed from YA 2019.
Example 3 2017 and 2018	2018	▸ Cost incurred from YA 2018 is qualifying expenditure. ▸ CA can be claimed from YA 2018.

Income tax exemption on income of religious institutions or organizations registered as a Company Limited by Guarantee

Currently, income tax exemption is given for all income received by religious institutions or organizations established for the purpose of religious worship or the advancement of religion and registered under the Registrar of Societies Malaysia, pursuant to Income Tax (Exemption) Order 2017 [P.U. (A) 52].

In Budget 2020, it was proposed that the same tax exemption be extended to religious institutions or organizations registered as a Company Limited by Guarantee with the Companies Commission of Malaysia.

To legislate this proposal, the Income Tax (Exemption) Order 2020 [P.U.(A) 139] was gazetted on 4 May 2020. The Order provides a 100% income tax exemption on all sources of income of a religious institution or organization (defined below) for a specific period, subject to the adherence to the conditions imposed by the Minister.

A "religious institution or organization" is defined to mean a religious institution or organization operating a place of worship and:

(a) Is a company limited by guarantee and incorporated under the Companies Act 2016;
(b) Is a Malaysian resident;
(c) Its objective is exclusively for the purpose of religious worship or the advancement of religion; and
(d) Is not operated or conducted primarily for profit

The Order provides that the exemption granted does not absolve the religious institution or organization from any requirement to submit any return, statement of accounts or any information, required under the Income Tax Act 1967 (ITA).

Applications for an exemption under the Order can be made on or after 1 January 2020. The Order is effective from YA 2020.

Income tax exemption on medical tourism

A company that provides private healthcare facilities and services to a healthcare traveler (as defined) was previously given a tax exemption on its income. Such exemption was equivalent to an investment tax allowance of 100% of the qualifying capital expenditure incurred for a period of five (5) years. The incentive applied to applications received by the Malaysian Investment Development Authority (MIDA) between 1 January 2015 and 31 December 2017 and was given to new companies as well as existing ones engaged in expansion, modernization or refurbishment, subject to conditions (see *Tax Alert No. 16/2017*).

In Budget 2018, the Government proposed to extend this incentive for another three years, until 31 December 2020 (see *Special Tax Alert: Highlights of 2018 Budget – Part I*) subject to stricter conditions. Now, at least 10% (instead of the previous 5%) of a qualifying company's total number of patients per YA must be made up of healthcare travelers. Further, at least 10% (instead of the previous 5%) of the company's gross income for each YA must be derived from the healthcare travelers.

Following the above proposals, MIDA issued the following two guidelines dated 8 February 2018:

(a) Guideline on the application for tax incentive for the promotion of healthcare travel:
    I. New private healthcare facility
    II. Expansion / modernization / refurbishment of an existing private healthcare facility

(b) Guideline on the application for verification of plant / machinery / medical devices / other facilities used for the purpose of private healthcare facility promoting healthcare travel

The Income Tax (Exemption) (No. 2) Order 2020 [P.U. (A) 141] was gazetted on 5 May 2020 to legislate the above-mentioned proposals.

The Order provides an income tax exemption on the statutory income derived from a qualifying project carried on by a qualifying company. The amount of tax exempted shall be equal to the amount of qualifying capital expenditure incurred by the qualifying company. The exemption is for a period of five consecutive years commencing from the date that the qualifying company first incurs qualifying capital expenditure, as determined by MIDA, and shall not be earlier than 1 January 2018.

In addition, as highlighted above, the additional conditions set out in the Order are as follows:

- The number of health travelers who receive private healthcare services from the qualifying project must be at least 10% (previously 5%) of the total number of patients from the qualifying project for each YA; and
- At least 10% (previously 5%) of the gross income of the qualifying company from the qualifying project for each YA must be generated from the health travelers.

The Order is deemed to have come into operation from YA 2018, and applies to applications made to MIDA between 1 January 2018 and 31 December 2020.

