



GUIDELINES ON MSC MALAYSIA FINANCIAL INCENTIVES (GRANDFATHERING AND TRANSITION UNDER SERVICES INCENTIVE)

1. INTRODUCTION

- 1.1 Pursuant to Malaysia's participation¹ in the Forum on Harmful Tax Practices (FHTP), Organisation for Economic Co-operation and Development (OECD), to implement the Base Erosion and Profit Shifting (BEPS) action plans, the income tax exemption under the MSC Malaysia Bill of Guarantee No. 5 has been revised to be consistent with the taxation standards under the OECD BEPS Action 5².
- 1.2 According to the aforesaid taxation standards, existing MSC Malaysia Status companies with income tax exemption are allowed to grandfather i.e. continue to enjoy the income tax exemption granted for non-intellectual property (non-IP) or services income under the Existing Regime, subject to compliance of MSC Malaysia Status Conditions of Grant issued to the companies.
- 1.3 The purpose of this document is to set out the guidelines on:
 - (a) grandfathering timeline applicable to existing MSC Malaysia Status companies with income tax exemption on non-IP or services income³; and
 - (b) transition of these companies from the Existing Regime to the Revised Regime in order to enjoy the income tax exemption in respect of non-IP or services income for the remaining exemption period.

¹ The details of Malaysia's participation can be found at <https://www.treasury.gov.my/index.php/en/tax/malaysia-s-commitment-in-international-tax-standard.html>

² The details on the taxation standards can be found at OECD, "Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5: 2015 Final Report", <http://www.oecd.org/tax/countering-harmful-tax-practices-more-effectively-taking-into-account-transparency-and-substance-action-5-2015-final-report-9789264241190-en.htm> and "Harmful Tax Practices – 2017 Progress Report on Preferential Regimes: Inclusive Framework on BEPS: Action 5", <http://www.oecd.org/tax/beps/harmful-tax-practices-2017-progress-report-on-preferential-regimes-9789264283954-en.htm>.

³ The relevant grandfathering timeline has been provided under the Promotion of Investments (Exclusion of Income For MSC Status Company) Regulations 2018 [P.U.(A) 332/2018] and Income Tax (Exemption) (No. 2) 2015 (Amendment) Order 2018 [P.U.(A) 396/2018].

1.4 In this document:

- (a) **“Eligibility Criteria”** means the eligibility criteria as specified in the New Guidelines;
- (b) **“Existing Regime”** means the income tax exemption granted under the Promotion of Investments Act 1986 or Income Tax (Exemption)(No. 2) Order 2015 [P.U.(A) 50/2015];
- (c) **“List of Promoted Activities”** means the list of MSC Malaysia promoted activities as specified in the New Guidelines;
- (d) **“New Conditions”** means the conditions imposed under the Revised Regime, as set out in **Appendix 1** or **Appendix 2**;
- (e) **“New Guidelines”** means the *“Guidelines on MSC Malaysia Financial Incentives (Services Incentive – Income tax Exemption)”* document with Effective Date of 1 January 2019; and
- (f) **“Revised Regime”** means the income tax exemption to be granted under the Income Tax (Exemption)(No. 10) Order 2018 [P.U.(A) 389/2018].

2. COMPANIES APPROVED ON OR BEFORE 16 OCTOBER 2017

2.1 Existing MSC Malaysia Status companies which have been granted approval of MSC Malaysia Status on or before 16 October 2017 and as at 1 January 2019, the exemption period has been activated and has not expired (i.e. either within first 5-year⁴ or second 5-year⁵ of the exemption period):

- (a) **Status quo:** These companies will grandfather under the Existing Regime and the exemption period (either first 5-year or second 5-year) can only be granted **until 30 June 2021**.
- (b) **Transition:** Subject to approval, the **remaining exemption period**⁶ will be granted under the Revised Regime:
 - (i) Eligibility Criteria and List of Promoted Activities are not applicable.
 - (ii) Percentage of tax exemption approved is to remain.

⁴ Pioneer certificate or commencement letter has been issued for the exemption period of first 5-year.

⁵ Approval has been issued for extension of exemption period of second 5-year.

⁶ “Remaining exemption period” refers to the period beginning from the subsequent date after the expiry of the grandfathering timeline until the expiry of 5 years from the commencement date under the Existing Regime.

