

Investors' Guide

INVESTORS' GUIDE

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I. INVESTMENT INCENTIVES BY LEGISLATION (AS AT 19 OCTOBER 2001)

Malaysia offers incentives for investments in promoted products and activities in the manufacturing, agriculture, hotel and tourism industry, research and development (R&D) and training activity. These incentives are contained in the Promotion of Investments Act 1986, Income Tax Act 1967, Labuan Offshore Business Activity Tax Act (LOBATA) 1990, Customs Act 1967, Sales Tax Act 1972, Excise Act 1976 and Free Zones Act 1990. The incentives are designed to grant partial or to a limited extent total relief from the payment of tax.

A. PROMOTION OF INVESTMENTS ACT 1986

(1) Pioneer Status (PS)

A company that is granted PS will enjoy different degree of exemptions depending on the types of promoted products or activities as follows:

(a) Promoted Product/Activity

Company will be granted exemption of income tax on 70% of the statutory income for 5 years. The balance 30% of that statutory income will be taxed at the prevailing company tax rate.

(b) Promoted Product/Activity in Promoted Area

Company located in Sabah, Sarawak, the Federal Territory of Labuan* and the

designated Eastern Corridor of Peninsular Malaysia which covers, Kelantan, Terengganu, Pahang and the district of Mersing in Johor, will be granted exemption of income tax on 85% of the statutory income for 5 years. The balance 15% of that statutory income will be taxed at the prevailing company tax rate.

(c) Promoted Product/Activity for High Technology Companies

Company will be granted full exemption of income tax i.e. on 100% of the statutory income for 5 years.

(d) Promoted Product in an Approved Industrial Linkage Scheme (SMIs producing intermediate goods)

Company will be granted full exemption of income tax i.e. on 100% of the statutory income for 5 years.

(e) Promoted Product/Activity of National and Strategic Importance

Company will be granted full exemption of income tax i.e. on 100% of the statutory income for 5 years and is eligible for extension of another 5 years. Companies that have started operations are also eligible but the incentives will only be given to the additional income. Companies currently enjoying PS may apply for the incentives at the end of the existing incentive period.

- (i) Companies accorded Multimedia Super Corridor (MSC) Status are also eligible for this incentive in

* only applicable to the hotel and tourism industry.

addition to other incentives under the Bill of Guarantees. The tax incentive accorded to the MSC companies is also extended to multimedia faculties located outside the MSC. A multimedia faculty under the proposed incentive is referred to as a centre of learning which provides courses in media, computer, information technology, telecommunications, communications and contents relating to data, voice, graphics and images.

- (ii) Companies in approved industrial linkage scheme capable of achieving world class standards in terms of price, quality and capacity are also eligible.

(f) Contract Research and Development (R&D) company

A company that provides R&D services in Malaysia to a company other than its related company, will be granted full exemption of income tax i.e. on 100% of the statutory income for 5 years.

Terms and conditions for companies enjoying PS:

- (i) Company granted PS shall within 6 months or such approved extended period request for a pioneer certificate, specifying among others the date of production from which the partial exemption/full exemption will be granted.
- (ii) Capital allowances have to be utilised during the pioneer period and will not be allowed to be carried forward to the post pioneer period.
- (iii) Losses unabsorbed during the pioneer period will not be allowed to be carried forward to the post pioneer period except for PS for Contract Research and Development Company.
- (iv) Dividends paid out of tax-exempt income to shareholders will also be exempted from tax.

(2) Investment Tax Allowance (ITA)

The Investment Tax Allowance is an alternative to the Pioneer Status and is designed to cater for projects which have large capital investments and long gestation periods.

As in the case of PS, a company granted ITA will enjoy different degree of exemptions as follows:

(a) Promoted Product/Activity

Company will be granted an allowance of 60% in respect of qualifying capital expenditure (such as factory, plant, machinery or other equipment used for approved project) incurred within 5 years from the date that the first capital expenditure incurred. The allowance can be utilised to set off up to 70% of the statutory income in the assessment year. The balance of that statutory income will be taxed at the prevailing company tax rate. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.

(b) Promoted Product/Activity In Promoted Area

Company located in Sabah, Sarawak, the Federal Territory of Labuan* and designated Eastern Corridor of Peninsular Malaysia which covers Kelantan, Terengganu, Pahang and the district of Mersing in Johor will be granted an allowance of 80% in respect of qualifying capital expenditure incurred within 5 years from the date the first capital expenditure incurred. The allowance can be utilised to set off up to 85% of the statutory income in the assessment year. The balance of that statutory income will be taxed at the prevailing company tax rate. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.

* only applicable to the hotel and tourism industry.

(c) Promoted Product/Activity For High Technology Companies

Company will be granted an allowance of 60% in respect of qualifying capital expenditure incurred within 5 years from the date the first capital expenditure incurred. The allowance can be utilised to set off against 100% of statutory income in the year of assessment. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.

(d) Promoted Product In An Approved Industrial Linkage Programme

Company will be granted an allowance of 100% in respect of qualifying capital expenditure incurred within 5 years from the date the first capital expenditure incurred. The allowance can be utilised to set off against 100% of statutory income in the year of assessment. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.

(e) Promoted Product/Activity Of National And Strategic Importance

Company will be granted an allowance of 100% in respect of qualifying capital expenditure incurred within 5 years from the date the first capital expenditure incurred. The allowance can be utilised to set off against 100% of statutory income in the year of assessment. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up. Companies that have started operation are also eligible but the incentives will only be given on the additional investment. Companies currently enjoying ITA may apply for the incentives at the end of the existing incentive period.

- (i) Companies accorded Multimedia Super Corridor (MSC) Status are also eligible for this incentive in

addition to other incentives under the Bill of Guarantees. The tax incentive accorded to the MSC companies is also extended to multimedia faculties located outside the MSC. A multimedia faculty under the proposed incentive refers to as a centre of learning which provides courses in media, computer, information technology, telecommunications, communications and contents relating to data, voice, graphics and images.

- (ii) Companies in approved industrial linkage scheme capable of achieving world class standards in terms of price, quality and capacity are also eligible.

(f) Research and Development (R&D) Activities

Different incentives are given to companies specialising in R&D activities, i.e. incentives for "R&D company" and incentives for "Contract R&D Company", as follows:

- (i) R&D Company (a company that provides R&D services in Malaysia to its related company or to any other company)

Company will be granted an allowance of 100% in respect of qualifying capital expenditure incurred within 10 years from the date the first capital expenditure incurred. The allowance can be utilised to set off up to 70% of the statutory income in the assessment year. The balance of that statutory income will be taxed at the prevailing company tax rate. Any unutilised allowance can be carried forward to the subsequent years until it is fully utilised.

- (ii) Contract R&D Company (a company that provides R&D services in Malaysia to a company other than its related company)

Company will be granted an allowance of 100% in respect of qualifying capital expenditure incurred within 10 years from the date the first capital expenditure incurred. The allowance can be utilised to set off up to 70% of the statutory income in the assessment year. The balance of that statutory income will be taxed at the prevailing company tax rate. Any unutilised allowance can be carried forward to the subsequent years until it is fully utilised.

- (iii) In-house R&D (research and development carried on in Malaysia within a company for the purpose of its own business)

Company will be granted an allowance of 50% in respect of qualifying capital expenditure incurred within 10 years from the date the first capital expenditure incurred. The allowance can be utilised to set off up to 70% of the statutory income in the assessment year. The balance of that statutory income will be taxed at the prevailing company tax rate. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.

- (g) Technical or Vocational training company

Company will be granted an allowance of 100% in respect of qualifying capital expenditure incurred within 10 years from the date the first capital expenditure incurred. The allowance can be utilised to set off up to 70% of the statutory income in the assessment year. The balance of that statutory income will be taxed at the prevailing company tax rate. Any unutilised

allowance can be carried forward to subsequent years until the whole amount has been used up.

Companies with existing technical or vocational training institutes that incur new investment to upgrade their training equipment or expand their training capacities are also eligible for this incentive.

(3) Industrial Adjustment Allowance (IAA)

IAA is available to companies in selected manufacturing sector namely in wood based, textile, machinery and engineering, stamping, mould, tools and dies and machinery sub-sector. The companies should already be in existence before 31.12.1990 and have been participating in certain industrial adjustment activities such as reorganisation, reconstruction or amalgamation within the sector.