Overseas developments

India extends Equalization Levy scope to cover e-commerce supplies or services

The Union Budget of India 2020 introduced an amendment to expand the scope of the Equalization Levy (EL) to cover consideration received by non-resident e-commerce operators (e-com EL) from specified transactions. The e-com EL provisions are effective from tax years commencing on or after 1 April 2020. The EL rate is 2% of consideration received or receivable by a non-resident e-commerce operator from specified transactions if such receipts exceed INR20 million (US$265,000) during the relevant tax year. While the e-com EL provisions are applicable from 1 April 2020, income of a non-resident e-commerce operator arising from a transaction which is subject to e-com EL is only exempt from income tax for tax years commencing on or after 1 April 2021.

Given the increasingly pervasive nature of digitalization, the wide scope of the e-com EL is likely to have an impact on a number of multinational enterprises (MNEs), irrespective of whether they are operating highly digitalized business models. The procedures relating to the collection and recovery of the e-com EL are expected to increase compliance obligations for non-resident e-commerce operators in India. Consequently, MNEs should undertake a detailed assessment of the impact of the e-com EL on their operating models and monitor their compliance obligations.

Detailed discussion

Background

Under Action 1 of the Organisation for Economic Co-operation and Development (OECD)'s Base Erosion and Profit Shifting (BEPS) Project (Addressing the

Tax Challenges of the Digital Economy), the OECD had considered, inter alia, an EL (i.e., a tax to equalize the tax positions of remote and domestic suppliers of similar goods and services) as an option for taxing digital transactions. While the Action 1 Report did not recommend introducing such a levy as an internationally agreed standard, it did state that countries could introduce a levy in their domestic laws as an additional safeguard against BEPS, provided existing treaty obligations were respected, or the levies were included in bilateral tax treaties. In India, the Finance Act, 2016 (FA 2016) introduced an EL with effect from 1 June 2016. The EL, as introduced by the FA 2016, is collected from the payer at 6% on the consideration received by non-residents for online advertisements and related services from specified persons (advertising EL).

The Union Budget 2020 expanded the scope of the EL to cover consideration received by non-resident e-commerce operators from specified transactions (the e-com EL), effective from tax years commencing on or after 1 April 2020. Whether the e-com EL is consistent with India's international obligations under existing tax treaties is not clear.

Key provisions of the e-com EL

The EL is levied on non-resident e-commerce operators at 2% of the consideration received or receivable for specified transactions.

An "e-commerce operator" is defined as a non-resident who owns, operates or manages digital or electronic facilities or platforms for the online sale of goods or online provision of services (or both).

"Specified transactions" are e-commerce supplies or services made or provided or facilitated by a non-resident e-commerce operator to any of the following:

- A person resident in India
- A non-resident to whom an advertisement, which targets an Indian resident customer or a customer who accesses the advertisement through an internet protocol (IP) address located in India, is sold
- A non-resident to whom data, collected from an Indian resident or from a person who uses an Indian IP address, is sold
- A person who buys such goods or services or both using an IP address located in India

Exclusions from the e-com EL

The e-com EL is not applicable if one of the following conditions is met:

- The non-resident e-commerce operator has a permanent establishment (PE) in India and the specified transaction is effectively connected to such a PE in India.
- The aggregate value of consideration for specified transactions does not exceed INR20 million.
- The advertising EL is levied.

Service or sales income of a non-resident which is otherwise taxable under the Indian tax laws (ITL) will be exempt from 1 April 2021 in the hands of the non-resident in India, if such income is subject to the e-com EL. Consequently, there appears to be a mismatch between the effective date of e-com EL provisions and the exemption provisions under the ITL.

Compliance obligations of the e-com EL

The e-com EL provisions introduce the following reporting and compliance obligations for non-resident e-commerce operators:

- Payment of the e-com EL on a quarterly basis by the applicable due dates
- Requirement to maintain and furnish annual statements in respect of all e-com EL levies on or before 30 June of the following Indian financial year

Failure to comply with the e-com EL provisions (such as the failure to deduct or pay the e-com EL) will attract interest, penalties and prosecution proceedings.

Unlike the advertising EL, the new levy imposes collection and other compliance obligations on the non-resident e-commerce operator and not on the payer of the consideration.