- (iii) Commencement date of the remaining exemption period under the Revised Regime will be 1 July 2021.
- (iv) Companies are required to comply with the New Conditions in **Appendix 1**, commencing from 1 July 2021.
- (v) Companies may apply to add new activities in accordance with the New Guidelines (must comply with the List of Promoted Activities).
- (vi) For extension of exemption period for second 5-year⁷:
 - (1) Companies are required to submit the application for extension no later than 30 days before the expiry of the first 5-year.
 - (2) Eligibility Criteria and List of Promoted Activities are not applicable.
 - (3) Percentage of tax exemption is to remain⁸.
 - (4) The exemption period for the second 5-year will begin from the subsequent date after the expiry of the exemption period for the first 5-year.
 - (5) Companies are required to comply with the same New Conditions in **Appendix 1** for the second 5-year.
 - (6) Companies may apply to add new activities in accordance with the New Guidelines (must comply with the List of Promoted Activities).

Example:

Company A has been awarded MSC Malaysia Status on 1 October 2017. Company A has been issued a pioneer certificate and the exemption period for the first 5-year is from 1 January 2018 until 31 December 2022 under Existing Regime. Company A is allowed to grandfather under the Existing Regime for the exemption period from 1 January 2018 until 30 June 2021. The remaining exemption period from 1 July 2021 until 31 December 2022 will be granted under the Revised Regime. Company A may apply for extension of exemption period for second 5-year under the Revised Regime. The exemption period to be granted for the second 5-year will be from 1 January 2023 until 31 December 2027.

⁷ A Tier 3 company may apply for extension of exemption period for second 5-year provided that the company applies to change to either Tier 1 or 2 and complies with the conditions imposed under Tier 1 or 2 by the expiry of the exemption period for first 5-year.

⁸ A Tier 3 company which has changed to either Tier 1 or 2 will be approved 100% income tax exemption for second 5-year.

3. COMPANIES APPROVED AFTER 16 OCTOBER 2017

3.1 Existing MSC Malaysia Status companies which have been granted approval of MSC Malaysia Status after 16 October 2017 and as at 1 January 2019, the exemption period has been activated and has not expired (i.e. within first 5-year⁹):

- (a) **Status quo:** These companies will grandfather under the Existing Regime and the exemption period (the first 5-year) can only be granted **until 31 December 2018**.
- (b) **Transition:** Subject to approval, the **remaining exemption period**¹⁰ will be granted under the Revised Regime:
 - (i) Eligibility Criteria and List of Promoted Activities are not applicable.
 - (ii) Percentage of tax exemption approved is to remain.
 - (iii) Commencement date of the remaining exemption period under the Revised Regime will be 1 January 2019.
 - (vii) Companies are required to comply with the New Conditions in **Appendix 2**, commencing from 1 January 2019.
 - (iv) Companies may apply to add new activities in accordance with the New Guidelines (must comply with the List of Promoted Activities).
 - (v) For extension of exemption period for second 5-year¹¹:
 - (1) Companies are required to submit the application for extension no later than 30 days before the expiry of the first 5-year.
 - (2) Eligibility Criteria and List of Promoted Activities are not applicable.
 - (3) Percentage of tax exemption is to remain¹².
 - (4) The exemption period for the second 5-year will begin from the subsequent date after the expiry of the exemption period for the first 5-year.
 - (5) Companies are required to comply with the New Conditions applicable for Year 3 onwards as stated in **Appendix 2** for the second 5-year.

⁹ Pioneer certificate or commencement letter has been issued for the exemption period of first 5-year.

¹⁰ "Remaining exemption period" refers to the period beginning from the subsequent date after the expiry of the grandfathering timeline until the expiry of 5 years from the commencement date under the Existing Regime.

¹¹ A Tier 3 company may apply for extension of exemption period for second 5-year provided that the company applies to change to either Tier 1 or 2 and complies with the conditions imposed under Tier 1 or 2 by the expiry of the exemption period for first 5-year.

¹² A Tier 3 company which has changed to either Tier 1 or 2 will be approved 100% income tax exemption for second 5-year.

- (6) Companies may apply to add new activities in accordance with the New Guidelines (must comply with the List of Promoted Activities).

4. COMPANIES WHICH HAVE YET TO ACTIVATE FIRST 5-YEAR OR YET TO OBTAIN EXTENSION OF SECOND 5-YEAR

- 4.1 If as at 1 January 2019, an existing MSC Malaysia Status company has yet to activate the exemption period for the first 5-year or has yet to obtain the extension of exemption period for the second 5-year¹³:
- (a) The exemption period for the first 5-year will be activated or the approval for the extension of the exemption period for second 5-year will be granted under and in accordance with the Existing Regime¹⁴.
 - (b) The exemption period can only be granted:
 - (i) If the approval of MSC Malaysia Status is granted on or before 16 October 2017, **until 30 June 2021**.
 - (ii) If the approval of MSC Malaysia Status is granted after 16 October 2017, **until 31 December 2018**.
 - (c) Subject to approval, the **remaining exemption period**¹⁵ will be granted under the Revised Regime.
 - (d) If the approval of MSC Malaysia Status is granted after 16 October 2017 and the date of first invoice is after 31 December 2018, the exemption period of the first 5-year will be approved under the Revised Regime.
 - (e) Where the exemption period for the first 5-year or any part of the first 5-year is to be granted under the Revised Regime:
 - (i) Eligibility Criteria and List of Promoted Activities are not applicable.
 - (ii) Percentage of tax exemption approved is to remain.