Companies will be granted an allowance of 60% to 100% based on the industrial adjustment activities undertaken. The allowance will be given in respect of qualifying capital expenditure incurred within 5 years. The allowance can be utilised to set off against 100% of adjusted income in the year of assessment.

Terms and conditions for companies enjoying ITA & IAA:

- (i) Any unutilised allowance can be carried forward to the subsequent years until it is fully utilised.
- (ii) Dividends paid out of tax-exempt income to shareholders will also be exempted.

(4) Infrastructure Allowance (IA)

IA is available to any company resident in Malaysia engaged in manufacturing, agricultural, hotel, tourism or other industrial/commercial activity in Sabah, Sarawak and the designated Eastern Corridor of Peninsular Malaysia.

Company will be granted an allowance of 100% in respect of capital expenditure on infrastructure (such as reconstruction, extension, or

improvement of any permanent structure including a bridge, jetty, port or road). The allowance can be utilised to set off up to 85% of statutory income in the year of assessment. The balance of that statutory income will be taxed at the prevailing company tax rate. Any unutilised allowance can be carried forward to the subsequent years until it is fully utilised.

(5) Double Deduction on Expenses for Promotion of Exports

This incentive is available to any company resident in Malaysia seeking opportunities for exports of manufactured and agricultural products.

The expenses eligible for double deduction are:

- (a) overseas advertising,
- (b) supply of free samples abroad,
- (c) export market research,
- (d) preparation of tenders for the supply of goods overseas,
- (e) supply of technical information abroad,
- (f) exhibits and/or participation required in trade or industrial exhibitions held locally or abroad approved by the Ministry of International Trade and Industry (MITI),
- (g) fares in respect of travel overseas by employees of companies for business,
- (h) accommodation and sustenance expenses incurred by Malaysian businessman going overseas for business, subject to RM200 per day,
- (i) cost of maintaining sales office overseas for the promotion of exports, and
- (j) professional service fees for designing the package of products for export subject to the conditions that the product is of export quality and the company uses local professional services.

For pioneer companies, the expenses are accumulated and allowed against their post-pioneer income.

(6) Incentive For Forest Plantation Project

Companies which undertake forest plantation projects are eligible for the following incentives:

- (i) full income tax exemption i.e 100% of statutory income for 5 years and eligible for extension of another 5 years; or
- (ii) Investment Tax Allowance of 100% of capital expenditure incurred within a period of 5 years to be set off against 100% of the statutory income in the assessment year. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.

(7) Incentive For Storage, Treatment And Disposal Of Toxic And Hazardous Waste.

Companies which are directly involved in the storage, treatment and disposal of toxic and hazardous waste in an integrated manner are granted:

- (i) income tax exemption on 70% of statutory income for 5 years; or
- (ii) Investment Tax Allowance of 60% of capital expenditure incurred within a period of 5 years to be set off against 70% of the statutory income in the assessment year. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.
- (iii) Activities located in the promoted areas are eligible for income tax exemption or Investment Tax Allowance in accordance with that given for promoted areas.

(8) Incentive For Waste Recycling Activities

Companies undertaking waste recycling activities of high value added using high technology are granted:

- (i) income tax exemption on 70% of statutory income for 5 years; or

- (ii) Investment Tax Allowance of 60% of capital expenditure incurred within a period of 5 years to be set off against 70% of the statutory income in the assessment year. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.
- (iii) Activities located in the promoted areas are eligible for income tax exemption or Investment Tax Allowance in accordance with that given for promoted areas.

(9) Incentive For The Conservation of Energy

(A) Companies providing energy conservation services are granted:

- (i) income tax exemption on 70% of statutory income for 5 years; or
- (ii) Investment Tax Allowance of 60% of capital expenditure incurred within a period of 5 years to be set off against 70% of the statutory income in the assessment year. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.
- (iii) Activities located in the promoted areas are eligible for income tax exemption or Investment Tax Allowance in accordance with that given for promoted areas.

This incentive is applicable for applications received from **28 October 2000 until 31 December 2002**, on condition that the company must implement the project within one year from the date the incentive is approved.

(B) Companies which incur capital expenditure for purpose of energy conservation measures in their own company are granted Accelerated Depreciation Allowance, to be written

off within a period of 3 years. This incentive is effective from the year of assessment 2001.

(10) Incentive For Utilising Biomass As A New Source Of Energy

Companies intending to generate 'energy' from 'biomass sources' are granted:

- (i) income tax exemption of 70% of statutory income for 5 years; or
- (ii) Investment Tax Allowance of 60% to be set off against 70% of statutory income for 5 years. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.
- (iii) Activities located in the promoted areas are eligible for income tax exemption or Investment Tax Allowance in accordance with that given for promoted areas.

This incentive is applicable for applications received from **28 October 2000 until 31 December 2002**, on condition that the company must implement the project within one year from the date the incentive is approved.

For purposes of this incentive, 'biomass sources' refer to the following:

- (i) Palm Oil Mill/Estates Waste
- (ii) Rice Mill Waste
- (iii) Sugar Cane Mill Waste
- (iv) Timber /Sawmill Waste
- (v) Paper Recycling Mill Waste
- (vi) Municipal Waste
- (vii) Biogas (from Landfill, Palm Oil Mill Effluent (POME), Animal Waste, others)

'Energy' forms in this incentive refer to the following:

- (i) Electricity
- (ii) Steam
- (iii) Chilled Water
- (iv) Heat

(11) Incentive for Companies Providing Cold Chain Facilities and Services for Food Products

To encourage companies to provide cold room and refrigerated facilities and related services such as collection and treatment of locally produced perishable food products, companies will be granted the following incentives:

- (i) income tax exemption of 70% on statutory income for 5 years; or
- (ii) Investment Tax Allowance of 60% on the capital expenditure incurred within 5 years, to be utilised against 70% of statutory income. Any unutilised allowance can be carried forward to subsequent years until the whole amount has been used up.
- (iii) Activities located in the promoted areas are eligible for income tax exemption or Investment Tax Allowance in accordance with that given for promoted areas.

exemption of income tax on 85% of the statutory income for 5 years. The balance 15% of that statutory income will be taxed at the prevailing company tax rate;

- (iii) companies undertaking ASP of national and strategic importance will be granted full exemption of statutory income from payment of income tax for 10 years.

Note:

- Dividends paid out of tax-exempt income to shareholders will also be exempted from tax.
- Capital allowances and losses unabsorbed have to be utilised during the exemption period and will not be allowed to be carried forward to the post exemption period.

B. INCOME TAX ACT 1967

(1) Income Tax Exemption

- (a) Approved Service Projects (ASP)
(Section 127)

The income of companies undertaking ASP is exempted at statutory level. The quantum of tax exemption on statutory income varies between 70% and 100% for a period of 5 and 10 years from the date of generation of income. The quantum of exemption available are as follows:

- (i) companies undertaking ASP will be granted partial exemption of income tax on 70% of the statutory income for 5 years. The balance 30% of that statutory income will be taxed at the prevailing company tax rate;
- (ii) companies undertaking ASP in Sabah, Sarawak and the designated 'eastern corridor' of Peninsular Malaysia will be granted partial

- (b) Trading Companies

Companies approved as "International Trading Company" are given income tax exemption amounting to 70% of the statutory income arising from increased export sales. For the purpose of this incentive, export sales do not include trading commissions and profits derive from trading at the commodity exchange. This exemption is for five (5) years. To qualify as an 'International Trading Company', a company must satisfy the following criteria:

- (i) be incorporated in Malaysia,
- (ii) achieve an annual sales turnover of more than RM25 million,
- (iii) equity holding of at least 70% by Malaysian,
- (iv) market manufactured goods, especially those from small and medium scale industry, and
- (v) be registered with MATRADE.

In addition, the company must satisfy the following conditions to enjoy for the tax incentive:

- (i) not more than 20% of annual sales is derived from trading of commodities,
- (ii) not more than 20% of annual sales is derived from the sales of the goods of related companies, and
- (iii) use local services such as banking, finance, insurance, ports and airports.