Implications

Since the release of the OECD Final Report on Action 1 of the BEPS Project in October 2015, India has considered various unilateral measures to address the broader tax challenges posed by the digitalization of the economy. The expansion of the EL by the FA 2020 to cover e-commerce supplies or services provided or facilitated by non-residents is another such measure.

The e-com EL amendment expands the scope of the EL significantly to cover a wide range of sale, service and facilitation transactions that are conducted online through a digital or electronic facility or platform by non-resident e-commerce operators, including advertisements targeting India or the sale of data collected from India. The provision is intended to target not only highly digitalized business models, but also a number of other MNEs that use technology to carry out sales and/or services. Given the increasingly pervasive nature of digitalization, a wide scope was enacted in an effort to respond to the broader impact of the digitalization of the economy. MNEs should assess in detail the implications of the e-com EL on their operating models and monitor their compliance obligations.

Inland Revenue Authority of Singapore (IRAS) – COVID-19 tax guidance and support measures for individuals and employers

Amidst the COVID-19 pandemic crisis, employers with a globally mobile workforce have had to make swift decisions for the well-being and safety of their employees. These include measures to recall Singaporean and Singapore Permanent Resident (SPR) employees currently exercising employment overseas to return to Singapore, following which they will be directed to work remotely from Singapore for their overseas employer.

Another affected group of employees is non-residents foreigners who were meant to be in Singapore on short-term assignment but who have been unable to leave Singapore due to the COVID-19 situation. Such employees remain in Singapore to work remotely for their overseas employer.

To further support employers with a globally mobile workforce, the IRAS granted a number of tax relief measures on 6 April 2020. These have been summarized in the table set out in Appendix 1.

Of particular note, the IRAS announced various tax deferral payment options spanning up to three months in respect of the YA 2020 tax liability and extended the deadline for the lodgement of YA 2020 income tax returns to 31 May 2020.

EY's views

The tax measures announced are indeed unprecedented and provide relief and clarity to employers.

However, it is important to note that with the COVID-19 situation evolving swiftly, the IRAS has yet to release any administrative guidelines on whether an application needs to be made by the employer and/or employee for the tax exemption measures to apply in respect of the employees working in Singapore remotely for their overseas employers. Hence, it is expected that there will be further measures and guidance released by the IRAS in due course on these matters, especially for employees based in Singapore who are required to work from home and who receive reimbursements from their employers for expenses incurred due to the work-from-home arrangement.

Next steps

Employers who have employees working remotely in Singapore temporarily due to the COVID-19 situation should review their mobility policy or employment terms to ensure that their documentation for the affected employees is clear and can meet the qualifying conditions for the tax exemption.

Unprecedented tax measures in support of employers with a global mobility workforce

	General tax treatment	Tax relief granted under COVID-19 measures
Singaporean / SPR employees exercising overseas employment and now working remotely from Singapore for that employment	Income attributable to the employment days in Singapore would be regarded to be sourced in Singapore and subject to tax for a tax resident employee, unless the employee qualifies for a tax exemption under a tax treaty or elects to be a non-resident and claims an exemption under the 60-day exemption rule. Under the 60-day exemption rule, a non-resident employee (excluding a director, public entertainer or an independent consultant) will be exempt from tax if he/she exercises employment in Singapore for a total of 60 days or less in a calendar year. In counting the employment days in Singapore, the total period inclusive of the date of arrival and the date of departure for each business trip to Singapore will need to be considered.	The days during which the employee works remotely in Singapore for the overseas employer will not be considered as employment days in Singapore for the period from the date of return to Singapore up to 30 September 2020*, provided that the following conditions are met: 1. There are no changes in the contractual terms governing the employment overseas before and after the employee's return to Singapore; and 2. This is a temporary work arrangement due to the COVID-19 situation. If all the conditions are met, the employment income for the period of stay in Singapore up to 30 September 2020* will not be taxed in Singapore. If any of the conditions are not met, the tax rules outlined under the "General tax treatment" column will apply to determine the taxation of income for the period of stay in Singapore. *This date is subject to review as the COVID-19 situation evolves.
Non-resident foreigners who are on short-term assignment in Singapore and are unable to leave Singapore due to the COVID-19 situation	Income attributable to short-term assignment and the extended period of stay in Singapore would be regarded to be sourced in Singapore and subject to tax unless the employee qualifies for tax exemption under a tax treaty or claims an exemption under the 60-day exemption rule. Otherwise, if the employee's aggregated days in Singapore exceed the 60-day mark but are less than 183 days in a calendar year, employment income becomes taxable at the non-resident flat rate of 15% or the resident progressive rates, whichever is higher.	The extended stay in Singapore after the end of the short-term assignment will not be regarded as employment days in Singapore if the following conditions are met: 1. The period of the employee's extended period of stay is for a period of not more than 60 days; and 2. The work done during the extended stay is not connected to the Singapore assignment and would have been performed overseas if not for the COVID-19 situation. If the conditions are met, the income attributable to the period of extended stay in Singapore will not be taxed. If any of the conditions are not met, the tax rules outlined under "General tax treatment" will apply to determine the taxation of income for the