¹³ Pioneer certificate or commencement letter for the exemption period of first 5-year or approval for extension of exemption period of second 5 year has yet to be issued.

¹⁴ Exemption granted under Existing Regime is subject to the company's compliance of the existing MSC Malaysia Status Conditions of Grant issued to the company.

¹⁵ "Remaining exemption period" refers to the period beginning from the subsequent date after the expiry of the grandfathering timeline until the expiry of 5 years from the commencement date under the Existing Regime.

- (iii) Commencement date of the exemption period under the Revised Regime will be:
 - (1) 1 July 2021 (if the approval of MSC Malaysia Status is granted on or before 16 October 2017); or
 - (2) 1 January 2019 or date of first invoice, whichever is later (if the approval of MSC Malaysia Status is granted after 16 October 2017).
- (iv) If the commencement date is 1 July 2021, companies are required to comply with the New Conditions in **Appendix 1** starting from the said commencement date.
- (v) If the commencement date is 1 January 2019 or date of first invoice, whichever is later, companies are required to comply with the New Conditions in **Appendix 2** starting from the said commencement date.
- (vi) Companies may apply to add new activities in accordance with the New Guidelines (must comply with the List of Promoted Activities).
- (vii) For extension of exemption period for second 5-year¹⁶:
 - (1) Companies are required to submit the application for extension no later than 30 days before the expiry of the first 5-year.
 - (2) Eligibility Criteria and List of Promoted Activities are not applicable.
 - (3) Percentage of tax exemption is to remain¹⁷.
 - (4) The exemption period for the second 5-year will begin from the subsequent date after the expiry of the exemption period for the first 5-year.
 - (5) Companies are required to comply with the New Conditions as stated in **Appendix 1** for the second 5-year.
 - (6) Companies may apply to add new activities in accordance with the New Guidelines (must comply with the List of Promoted Activities).

¹⁶ A Tier 3 company may apply for extension of exemption period for second 5-year provided that the company applies to change to either Tier 1 or 2 and complies with the conditions imposed under Tier 1 or 2 by the expiry of the exemption period for first 5-year.

¹⁷ A Tier 3 company which has changed to either Tier 1 or 2 will be approved 100% income tax exemption for second 5-year.

- (f) Where the remaining exemption period for the second 5-year is to be granted under the Revised Regime:
- (i) Eligibility Criteria and List of Promoted Activities are not applicable.
 - (ii) Percentage of tax exemption is to remain.
 - (vi) Commencement date of the remaining exemption period for the second 5-year under the Revised Regime will be 1 July 2021.
 - (iii) Companies are required to comply with the New Conditions as stated in **Appendix 1** commencing from 1 July 2021.
 - (iv) Companies may apply to add new activities in accordance with the New Guidelines (must comply with the List of Promoted Activities).
- (g) For the avoidance of doubt, for any exemption period granted under the Revised Regime, the commencement date of the said exemption period cannot be earlier than 1 January 2019.
- (h) A summary of the above guidelines on transition is set out below:

MSC Status approval date	Scenario	Exemption period allowed under Existing Regime (grandfathering period)	Exemption period to be granted under Revised Regime	Commencement date under Revised Regime	New Conditions to be complied with starting from the commencement date under Revised Regime
On or before 16 October 2017	Yet to activate first 5-year	From date of first invoice until 30 June 2021	From 1 July 2021 until expiry of 5 years from date of first invoice	1 July 2021	Appendix 1
	For extension of second 5-year:	N/A	From the subsequent date after expiry of first 5-year until expiry of 5 years	Subsequent date after expiry of first 5-year	Appendix 1
	Yet to obtain extension for second 5-year	From the subsequent date after expiry of first 5-year (start date) until 30 June 2021	From 1 July 2021 until expiry of 5 years from start date	1 July 2021	Appendix 1
After 16 October 2017	Yet to activate first 5-year	From date of first invoice until 31 December 2018	From date of first invoice (if issued after 31 December 2018) or 1 January 2019, whichever is later, until expiry of 5 years	Date of first invoice or 1 January 2019, whichever is later	Appendix 2
	For extension of second 5-year	N/A	From the subsequent date after expiry of first 5-year until expiry of 5 years	Subsequent date after expiry of first 5-year	Appendix 1

5. INSTITUTION OF HIGHER LEARNING (IHL) AND INCUBATOR

- 5.1 Existing IHL and Incubator entities impacted by the aforesaid grandfathering timeline may apply for income tax exemption for the **remaining exemption period**¹⁸ or the extension of exemption period for second 5-year, in accordance with the guidelines set out in this document.
- 5.2 For any exemption period granted under the Revised Regime, the IHL and Incubator entities are required to comply with the following new conditions as determined by the approval committee:
- (a) To employ an adequate number of full time employees with adequate amount of monthly base salary; and
 - (b) To incur an adequate amount of annual operating expenditure and investment of fixed asset.