(c) Operational Headquarters Company (OHQ)

An approved OHQ company is a locally incorporated company which carries on a business in Malaysia of providing qualifying services to its offices or related companies outside Malaysia and which is approved by the Minister of Finance.

The qualifying services are in respect of:

- (i) general management and administration;
- (ii) business planning and co-ordination;
- (iii) procurement of raw materials, components and finished products;
- (iv) technical support and maintenance;
- (v) marketing control and sales promotion planning;
- (vi) training and personnel management;
- (vii) treasury and fund management services;
- (viii) corporate financial advisory services;
- (ix) research and development (R&D) work;

Companies granted an approved OHQ status will enjoy a 10% concessionary tax on business income, income from loan/fund management services and royalty income received from research and development work.

Income arising from sources outside Malaysia and received in Malaysia by a resident company is not subject to tax.

The tenure of the OHQ incentives is for a period of five (5) years which may be extended for another five (5) years.

(d) Venture Capital Industry

The following incentives are available:

(i) Venture Capital Companies Investing In Venture Companies:

Venture Capital Companies(VCC) investing in venture companies are given full tax exemption on all sources of income for 10 years of assessment or the years of assessment equivalent to the life span of the fund(if any) established for the purpose of investing in the venture company whichever is the lesser. Where a VCC incurs a loss from the disposal of shares in a venture company in the basis period for any year of assessment within the exempt period, such loss shall be carried forward to the post-exempt period.

Conditions to qualify for the exemption:

- Be a company incorporated under the Companies Act 1965, a partnership, a scheme or an arrangement investing in a venture company in the form of seed-capital, start-up or early-stage financing.
- Have at least 70% of its funds invested in venture companies which are not its related companies at the time of first investment.
- The venture companies must be a resident in Malaysia for the basis year for the year of assessment and involved in

products/activities promoted by the Government include those recognised by the following:

- o Promotion Investments Act 1986 such as Pioneer Status or Investment Tax Allowance incentive granted by MIDA/MITI, high-tech incentives granted by MIDA, MSC status granted by MDC, and SMIDEC;
- o Technology-based activities approved by MESDAQ;
- o Industrial Research & Development Grant Scheme granted by Ministry of Science, Technology and the Environment; or
- o MSC Research & Development Grant Scheme granted by MDC.

VCC must obtain annual certification from the Security Commission that the conditions imposed for the incentives have been complied. The letter of certification must be attached with the income tax return form for submission to the Inland Revenue Board. This incentive is effective from the year of assessment 2000 in respect of the basis period ending in the year 2000.

(ii) Companies or Individuals Investing In Venture Companies:

A company or an individual having a business source, having invested in a venture company at start-up, seed capital and early stage financing are entitled to a deduction from the adjusted income equivalent to the value of the investment made in the venture company. If the company or individual does not have

sufficient adjusted income to offset the investment, the deductions will be allowed to be carried forward.

Conditions to qualify for the deduction:

- Be a resident in Malaysia and making investments in a venture company for financing or funding at seed-capital, start-up or early-stage.
- The investment in the venture company is in a form of holding of shares which at the time of acquisition are not listed for quotation in the official list of a stock exchange.
- The venture companies must not be its related companies at the time of first investment.
- The venture companies must be resident in Malaysia for the basis year of the year of assessment and involved in products/activities promoted by the Government include those recognised by the following:
 - o Promotion Investment Act 1986 such as Pioneer Status or Investment Tax Allowance incentive granted by MIDA/MITI, high-tech incentives granted by MIDA, MSC status granted by MDC, and SMIDEC;
 - o Technology-based activities approved by MESDAQ;
 - o Industrial Research & Development Grant Scheme granted by Ministry of Science, Technology and the Environment; or
 - o MSC Research & Development Grant Scheme granted by MDC.

A company or an individual must obtain annual certification from the Securities Commission that the conditions imposed for the incentives have been complied. The letter of certification must be attached with the income tax return form for submission to the Inland Revenue Board. This incentive is effective from the year of assessment 2001. For a company the incentive 1(d)(i) and (ii) are mutually exclusive.

For purposes of obtaining tax incentives, the definitions for stages of financing are as follows:

“early-stage financing” means financing or funding provided to a venture company as:

- (a) capital expenditure and/or working capital to initiate commercialisation of a technology or product;
- (b) additional capital expenditure and/or working capital to increase production capacity, marketing or product development; or
- (c) an interim funding for venture companies expecting to be listed on the official list of a stock exchange.

For products or activities that are not on the Malaysian Exchange Of Securities Dealing & Automated Quotation (MESDAQ)’s list of technology-based activities, subclauses (b) or (c) would only be applicable if the financing or funding has been provided for from seed-capital or start-up stage.

“seed-capital financing” means financing or funding provided to a venture company, for the purposes of research, assessment and development of an initial concept and/or prototype.

“start-up financing” means financing or funding provided to a venture company for product development and initial marketing.

(e) Tour Operators

(i) Incentive for bringing in Foreign Tourists

Exemption from tax on income earned from the business of operating tours provided that the tour operators are licensed with the Ministry of Culture, Arts & Tourism and the tour operators bring in at least 500 foreign tourists per year through group tours. This incentive is extended until year of assessment 2001 (current year basis).

(ii) Incentive for Domestic Tourism

Exemption from tax on income earned from the business of operating tours provided that the tour operators are licensed with the Ministry of Culture, Arts and Tourism and the tour operators conduct domestic tour packages with at least 1,200 local tourists per year. For this purpose, a domestic tour package means any tour package within Malaysia participated by local tourists (individuals who are Malaysian citizens or residing in Malaysia) inclusive of transportation by air, land or sea and providing at least one night accommodation. This incentive is extended until year of assessment 2001 (current year basis)

(f) Organisers of International Conference

Local companies which organise international conferences in Malaysia will be eligible for income tax exemption on income earned from bringing at least 500 foreign participants per year into the country.

(g) Promotion of Export

- (i) exemption of statutory income equivalent to 10% of the value of

increased exports is given to manufacturers provided that the goods exported attain at least 30% value added;

(ii) exemption of statutory income equivalent to 15% of the value of increased exports is given to manufacturers provided that the goods exported attain at least 50% value added;

(iii) exemption of statutory income equivalent to 10% of the value of increased exports is given to companies which export fruits and cut flowers;

(iv) exemption of statutory income equivalent to 10% of the value of increased exports is given to companies in selected services sector as follows:

- (a) legal;
- (b) accounting;
- (c) engineering consultancy;
- (d) architecture;
- (e) marketing;
- (f) business consultancy;
- (g) office services;
- (h) construction management;
- (i) building management;
- (j) plantation management;
- (k) health;
- (l) education;
- (m) publishing; and
- (n) information and communication technology

(h) Promotion of Car and Motorcycle Racing Events

Drivers and organisers of car and motorcycles racing of international standard held in Malaysia are eligible for:

- (i) full tax exemption on income earned by the drivers;

- (ii) 50% tax exemption on income earned by the organisers.

(i) Promotion of Boat/Yacht Maintenance Activities in Langkawi

Companies undertaking repair and maintenance activities of luxury boats and yacht in Langkawi are eligible for full income tax exemption for 5 years.

(j) Incentive for Investor and Producer engaged in Food Production

First alternative :

- (i) a company which invest in a subsidiary company engaged in food production will be granted tax deduction equivalent to the amount of investment made in that subsidiary; AND

- (ii) the subsidiary company undertaking food production will be given income tax exemption of 100% on its statutory income for 10 years commencing from the first year the company enjoys profit in which:

- (a) losses incurred before the exemption period is allowed to be brought forward after the exemption period of 10 years .

- (b) losses incurred during the exemption period is also allowed to be brought forward after the exemption period of 10 years; and

- (c) dividends paid from the exempt income be exempted in the hand of the shareholders

OR

Second alternative :

- (i) the company which invests in the subsidiary company engaged in food production will be given group relief

for the losses incurred by subsidiary company before it records any profit;
AND

- (ii) the subsidiary company undertaking food production be given income tax exemption of 100% on its statutory income for 10 years commencing from the first year the company enjoys profit in which:
 - (a) losses incurred during the exemption period is also allowed to be brought forward after the exemption period of 10 years; and
 - (b) dividends paid from the exempt income be exempted in the hand of the shareholders

The incentives are granted with the following conditions:

- (i) the investing company should own 100% of the subsidiary company that undertakes food production;
- (ii) the eligible food products are as approved by the Minister of Finance. Initially the approved food products are kenaf, vegetables, fruits, herbs, spices, aquaculture and rearing of cattle, goat and sheep; and
- (iii) the food production project should commence within a period of one year from the date the incentive is approved.

