

## Client Alert

23 October 2019

### Malaysia Releases New Guidelines for the Principal Hub 2.0 Incentive

On 8 October 2019, the Malaysian Investment Development Authority ("**MIDA**") announced enhancements to the Principal Hub ("**PH**") incentive, referring to it as the PH 2.0 incentive. Following the announcement, MIDA issued new guidelines for PH 2.0, which are applicable to PH applications received by MIDA from 1 January 2019 to 31 December 2020.

We discuss below the key features of the guidelines, and what they may mean to you.

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#### **Concessionary Tax Rates under PH 2.0**

Locally incorporated companies that satisfy specific conditions will be able to enjoy the following concessionary corporate income tax ("**CIT**") rates on trading and services income derived from qualifying PH activities:

	Category	Concessionary CIT Rate	Period of Enjoyment
(a)	New companies <sup>1</sup>	Tier 1: 0% Tier 2: 5%	5 years  (plus an extension of 5 years where additional conditions are satisfied)
(b)	Existing companies	10%  (instead of a full tax exemption on value added income under the previous PH regime)	5 years

<sup>1</sup> "New companies" are defined in the guidelines to include a "new locally incorporated company which has an existing entity or related entity in Malaysia but has not undertaken any PH qualifying services in Malaysia".





It should be noted that royalties and other income derived from intellectual property rights owned by the PH company are excluded from the PH 2.0 incentive.

The PH company will also be entitled to a customs duty exemption when bringing raw materials, components, or finished products into free industrial zones, licensed manufacturing warehouse, free commercial zones, and bonded warehouses for production or re-packaging, cargo consolidation and integration before distribution to its final consumers.

### **Minimum Requirements**

We have set out below the key minimum requirements:

<b>Eligibility Conditions</b>	
Company Status	<ul style="list-style-type: none"><li>• Incorporated under the Companies Act 2016 and resident in Malaysia.</li></ul>
Local Equity / Ownership	<ul style="list-style-type: none"><li>• No requirements.</li></ul>
Paid-up Capital	<ul style="list-style-type: none"><li>• More than RM 2.5 million.</li></ul>
Core Income Generating Activities	<ul style="list-style-type: none"><li>• Provides a minimum of 4 to 5 services depending on the category of the PH company, including:<ul style="list-style-type: none"><li>(i) regional profit and loss ("<b>P&amp;L</b>") / business unit management services; and</li><li>(ii) strategic business planning and corporate development activities.</li></ul></li></ul>
Network Companies	<ul style="list-style-type: none"><li>• Serving and controlling a minimum number of network companies of 10 or 15 network companies<sup>2</sup>, depending on the category of the PH company.</li></ul>

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<sup>2</sup> "Network companies" are defined as:

- (i) related companies or entities within a same group including subsidiaries, branches, and joint venture entities; or
- (ii) non-related companies that have contractual agreements with the applicant or the applicant's ultimate company with regard to the applicant's business and supply chain for at least 3 years.



Employment Requirements	<ul style="list-style-type: none"><li>• Must hire a specified number of employees for high value jobs and key strategic / management positions with a minimum monthly salary of RM 5,000 and RM 25,000 respectively.</li><li>• At least 50% of the high value jobs must be filled by Malaysians.</li><li>• Provide structured internship and training programs approved by Talent Corporation Malaysia for Malaysians.</li></ul>
Annual Operating Expenditure	<ul style="list-style-type: none"><li>• New companies must incur a minimum annual operating expenditure of RM 5 million or RM 10 million, depending on the tier.</li><li>• Existing companies must incur a minimum annual operating expenditure of RM 10 million (or average operating expenditure for the past 3 years + 30% whichever is higher) or RM 13 million (or average operating expenditure for the past 3 years + 20% whichever is higher), depending on the relevant category of the applicant company.</li><li>• The definition of annual operating expenditure excludes the cost of goods sold and expenses that are not directly related to core income generating activities such as depreciation and interest on borrowings.</li><li>• The company should be the planning, control and reporting centre for the qualifying services.</li></ul>
Annual Sale Turnover	<ul style="list-style-type: none"><li>• The minimum threshold for new companies is RM 500 million.</li><li>• The minimum threshold for existing companies is the <u>higher</u> of either:<ul style="list-style-type: none"><li>(i) RM 500 million; or</li><li>(ii) the average sales turnover of the company for the past 3 years.</li></ul></li></ul>
Use of Local Ancillary Services	<ul style="list-style-type: none"><li>• The PH company should make significant use of local financial institution services (including finance and treasury), logistics,</li></ul>



	legal and arbitration services, finance and treasury services.
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### **Qualifying Services**

The list of qualifying PH services are as follows:

<b>No.</b>	<b>Cluster</b>	<b>Qualifying Service</b>
1.	Strategic services	<ul style="list-style-type: none"><li>• Regional P&amp;L / business unit management</li><li>• Strategic business planning and corporate development</li><li>• Corporate finance advisory services</li><li>• Brand management</li><li>• Intellectual property management</li><li>• Senior-level talent acquisition and management</li></ul>
2.	Business services	<ul style="list-style-type: none"><li>• Bid and tender management</li><li>• Treasury and fund management</li><li>• Research, development and innovation</li><li>• Project management</li><li>• Sales and marketing</li><li>• Business development</li><li>• Technical support and consultancy</li><li>• Information management and processing</li><li>• Economic / investment research analysis</li><li>• Strategic sourcing, procurement and distribution</li><li>• Logistics services</li></ul>
3.	Shared services	<ul style="list-style-type: none"><li>• Corporate training and human resource management</li><li>• Finance and accounting (transactions, internal audit)</li></ul>

### **Compliance Obligations**

A PH company is required to submit a PH Compliance Assessment Form within 6 months from the financial year-end of the company to MIDA on an annual basis for



performance evaluation. Failure to do so within the stipulated timeline or to request for an extension of time will cause the incentive to be withdrawn.

In addition, the new guidelines state that the PH company is required to comply with the specified conditions throughout the exemption period. If the PH company fails to comply with the stipulated conditions in any year of assessment, it will not be entitled to the exemption for that year of assessment. This signals the Malaysian Government's intention to tighten enforcement of the requirements, in line with international standards for tax incentives and preferential regimes.

### **Next Steps**

The PH incentive was first introduced in 2015 in an effort to attract multinational companies to set up their regional and global operations to manage, control and support key functions including risk management, decision-making, strategic business activities in Malaysia.

We will be monitoring legislative updates relating to the PH incentive. At the time of this alert, the relevant statutory orders have not yet been made available to revise the incentive.

Companies interested in applying for the PH 2.0 incentive should consider the eligibility criteria and conditions in greater detail, especially since the Government has signaled its intention to tighten enforcement in the future.

Our team can support companies with their preliminary assessments of eligibility, and also with the preparation and submission of their PH 2.0 applications to MIDA.

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