6. TRANSITION

- 6.1 The granting of any exemption period or remaining exemption period under the Revised Regime is subject to the companies fulfilling the applicable New Conditions and approval of the approval committee.

7. SEGREGATION OF INCOME

- 7.1 The companies are required to segregate the IP income from the statutory income in order to enjoy the tax exemption during the grandfathering period and during the exemption period granted under the Revised Regime.
- 7.2 IP income means any income from royalty and other income derived from an intellectual property right¹⁹ if it is receivable as consideration for the commercial exploitation of that right.

ISSUED BY MALAYSIA DIGITAL ECONOMY CORPORATION (MDEC)

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Disclaimer: The information contained in these Guidelines is to provide details, explanations and/or clarifications on the financial incentives granted under MSC Malaysia. You are advised to refer to the applicable legislations. MDEC cannot accept responsibility for any action or decision made in reliance of these Guidelines or any liability incurred or loss suffered as a consequence of relying on these Guidelines. These Guidelines are not intended to address all possible tax issues that may arise and you are advised to seek professional advice in respect of the tax issues. MDEC reserves the right to amend or update these Guidelines from time to time, based on approval of the Government of Malaysia.

¹⁸ "Remaining exemption period" refers to the period beginning from the subsequent date after the expiry of the grandfathering timeline until the expiry of 5 years from the commencement date under the Existing Regime.

¹⁹ "Intellectual property right" means a right arising from any patent, utility innovation and discovery, copyright, trade mark and service mark, industrial design, layout-design of integrated circuit, secret processes or formulae and know-how, geographical indication, the grant of protection of a plant variety, or other like rights, whether or not registered or registrable.

APPENDIX 1
New Conditions

Conditions	Tier 1	Tier 2	Tier 3
(1) Location of approved MSC Malaysia qualifying activities	Designated Premises within MSC Malaysia Cybercities or Cybercentres²⁰	Other Commercial Premises within MSC Malaysia Cybercities or Cybercentres	Not subjected to location requirement
(2) Undertake the approved MSC Malaysia qualifying activities in Malaysia			
	Minimum KPI Numbers		
(3) Full time employees (comprising Knowledge Workers) with monthly base salary	(i) 50 full time employees with monthly base salary of RM5k; OR (ii) 30 full time employees with monthly base salary of RM10k	(i) 30 full time employees with monthly base salary of RM5k; OR (ii) 20 full time employees with monthly base salary of RM8k	
	data centre: 5 full time employees with monthly base salary of RM5k		
(4) Annual operating expenditure and investment in fixed asset	RM3.5mil	RM1mil	
	data centre: RM10mil		
(5) % of Malaysian Knowledge Workers (for the full time employees in (3) above)	70%	50%	

²⁰ List of MSC Malaysia Cybercities or Cybercentres is available at MDEC's website (www.mdec.my).

APPENDIX 2
New Conditions

Conditions	Tier 1	Tier 2	Tier 3
(1) Location of approved MSC Malaysia qualifying activities	Designated Premises within MSC Malaysia Cybercities or Cybercentres²¹	Other Commercial Premises within MSC Malaysia Cybercities or Cybercentres	Not subjected to location requirement
(2) Undertake the approved MSC Malaysia qualifying activities in Malaysia			
Minimum KPI Numbers			
To be complied with in Year 1 and Year 2 of the exemption period:			
(3) Full time employees (comprising Knowledge Workers) with monthly base salary	2 full time employees with monthly base salary of RM5k		
(4) Annual operating expenditure	RM50k		
To be complied with from Year 3 onwards until expiry of exemption period:			
(5) Full time employees (comprising Knowledge Workers) with monthly base salary	(i) 50 full time employees with monthly base salary of RM5k; OR (ii) 30 full time employees with monthly base salary of RM10k		(i) 30 full time employees with monthly base salary of RM5k; OR (ii) 20 full time employees with monthly base salary of RM8k
	data centre: 5 full time employees with monthly base salary of RM5k		
(6) Annual operating expenditure and investment in fixed asset	RM3.5mil		RM1mil
	data centre: RM10mil		
(7) % of Malaysian Knowledge Workers (for the full time employees in (5) above)	70%		50%

²¹ List of MSC Malaysia Cybercities or Cybercentres is available at MDEC's website (www.mdec.my).