Application for these incentives should be submitted to the Ministry of Agriculture before **31 December 2003** for the approval of the Minister Of Finance .

(2) Investment Allowance (IA) (Schedule 7B)

IA is an alternative to income tax exemption under section 127 for companies undertaking ASP. Under the IA, the quantum of allowance varies as follows:

- (i) companies undertaking ASP will be granted IA of 60% in respect of qualifying

capital expenditure incurred within 5 years from the date the capital expenditure is first incurred. The allowance can be utilised to set off against 70% of the statutory income;

- (ii) companies undertaking ASP in Sabah, Sarawak and the designated eastern corridor of Peninsular Malaysia will be granted IA of 80% in respect of qualifying capital expenditure incurred within 5 years from the date the capital expenditure is first incurred. The allowance can be utilised to set off against 85% of the statutory income;
- (iii) companies undertaking ASP of national and strategic importance will be granted IA of 100% in respect of qualifying capital expenditure incurred within 5 years from the date the capital expenditure is first incurred. The allowance can be utilised to set off against 100% of statutory income.

Note:

- Dividends paid out of tax-exempt income to shareholders will also be exempted.
- Any unutilised allowance can be carried to the subsequent years until it is fully utilised.

(3) Reinvestment Allowance (RA)

RA is given to manufacturing and agricultural companies producing essential food (rice, maize, vegetable, tubers, livestock farming, production of aquatic products and any other activities approved by the Minister of Finance) undertaking expansion, modernisation and diversification activities.

The level of RA granted are as follows:

- (a) Projects in promoted areas such as Sabah, Sarawak and designated Eastern Corridor of Peninsular Malaysia which covers Kelantan, Terengganu, Pahang and the district of Mersing in Johor.
 - RA of 60% in respect of qualifying capital expenditure incurred. The

allowance can be utilised to set off against 100% of statutory income in the year of assessment.

(b) Projects in non-promoted areas (Western Corridor of Peninsular Malaysia);

(i) The RA of 60% in respect of qualifying capital expenditure. The allowance can be utilised to set off up to 70% of statutory income in the assessment year. The balance of the statutory income will be taxed at the prevailing company tax rate.

(ii) Companies that carry out reinvestment which can improve their productivity level significantly will be granted RA of 60% which is allowed to be utilised to set off against 100% of statutory income.

Definition of “significant increase in productivity”

The process efficiency ratio (PER) has increased by at least the same rate as the GDP growth rate for that industry.

Formula : Process Efficiency Ratio (PER)

$$\text{PER} = \frac{\text{Total Output} - \text{BIMS}}{\text{Total Input} - \text{BIMS}}$$

Whereby, BIMS (Bought in materials and services) is defined as value of materials consumed in the production process (including payment for the transport, tax paid including those on materials) + value of equipment used such as packaging materials, daily used materials (including office stationery, materials for improvement and maintenance) + publication cost + lubricants + cost of goods sold in same condition such as utilities (water, electricity and fuels) + payments to contractors + payment to industrial work done by others + payment for non-industrial services.

Eligibility criteria:

- (i) The company must be in operation for at least 12 months.
- (ii) The RA will be given for a period of 5 years beginning from the year the first reinvestment is made;
- (iii) Assets acquired from RA cannot be disposed within 2 years of reinvestment.

(4) Double Deduction Incentive

i. Research & Development (R&D)

The types of R&D that are eligible for the double deduction are :

(a) Approved Research- Section 34A of Income Tax Act 1967

Double Deduction on non-capital expenditure incurred on research and development approved by the Minister of Finance (delegated to the Inland Revenue Board).

(b) Payment for Services- Section 34B (1) (b) & (c) Double deduction on payment for use of services of:

- (i) approved research institutions;*
- (ii) approved research and development (R&D) company;**
- (iii) a contract research and development (R&D) company.**

Note:

*Approved research institution includes the following:

- (i) all government research institutions, including institutions corporatised under Section 24 of the Companies Act 1965;
- (ii) government funded universities which undertake research that conform to the definition of R & D as indicated above.

** R&D company or contract R&D company refer to companies which are established in conformity with Section 2 of the Promotion of Investments Act 1986.

(c) Cash Contributions Section 34B (1) (a)

Double deduction on cash contributions made to approved research institutions. The list of approved research institutions as at 19 October 2001 are:

- (i) Malaysian Agricultural Research and Development Institute (MARDI)
- (ii) Rubber Research Institute of Malaysia (RRI)
- (iii) Forest Research Institute Malaysia (FRIM)
- (iv) Malaysian Institute of Micro Electronic System (MIMOS)
- (v) Palm Oil Research Institute of Malaysia (PORIM)
- (vi) Standard and Industrial Research Institute of Malaysia (SIRIM)
- (vii) Mineral Research Institute
- (viii) Malaysian Centre for Remote Sensing (MACRES)
- (ix) Veterinary Research Institute
- (x) Fisheries Research Institute
- (xi) Institute for Medical Research (IMR)
- (xii) Malaysian Institute for Nuclear Technology Research (MINT)
- (xiii) Unit Pengurusan Penyelidikan, Universiti Kebangsaan Malaysia (UKM)

- (xiv) Pusat Inovasi dan Perundingan, Universiti Sains Malaysia (USM)
- (xv) Pusat Penyelidikan dan Perundingan, Universiti Utara Malaysia (UUM)
- (xvi) Unit Penyelidikan, Universiti Putra Malaysia (UPM)
- (xvii) Pusat Penyelidikan, Universiti Islam Antarabangsa Malaysia (UIAM)
- (xviii) Unit Perundingan, Universiti Malaya (UM)
- (xix) Unit Penyelidikan dan Pembangunan, Universiti Teknologi Malaysia (UTM)
- (xx) Unit Penyelidikan, Universiti Malaysia Sabah (UMS)
- (xxi) Unit Pemindahan Teknologi & Perundingan, Universiti Malaysia Sarawak (Unimas)
- (xxii) Pusat Sains dan Teknologi Pertahanan, Kementerian Pertahanan
- (xxiii) Biro Penyelidikan dan Perundingan, Universiti Teknologi MARA (UiTM)

For purposes of this incentive, R&D is defined as follows:

“Research and development (R&D) means any systematic or intensive study undertaken in the field of science or technology with the object of using the results of the study for the production or improvement of materials, devices, products, produce or processes but does not include:

- (i) quality control of products or routine testing of materials, devices, products or produce;
- (ii) research in the social sciences or the humanities;

- (iii) routine data collection;
- (iv) efficiency surveys or management studies;
- (v) market research or sales promotion; and
- (vi) with effect from year of assessment 1998, a company carried out designing or prototyping as an independent activity will also qualify for R&D incentives"

ii. Training

Effective from 1 July 1993 double deduction for expenses on training will be considered only for companies which do not contribute to the Human Resource Development Fund (HRDF) and the trainees must be full-time employees who are Malaysian citizens.