	In counting the employment days in Singapore in a calendar year, both the period of short-term assignment and the extended period of stay in Singapore falling in the same calendar year will be included in the count.	period of the extended stay. In addition, the tax rules will apply as per normal in respect of the income earned during the short-term assignment period.
Deferral payment option	Lump sum payment: Tax liability must be settled within 30 days from the date of the tax notice. 12-month interest-free instalment (GIRO) payment: The instalment cycle will run from May 2020 to April 2021.	Lump sum payment: Due date for tax payments in May, June and July 2020 will be deferred by three (3) months. For example, if the current due date for tax payment is 15 May 2020, tax payment will be deferred to 15 August 2020. GIRO: The instalment cycle will run from August 2020 to July 2021. Application for tax deferral needs to be submitted by 31 July 2020. Once the request is approved by the IRAS, the deferral will supersede the current payment due date or GIRO arrangement. Any individual who needs additional help with tax payment due to financial difficulties can write to the IRAS for special consideration.
Tax filing deadline	15 April (hardcopy filing) or 18 April (electronic filing)	Both will be extended until 31 May 2020. This is inclusive of the filing of the Not Ordinarily Resident (NOR) scheme application forms for applicable individuals.
Tax clearance for foreign employees in April 2020	Tax clearance (Form IR21) needs to be filed with the IRAS at least one month before the cessation date or departure date, whichever is earlier. The employer is required to withhold all monies due and payable to the employee and cannot release the monies to the employee until the employer receives notification from the IRAS or after one month from the filing of the Form IR21.	Employers who are required to seek tax clearance for their employees in the month of April will be given one month's extension to file the Form IR21. The current requirement for employers to withhold monies and release monies upon receipt of IRAS notification or after one month from filing of the Form IR21 remains.

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Important dates

Note: Please see EY Special Tax Alert No. 11/2020 for information on the grace periods which have been provided to help businesses cope with the Movement Control Order.

15 May 2020	Due date for monthly instalments. As a concession, this deadline is extended to 31 May 2020 pursuant to the IRB's "Frequently Asked Questions on Tax Matters during the MCO Period (18 March 2020 to 12 May 2020)" document ("FAQ document") dated 6 May 2020
31 May 2020	6th month revision of tax estimates for companies with November year-end
31 May 2020	9th month revision of tax estimates for companies with August year-end
31 May 2020	Statutory deadline for filing of 2019 tax returns for companies with October year-end. As a concession, this deadline is extended to 31 August pursuant to the Return Form (RF) Filing Programme for the Year 2020 (Amendment 3/2020) ("updated RF Filing Programme").
15 June 2020	Due date for monthly instalments
30 June 2020	6th month revision of tax estimates for companies with December year-end
30 June 2020	9th month revision of tax estimates for companies with September year-end
30 June 2020	Statutory deadline for filing of 2019 tax returns for companies with November year-end. As a concession, this deadline is extended to 30 September 2020 pursuant to the updated RF Filing Programme.

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