

Questionnaire

Malaysia's experiences regarding base erosion and profit shifting issues

1. **How does base erosion and profit shifting affect your country?**
2. **If you are affected by base erosion and profit shifting, what are the most common practices or structures used in your country or region, and the responses to them?**

As BEPS arrangement artificially shifts profit from Malaysia to other tax jurisdictions, it results in the erosion of tax revenue hence impact tax collection and undermine the credibility of the tax system due to negative public perception.

Commonly encountered profit shifting structure includes the following:-

- a. Excessive or unwarranted intra group payments such as interest on loans, management fees or technical services fees, or payment for intellectual properties.
It is difficult to determine if these payments are excessive or represent a fair return for the value of service received. Malaysia being the payor of such fees is greatly susceptible to the risks of BEPS via these kind of payments as these deductions are generally allowable when computing taxable income of a company and will result in a reduction of tax paid.
- b. Global Value Chain Model
Globalisation and rapid technological changes have resulted in a shift from traditional business models to new business global value chain model/ Centralised Business Model. Such business models make it easier for MNCs to shift profits between different tax jurisdictions. Malaysia has encountered cases of supply chain restructuring where risks are contractually transferred out which resulted in profits being shifted from a local company to a regional office. With this ability to contractually shift risk between members of the group, MNC can plan where profits are reported.
- c. Mispricing of services rendered
 - Important functions such as R&D performed here with only normal routine compensation given to the local entity
 - Marketing activities performed in order to capture the local market was not compensated
 - Low compensation given higher functions performed, assets employed and risks borne

The above are in relation to Actions 8, 9, 10 to assure that the transfer pricing outcomes are in line with value creation. By not properly compensating the local

entities, Malaysia's tax base is eroded as taxes are not paid in jurisdiction where economic activities are generated. Profits are easily shifted to related parties in low tax jurisdiction where there are no/minimal real economic activities.

3. When you consider an MNE's activity in your country, how do you judge whether the MNE has reported an appropriate amount of profit in your jurisdiction?

Through transfer pricing audit activities. Cases are first selected based on a risk assessment procedure. Malaysia has specific provisions on transfer pricing in our legislation.

4. What main obstacles have you encountered in assessing whether the appropriate amount of profit is reported in your jurisdiction and in ensuring that tax is paid on such profit?

The main obstacles faced include:-

- a. Lack of information due to difficulties in obtaining the relevant information especially information regarding foreign operations.
- b. Lack of transparency on the part of the MNE in disclosing relevant information on international dealings necessary for understanding the global business.
- c. Information not provided in a timely manner.
- d. Lack of comparables (from transfer pricing perspective).

Other relevant obstacles:

- e. Inadequate legislation.
- f. Lack of skills on auditors part to identify and deal with profit shifting issues.
- g. Insufficient resources (number of personnel) to deal with high risk cases – this will ultimately impact on compliance level of MNCs in local jurisdiction.

The Subcommittee have identified a number of actions in the Action Plan that impact on taxation in the country where the income is earned (the source country), as opposed to taxation in the country in which the MNE is headquartered (the residence country), or seek to improve transparency between MNEs and revenue authorities as being particularly important to many developing countries (while recognising that there will be particular differences between such countries). These are:

- Action 4 – Limit base erosion via interest deductions and other financial payments
- Action 6 – Prevent Treaty Abuse
- Action 8 – Assure that transfer pricing outcomes are in line with value creation: intangibles

- Action 9 – Assure that transfer pricing outcomes are in line with value creation: risks and capital
- Action 10 – Assure that transfer pricing outcomes are in line with value creation with reference to other high risk transactions (in particular management fees)
- Action 11 – Establish methodologies to collect and analyse data on BEPS and the actions to address it
- Action 12 – Require taxpayers to disclose their aggressive tax planning arrangements
- Action 13 – Re-examine transfer pricing documentation

5. Do you agree that these are particularly important priorities for developing countries?
Yes.

6. Which of these OECD's Action Points do you see as being most important for your country, and do you see that priority changing over time?
Action 10. Priority may change depending on changes in existing domestic policies over time.

7. Are there other Action Points currently in the Action Plan but not listed above that you would include as being most important for developing countries?
Action 7, Action 2.

8. Having considered the issues outlined in the Action Plan and the proposed approaches to addressing them (including domestic legislation, bilateral treaties and a possible multilateral treaty) do you believe there are other approaches to addressing that practices that might be more effective at the policy or practical levels instead of, or alongside such actions, for your country?
No.

9. Having considered the issues outlined in the Action Plan, are there are other base erosion and profit shifting issues in the broad sense that you consider may deserve consideration by international organisations such as the UN and OECD?
No.

10. Do you want to be kept informed by email on the Subcommittee's work on base erosion and profit shifting issues for developing countries and related work of the UN Committee of Experts on International Cooperation in Tax Matters?
Yes.

Do you have any other comments you wish to share with the Subcommittee about base erosion and profit shifting, including your experience of obstacles to assessing and then addressing the issues, as well as lessons learned that may be of wider benefit?

No comments for now.