(a) Approved Training Institutions

Companies, including those in the services sector not covered by the Human Resources Development Fund (HRDF) are eligible for double deductions on training expenses if such training were to be undertaken in approved training institution or government training institutions. Companies undertaking training in approved training institutions could claim double deduction on expenses billed by the respective approved training institutions. (No other expenses are allowed for double deduction). The approved training institutions as at 19 October 2001 are as follows:

- (i) National Productivity Corporation (NPC)
- (ii) Standard and Industrial Research Institute of Malaysia (SIRIM)
- (iii) Universiti Teknologi Mara (UiTM)
- (iv) Malaysian Agricultural Research and Development Institute (MARDI)
- (v) Forest Research Institute of Malaysia (FRIM)

- (vi) The Centre For Instructor and Advanced Skill Training (CIAST)
- (vii) Penang Skills Development Centre (PSDC)
- (viii) Institut Kemahiran Mara (IKM)
- (ix) Industrial Training Institute (ITI)
- (x) German-Malaysia Institute (GMI)
- (xi) Malaysia Timber Industry Board (MTIB)
- (xii) Federation of Malaysian Manufacturer - Entrepreneur and Skills Development Centre (FMM-ESDC) (certain programmes only)
- (xiii) Perak Entrepreneur and Skills Development Centre (PESDC)
- (xiv) Tuas Polytech (British Malaysian Institute)
- (xv) ASEAN Timber Technology Centre (ATTC)
- (xvi) Sarawak Timber Industry Development Corporation (STIDC)
- (xvii) Kedah Industrial Skills & Management Development Centre (KISMEC)
- (xviii) Malaysia France Institute (MFI)
- (xix) Selangor Human Resource Development Centre (SHRDC)
- (xx) Pusat Pembangunan Tenaga Industri Johor (PUSPATRI)
- (xxi) Malaysian Institute of Nuclear Technology (MINT)
- (xxii) Pahang Skills Development Centre

(b) Approved Training Programmes

- (i) Manufacturing companies in production

Manufacturing companies undertaking training programmes locally or overseas approved by MIDA for the purpose of upgrading/developing

craft, supervisory skills, technical skills, productivity and quality improvements.

- (ii) Manufacturing companies not yet in production

Qualified manufacturing companies undertaking training programmes that are approved by MIDA for the purpose acquiring/developing craft, supervisory or technical skills, that can contribute to future production.

- (iii) Training for handicapped person

A company which incurred training expenses in the training of any handicapped person who is not an employee of the company. The training should be done either in-house or at any approved training institution in Malaysia. Such handicapped person must be classified as handicapped by the Ministry of National Unity and Social Development and the training undertaken must serve to enhance his/her employment prospect.

- (iv) Tourism Industry

Companies in the hotel or tour operating business which undertake training for the purpose of upgrading the level of skills and professionalism in the tourism industry and approved by the Minister of Culture, Arts and Tourism.

- (iv) Non-manufacturing Companies

Non-manufacturing companies that send their employees to attend training programmes approved by the Ministry of Finance in the following institutions as at 19 October 2001 are:

- (a) Institute Bank-Bank Malaysia (IBBM)
- (b) Malaysian Insurance Institute (MII)

- (c) Persekutuan Penghantar Fret Malaysia

- (d) Association of Consulting Engineers Malaysia (ACEM)

- (e) Persatuan Elektrik & Elektronik

- (f) AFCM Training Services Sdn. Bhd

- (g) Institut Pengurusan (Malaysia) (MIM)

- (h) Institut Jurutera Malaysia (IEM)

iii. Freight Charges

- (a) Double deduction on freight charges for manufacturers in Sabah & Sarawak who export rattan and wood-based products.
- (b) Double deduction on freight charges for all manufacturers who ship their goods from Sabah & Sarawak to Peninsular Malaysia provided they use the ports in Peninsular Malaysia. This incentive is effective from the year of assessment 2000 (current year basis).

iv. Insurance Premiums

- (a) Double deduction on premiums paid for export credit insurance.
- (b) Double deduction on insurance premiums paid for the import of goods provided the risk are insured with an insurance company incorporated in Malaysia.
- (c) Double deduction on insurance premiums paid for export of goods provided the risk are insured with an insurance company incorporated in Malaysia.

v. Overseas Promotion

- (a) Tourism Industry

Double deduction for tourism industry is granted on expenditure incurred by hotels

and tour operators for overseas promotions as follows:

- (i) expenditure on publicity and advertisement in any mass media outside Malaysia;
- (ii) expenditure on the publication of brochures, magazines and guide books, including delivery costs which are not charged to the overseas customers;
- (iii) expenditure on market research to explore for new markets overseas, subject to the prior approval of the Ministry of Culture, Arts and Tourism;
- (iv) expenditure which includes fares to any country outside Malaysia for purposes of negotiating or securing a contract for advertising or participating in trade fairs, conferences or forum approved by the Ministry of Culture, Arts and Tourism. Such expenses are subject to a maximum for RM200 per day for lodging and RM100 per day for food for the duration of the stay overseas;
- (v) expenditure for organising trade fairs, conferences or forum approved by the Ministry of Culture, Arts and Tourism; and
- (vi) maintenance of sales office overseas.

(b) Approved International Trade Fairs

Double deduction is allowed for expenditure incurred by a company for participating in an approved international trade fair held in Malaysia.

(c) Export of services

Double deduction incentive on expenses incurred pertaining to promotion of export of services, which is currently available to the tourism sub sector, is extended to the entire services sector.

The expenses eligible for double deduction are as follows:

- (i) export market research;
- (ii) preparation of tenders for the supply of services overseas;
- (iii) supply of technical information abroad;
- (iv) fares in respect of overseas business travel by employees;
- (v) accommodation and sustenance expenses incurred by Malaysian businessmen going overseas for business, subject to RM200 per day for lodging and RM100 per day for food;
- (vi) cost of maintaining office overseas for purpose of promotion of services; and
- (vii) professional fees incurred in packaging design for exports.

Double deduction on promotion of export of services for companies eligible for tax incentives under Section 127 or Schedule 7B of the Income Tax Act 1967, is allowed to be accumulated and offset against their post-exemption income.

vi. Promotion of Local Brand Name

Double deduction is granted for 'qualifying advertising expenditure' incurred within Malaysia in respect of Malaysian brand name goods.

For purposes of this incentive the 'qualifying advertising expenditure' refers to the following:

- (a) advertisements on the Internet where the host website is located in Malaysia;
- (b) advertisements in magazines and newspaper where the magazines and newspapers are printed in Malaysia;
- (c) advertisements on local licensed television stations;

- (d) advertisements approved by the relevant local authority on advertisement hoardings located in Malaysia;
- (e) advertisements in trade publications where the trade publications are printed in Malaysia;
- (f) advertisements in any form in the course of sponsoring an approved international sporting event in Malaysia; and
- (g) advertisements in any form in the course of sponsoring an approved international trade conference or an approved international trade exhibition held in Malaysia.

To be eligible for this incentive, the local brands must satisfy the following criteria:

- (a) brand name is owned by a company which is locally incorporated with at least 70% Malaysian owned;
- (b) the brand name is registered in Malaysia;
- (c) the brand name product must achieve export quality standards; and
- (d) expenditure incurred in advertising must be incurred in Malaysia.

(5) Single Deduction

- (a) Approved Investment Overseas.

Single deduction on pre-operating expenses such as cost of market research for approved investment overseas.

- (b) Training Expenses.

Single deduction on pre-operating training expenses incurred by any company.

- (c) Technical or Vocational Training Institute.

Single deduction for contribution in cash to a technical or vocational training institute established and maintained by the Government or statutory body.

- (d) Organisation for the Promotion and Conservation of the Environment.

Single deduction for donations to an approved organisation established exclusively for the protection and conservation of the environment.

- (e) Single deduction for gift under Section 44(6A).

Single deduction for an amount equal to value as determined by the Department of Museums & Antiquities, the National Archives or National Art Gallery of any gift or artefact or manuscript made to the State/National Art Gallery, Government or State Government.

- (f) Single deduction for an amount equal to expenditure incurred:

- (i) on the provision of services, public amenities and contribution to a charity or community project pertaining to education, health, housing and infrastructure and information & communication technology approved by the Minister of Finance.

- (ii) on the provision and maintenance of a child care centre for the benefit of persons employed by him in his business;

- (iii) in establishing and managing a musical or cultural group approved by the Minister;

- (iv) on sponsoring local and foreign cultural performances approved by the Ministry of Culture, Art and Tourism.

- (v) as operational expenditure including payments to consultants related to the usage of IT to improve management and production processes,

- (vi) in obtaining quality systems and standards and halal certification.

(6) Industrial Building Allowance

Industrial Building Allowance (IBA) is granted to companies incurring capital expenditure on construction or purchase of a building which is used for specific operational purposes as per Schedule 3 of the Income Tax Act 1967.

The IBA consists of a normal IBA which would enable the capital expenditure to be fully utilized within 45 years by allowing an initial allowance of 10% and an annual allowance of 2%. Whereas a special IBA to enable the capital expenditure to be utilized within a shorter period is given by allowing allowances at higher rates.

For normal IBA, it is granted to a building used for the purposes of a business and the building is used as:

- (a) a factory;
- (b) a dock, wharf, jetty or other similar building;
- (c) a warehouse and the business consists or mainly consists of the hire of storage space to the public;
- (d) water or electricity supply projects or telecommunication project for the public;
- (e) a licenced private hospital, maternity home and nursing home;
- (f) a hotel building which has been constructed or purchased during the Pioneer Status or Investment Tax Allowance incentive period;
- (g) a public road or ancillary structures which expenditure is recoverable through toll collection;
- (h) a building to carry out an Approved Service Sector Projects;
- (i) a building constructed by a person pursuant to an agreement entered into between that person and the government on a *build -lease - transfer basis* subject to the approval of the Minister;
- (j) in connection with the working of a farm and the business consists or mainly consists of the working of the farm, with or without other farms;

- (k) in connection with the working of a mine and the business consists or mainly consists of the working of a mine, with or without other mines; and
- (l) for the purpose of research approved by the Minister, research and employees training undertaken by a company which is participating in industrial adjustment project approved under the Promotion of Investment Act 1986 and research undertaken by a research and development company or a contract research and development company as defined under Section 2 of the Promotion of Investment Act 1986.

A special IBA is given in the form of 10% allowance of the expenditure incurred for the construction or purchase of buildings. This would enable the expenditure to be fully utilised within 10 years on the followings:

- (a) buildings which are used for the purposes of storage of goods for exports or for the storage of imported goods which are to be processed and distributed or re-export;
- (b) buildings for the purposes of industrial, technical or vocational training approved by the Minister;
- (c) buildings for a school or an educational institution approved by the Minister of Education;
- (d) buildings for the purposes of living accommodation for employees in manufacturing, Approved Services Project and hotel or tourism business;
- (e) buildings for the purposes of the provision of child care facilities for employees.

A more special IBA is given in the form of 20% allowance to enable the expenditure to be fully utilized within 5 years to a building used for the purposes of a business of that person which consists wholly or partly of the working of the farm, or the construction on that farm of a building which is provided by that person for the welfare of persons, or as living accommodation for a person employed on or in connection with the working of that farm.

(7) Accelerated Capital Allowance

- (a) Computer and information technology assets.

Initial allowance of 20% and annual allowance of 40%.

- (b) Environmental protection equipment.

Initial allowance of 40% and annual allowance of 20%.

- (c) Deduction for acquiring property rights

Capital expenditure on acquiring proprietary rights such as patent, industrial design and trademarks is allowed as deduction of 10% on the cost of the acquisition of the proprietary rights for 10 years.

(8) Deduction for Capital Expenditure on Approved Agricultural Projects

Capital expenditure on approved agricultural projects under schedule 4A of the Income Tax Act, 1967 allows a person carrying on an approved agricultural project to elect so that the qualifying capital expenditure incurred by him in respect of that project is deducted from his aggregate income, including income from other sources. Where there is insufficient aggregate income for the qualifying farm, expenditure to be deducted from the unabsorbed expenditure will be carried forward to subsequent years of assessment he so elects, he will not be entitled to any capital allowance or agricultural allowance on that same capital expenditure.

This incentive is not available to companies which have been granted incentive under the Promotion of Investment Act, 1986 and the repealed Investment Incentive Act, 1968 and whose tax relief period have not started or have not expired.

The qualifying capital expenditure eligible for deduction for purposes of this incentive are as follows:

- (a) the clearing and preparation of land;

- (b) the planting (but not replanting) of a crop relating to an approved agricultural project;
- (c) the construction on a farm of a road or bridge;
- (d) the construction on a farm of a building used for the purposes of an approved agricultural project which is carried out on that farm or the construction on that farm of building provided for the welfare and accommodation of persons employed in that project and which, if that project ceased to be carried out, is likely to be little or no value to any person except in connection with the working of another farm;
- (e) the construction of a pond or the installation of an irrigation or drainage system which is used for the purpose of an approved agricultural project.

Only expenditure incurred within a specific time frame and in respect of a farm cultivation and utilising a specified minimum hectareage for each approved project as stipulated by the Minister of Finance will qualify. The approved projects are as follows:

	Project	Period	Minimum Hectarage
1.	Aquaculture (Prawns)	2 years	40 hectares
2.	Cultivation of Crops:		
	Papaya	1 year	40 hectares
	bananas	1 year	40 hectares
	passion fruit	1 year	40 hectares
	star fruit	2 years	8 hectares
	guava (jambu)	2 years	8 hectares
	mangosteen	7 years	8 hectares
3.	Floriculture*	2 years	8 hectares

* (Plants, bulbs, tubers and roots with or without flowerbuds, of the kind specified in chapter 6 of the Custom Duties Order 1988, which are suitable for planting or ornamental use, excluding mushroom spawn, budded or seedling rubber stumps and rubber budwood.

(9) Special Tax Treatment for Gift

(a) Training Activity

Special tax treatment for donation of used machinery or equipment, to a technical or vocational training institute established and maintained by the Government or statutory body or technical or vocational training institute approved by the Minister of Finance.

(b) Research Activity

Special tax treatment for donation of used machinery or equipment to approved research institutes.

(c) For both (a) & (b)

The disposal value of such machinery or equipment is deemed as zero. Any unutilised capital allowance (residual expenditure) in respect of the machinery or equipment will be given full deduction in the year of assessment in which the machinery or equipment are donated.

Prior to this, the disposal value of such gifts is taken to be the market value and if the value is higher than the utilised capital allowance, the donor is subject to tax on the balancing charge.

(10) Tax Exemption to Promote Labuan as International Offshore Financial Centre (IOFC)

(i) Dividends received from an offshore company, which are paid, credited or distributed out of income derived from an offshore business activity is exempted from income tax. If the shareholder of the offshore company is a domestic company in Malaysia, the income from such dividends enjoys second-tier exemption.

(ii) Royalties received from an offshore company by a non-resident or another offshore company is exempted from income tax.

(iii) Interest received from an offshore company by a non-resident or another offshore company is exempted from income tax.

(iv) Technical and management fees received from an offshore company by a non-resident or another offshore company is exempted from income tax.

(v) Distributions received from an offshore trust by the beneficiaries are exempted from tax.

(vi) Documents for offshore business activities, transfer of shares in an offshore company and Memorandum & Articles of Association of an offshore company is exempted from stamp duty.

(vii) 65% tax exemption on statutory income of Labuan trust company and service providers providing qualifying professional services of accounting, financial, legal and secretarial services to offshore company until the year of assessment 2004.

(viii) 50% tax exemption on gross income of non-citizen employee working in a managerial capacity in an offshore company until the year of assessment 2004

(ix) 50% tax exemption on gross income of a non-citizen trust officer working in a trust company until the year of assessment 2004.

(x) 50% tax exemption on Labuan and housing allowances of citizen working in an offshore company and government services in Labuan.

(xi) Withholding tax exemption on rental payment to non-residents from the use of moveable property by an offshore leasing company.

(xii) Duty free goods for individuals whose period of stay in Labuan is 24 hours (formerly 72 hours).

C. Labuan Offshore Business Activity Tax Act 1990 (LOBATA)

- I. Offshore companies in Labuan undertaking offshore trading activities can choose either to:
 - (i) pay tax at a rate of 3% from the net profit; or
 - (ii) pay RM20,000.
- II. Income of offshore companies from non-trading activities is not subject to any tax.
- III. Where an offshore company carrying on both offshore trading and non-trading activity, it is deemed to be carrying on offshore trading activity.

D. Customs Act 1967, Sales Tax Act 1972, Excise Act 1976 and Free Zones Act 1990

(1) Manufacturing Sector

- (a) Import duty exemption on raw materials/components used in:
 - (i) Production for export market
Raw materials/components used directly and not manufactured locally, or manufactured locally but not of acceptable quality and price.
 - (ii) Production for domestic market
Raw materials/components used directly and not available locally, with effect from 1 January 1999.
- (b) Import duty/excise duty and Sales Tax exemption for machinery and equipment
 - (i) not available locally and used directly in the manufacturing process;

- (ii) locally purchased machinery/equipment used directly in the manufacturing process.

Duty exemption on spares and consumables was withdrawn in 1996 to encourage domestic production. However to reduce cost of production in the midst of economic turmoil, duty exemption was granted selectively based on specific criteria until 31 December 2003. The criteria are as follows:

- (i) Company must export at least 80% of their production;
- (ii) spares and consumables that have limited demand and not feasible for domestic production;
- (iii) Import duty on such items exceed 5%.

(c) Duty Drawback

Manufacturers who have paid duty on the import of raw materials & components used for the production of goods for export within a year are eligible to claim drawback on the duty paid. Drawback can be claimed from the Customs Department but subject to the conditions under Section 99 of the Customs Act, 1967.

(d) Sales Tax Exemption

Manufacturers of taxable goods with annual sales turnover exceeding RM100,000 are required to be licensed under Sales Tax Act 1972 and be eligible for exemption from sales tax on inputs (in line with single stage tax concept). However manufacturers with annual sales turnover less than RM100,000, have the option either to obtain exemption from sales tax on inputs (by being licensed) or pay sales tax on inputs but enjoy exemption on output.

There are few categories of goods exempted at both the input and output stage, i.e all goods(including packing materials) used in the manufacture of the following;

- (i) controlled articles(goods);
- (ii) pharmaceutical products;
- (iii) milk products;
- (iv) batik fabrics;
- (v) perfumes and eau d' toilette, beauty or make-up preparations, photographic cameras, wrist-watches, pens;
- (vi) computers and computers peripherals, parts and accessories;
- (vii) carton boxes, corrugated paper or paperboard, folding carton boxes and cases of non-corrugated paper and paperboard;
- (viii) products in the printing industry;
- (ix) agricultural or horticultural sprayers;
- (x) plywood;
- (xi) re-treaded tyres;
- (xii) uninterruptible power systems;
- (xiii) machinery; and
- (xiv) manufactured goods for export.

(2) Agricultural Sector

- (a) Full import duty exemption on raw materials/components used in:
 - (i) Production for export market. Imported direct raw materials/ components not available locally or available locally but not of acceptable quality and price.

- (ii) Production for domestic market. Direct raw materials/ components not available locally.

- (b) Full import/excise duty and sales tax exemption on machinery/ equipment

Full exemption from:

- (i) imported machinery/ equipment not available locally.
- (ii) locally purchased machinery/ equipment.

(3) Service Sector

- (a) Import duty and sales tax exemption on raw materials/ components for imported raw materials/components used directly in the implementation of ASP and are not available locally.
- (b) Excise duty and sales tax exemption on machinery/ equipment for locally purchased machinery/equipment used in the implementation of ASP.

(4) Tourism Sector

Duty exemption on materials/ equipment for accommodation and non-accommodation tourism projects

Full exemption from:

- (a) import duty and sales tax on identified imported materials/ equipment.
- (b) sales tax and excise duty on identified locally purchased equipment.

(5) Film & Music Sector

Duty exemption on equipment for recording studios, production houses and cineplexes.

Full exemption from:

- (a) import duty and sales tax on identified imported equipments.
- (b) sales tax and excise duty on selected locally purchased equipment.

(6) Research Activity

Duty exemption on machinery/equipment, materials, raw materials and samples used for approved research projects, in house research, contract research and development company .

Full exemption from:

- (a) import duty and sales tax on imported items.
- (b) sales tax and excise duty on locally purchased items.

(7) Training Activity

Duty exemption on machinery/equipment, materials, raw materials and samples used in approved training programme or by an approved training institution and technical or vocational training company.

Full exemption from:

- (a) import duty and sales tax on imported items.
- (b) sales tax and excise duties on locally purchased items.

(8) Environment Protection

- (a) Manufacturing companies that purchase machinery/equipment for pollution control.

Full exemption from:

- (i) import duty and sales tax on imported machinery/equipment not available locally.

- (ii) sales tax and excise duty on locally purchased machinery/equipment.

- (b) Companies undertaking storage, treatment and disposal of toxic and hazardous wastes.

Full exemption from:

- (i) import duty and sales tax on imported machinery/equipment that are not available locally.
- (ii) sales tax and excise duty on locally purchased machinery/equipment.

The level and criteria of exemption on raw material/component are the same as the exemption on raw material/component for the manufacturing sector.

- (c) Catalytic Converters

Exemption from import duty and sales tax on catalytic convertors used in motor vehicle assemblers.

- (d) Companies providing energy conservation services & Companies which incur capital expenditure arising from energy conservation measures undertaken in their own company.

Full exemption from:

- (i) import duty and sales tax on imported machinery/equipment that are not available locally.
- (ii) sales tax and excise duty on locally purchased machinery/equipment.

- (e) Companies utilising biomass as a new source of energy.

Full exemption from:

- (i) import duty and sales tax on imported machinery/ equipment that are not available locally.
- (ii) sales tax and excise duty on locally purchased machinery/ equipment.

- (9) **All goods except petroleum and petroleum products are exempted from sales tax, as Labuan is a free port.**

- (10) **Incentives for International Procurement Centres (IPCs)**

IPC are exempted from import duties on raw materials, components and finished products into the Free Zone or Licensed Manufacturing Warehouses under section 11, Free Zones Act 1990 and section 14, Customs Act 1967.

Non-tax incentives includes:

- (a) expatriate posts will be approved based on requirement of IPC;
- (b) open one or more foreign currency accounts with any licensed commercial bank to retain their export proceeds without any limit imposed;
- (c) enter into foreign exchange forward contracts with any licensed commercial bank to sell forward export proceeds based on projected sales; and
- (d) exempted from the requirements of the Ministry of Domestic Trade and Consumer Affairs Guidelines on foreign equity ownership on wholesale and retail trade.

The term IPC refers to a locally incorporated company, local or foreign owned, which carries on a business in Malaysia to undertake procurement

and sales of raw materials, components and finished products from local or third countries to its group of related and unrelated companies in Malaysia or abroad.

In order to qualify for the whole package of incentives offered, the IPC must be an 'approved IPC status company'. To qualify as an 'approved IPC status company' it must satisfy the following conditions:

- (a) locally incorporated under the Company's Act 1965 with a minimum paid-up capital of RM0.5 million;
- (b) a minimum total operating expenditure of RM1.5 million per year;
- (c) a minimum annual business turnover (sales) of RM100 million; and
- (d) goods to be handled directly through Malaysian ports and airports.

SUMMARY OF DIRECT & INDIRECT TAX INCENTIVES BY SECTORS

(1) Manufacturing Sector

- (a) Pioneer Status or Investment Tax Allowance
- (b) Industrial Adjustment Allowance
- (c) Infrastructure Allowance
- (d) Reinvestment Allowance
- (e) Industrial Building Allowance
- (f) Double deduction on expenses for export promotion
- (g) Double deduction for participating in approved international trade fair in Malaysia
- (h) Double deduction for promotion of Malaysian brand names
- (i) Double deduction incentive for research and development

- (j) Double deduction incentives for training
- (k) Double deduction incentives on freight charges
- (l) Double deduction on export credit insurance premium
- (m) Single deduction on pre-operating training expenses
- (n) Single deduction on expenses incurred for obtaining quality systems and halal certification and accreditation
- (o) Tax exemption on the value of increased exports
- (p) Accelerated Capital Allowance
 - use of environmental protection equipment
 - use of computers and information technology assets
 - upon expiry of reinvestment allowance only for companies that reinvest in promoted products
- (q) Duty exemption on machinery, equipment, raw materials & components for:
 - producing manufactured goods
 - research activity
 - training activity
 - environmental protection
- (h) Double deduction for promotion of exports
- (i) Double deduction on export credit insurance premium
- (j) Tax exemption on the value of increased exports
- (k) Special tax treatment for gifts in cash
- (l) Duty exemption on machinery, equipment, raw materials & components for:
 - producing manufactured goods
 - research activity
 - training activity
 - environment protection
- (m) (i) Tax deduction for the investor company, equivalent to the amount of investment made in a 100% owned subsidiary company engaged in food production AND income tax exemption for 10 years for the subsidiary company engaged in food production; OR
 - (ii) Investor company is given group relief for the losses incurred by the subsidiary company which is owned 100% by the investor company AND income tax exemption for 10 years for the subsidiary company engaged in food production.

(2) Agricultural Sector

- (a) Pioneer Status or Investment Tax Allowance
- (b) Infrastructure allowance
- (c) Reinvestment allowance
- (d) Single deduction on pre-operating training expenses
- (e) Deduction on capital expenditure (agricultural allowance) for approved agricultural projects
- (f) Double deduction incentives for research and development
- (g) Double deduction incentives for training
- (n) Pioneer Status/Investment Tax Allowance for companies providing cold chain facilities and services for perishable local food products.
- (o) Single deduction on expenses incurred for obtaining quality systems and halal certification and accreditation
- (p) Accelerated Capital Allowance
 - use of environmental protection equipment
 - use of computers and information technology assets

(application to be submitted by 31 December 2003)

- upon expiry of reinvestment allowance only for companies that reinvest in production of promoted food items.

(3) Service Sector

(I) Approved Service Projects (ASP)

- (a) Tax Exemption/Investment Allowance
- (b) Industrial Building Allowance
- (c) Duty Exemption on Machinery/ Equipment & Raw Materials/ Components
- (d) Double Deduction Incentive on Promotion of Export of Services
- (e) Double Deduction Incentive For Research & Development (Entire Services Sector)
- (f) Double Deduction Incentive on Training (Entire Services Sector)
- (g) Tax exemption on value of increased export
- (h) Accelerated capital allowance for computers
- (i) Accelerated capital allowance for environment friendly equipment

(II) Tourism Sector

- (a) Pioneer Status/Investment Tax Allowance
- (b) Infrastructure Allowance
- (c) Double deduction incentive for research & development
- (d) Double deduction incentives for training
- (e) Double deduction on overseas promotion
- (f) Double deduction for participating in approved international trade fair in Malaysia
- (g) Single deduction on pre-operating training expenses

- (h) Single deduction on cultural performances
- (i) Industrial Building Allowance
- (j) Accelerated capital allowance for environmental friendly equipment
- (k) Tax exemption for tour operators (Domestic and foreign tourist)
- (l) Tax exemption for promoting international conferences in Malaysia
- (m) Duty exemption on selected materials & equipments for tourism companies, musical studios and
- (n) No import and excise duties on CKD components for locally assembled tourist buses.
- (o) No sales tax on pewterware, camera, watches, lighters, fountain pens, transistor radios, perfumes and cosmetic products.
- (p) Abolishment of service tax in Labuan & Langkawi

(III) Research & Development Activity

- (a) Pioneer Status for Contract Research and Development Company.
- (b) Investment Tax Allowance (ITA) for Research and Development Company and Contract Research and Development Company (as an alternative to PS).
- (c) ITA for in-house research
- (d) Double Deduction Incentive
- (e) Industrial Building Allowance
- (f) Accelerated Capital Allowance
 - use of environmental protection equipment
 - use of computer and information technology assets
- (g) Special Tax Treatment for Gifts

- (h) Duty Exemption on Machinery & Materials

(IV) Training Activity

- (a) Investment Tax Allowance for new & existing Technical or vocational Training Company.
- (b) Double Deduction Incentive for training expenses for SMI
- (c) Single deduction for gift in cash
- (d) Industrial Building Allowance
- (e) Accelerated Capital Allowance
 - for computer and IT assets
- (f) Special Tax Treatment for Gifts
- (g) Duty Exemption on Machinery & Materials

(V) Companies providing cold chain facilities and services.

- Pioneer Status /Investment Tax Allowance

(4) Environmental Protection Activity

- (a) Pioneer Status/Investment Tax Allowance for carrying out promoted product/activity such as:
 - (i) forest plantation project(strategic project);
 - (ii) recycling of agricultural waste or agricultural by-products, chemicals and reconstituted wood-based panel boards or products;
 - (iii) storing, treating and disposing of dangerous toxic and hazardous waste;
 - (iv) energy conservation(application to be submitted by Dec 2002)
 - (v) utilising biomass (application to be submitted by Dec 2002)
- (b) Infrastructure allowance
- (c) Single deduction for gifts in cash
- (d) Accelerated capital allowance for environmental protection equipment

- (e) Duty exemption on machinery, equipment & materials

- (f) Duty exemption on catalytic converters

(5) Investment Activity Overseas

- (a) Tax exemption on income;
- (b) Single deduction on pre-operating expenses for approved investment overseas.

(6) Labuan Offshore Business Activity Tax Act 1990 (LOBATA)

- (i) Offshore companies in Labuan undertaking offshore business can elect to pay tax at a rate of 3% from net profit or pay RM20,000.
- (ii) Income of offshore companies from non-trading activities is not subjected to any taxes.

E. Non-tax Incentives

A number of other non-tax incentives are also provided to spur the private sector to take advantage of investment opportunities that will assist the development of the Malaysian economy. These incentives include:

1. Export Credit Refinancing Facilities;
2. Export Credit Insurance and Guarantee Schemes; and
3. Industrial Technical Assistance Fund.

E1. Export Credit Refinancing (ECR) Scheme

Export Credit Refinancing is a scheme whereby Export Import Bank of Malaysia Berhad (Exim Bank) provides short-term financing to direct/indirect exporters, via the commercial banks.

Objectives of the ECR scheme:

- To promote the export of manufactured products, agricultural products and selected primary commodities that have significant value-added and utilize local content resources;

- To provide exporters with ready access to credit facilities at competitive rates of interest;
- To develop backward linkages in export-oriented industries.

Two types of facilities are available to exporters under the scheme;

- The pre-shipment ECR; and
- The post-shipment ECR

Eligibility for ECR Facilities

Eligible exporter

- Direct exporter either:
 - Manufacturer

- Agricultural products producer
- Trader

- Indirect exporter (supplier of domestic input)

Eligible product

- Product not listed in the Negative List of Exim Bank's Export Credit Refinancing Guidelines;
- Product with a minimum Value Added (VA) of 20 per cent and a minimum Domestic Content (DC) of 30 per cent; or
- Products listed in Appendix 3 of Exim Bank's Export Credit Refinancing Guideline.

Detail of the two facilities are explained as per the following table:

	Pre-shipment ECR		Post-shipment ECR
Purpose	Loan advance to manufacturing/agricultural products producer to facilitate the production of eligible goods or loan advance to trader for purchasing of domestic Intermediate/final products, for export prior to shipment.		Loan advance for a period after shipment to finance the export of eligible goods on usance terms of minimum 30 days
Methods of Financing	Order-Based	Certificate of Performance (CP)	Bills Discounting
User	(a) Direct Exporter – New Exporter; or – Seasonal Exporter; or – Exporter whose maximum exports for the last financial year and the preceding 12 months is less than RM1 million; and (b) Indirect Exporter	Direct Exporter whose maximum exports for the last financial year and the preceding 12 months is RM1 million and above Note: Exporter whose exports for the last financial year and the last preceding 12 months is between RM1 billion to RM3 million can use either order-based or CP method	Direct Exporter whose exports of eligible goods on usance terms of minimum 30 days
Margin of Financing	Max. of 80% of value of export order	Amount specified on the CP	Max. of 100% of value of export bill
Period of Financing	Max. of 4 months	Max. of 4 months.	Min. period of 7 days Max. period of 6 months

Interest Rate	Shall be at Exim Bank's ECR funding rate.	Shall be at Exim Bank's ECR funding rate.	Shall be at Exim Bank's ECR funding rate.
Limit	The max limit of RM50 million loans outstanding at Any one Request for financing limit of exceeding RM50 million is subject to recommendation of exporter's bank.	The eligible amount of financing is segregated into 3 period of 4 months each, subject to a max amount of RM50 million per period. Request for financing limit of exceeding RM50 million is subject to recommendation of exporter's bank.	The max. limit of RM50 million loans outstanding at any one time Request for financing limit of exceeding RM50 million is subject to recommendation of exporter's bank.
Repayment	Upon receipt of: For direct exporter: – export proceeds; or – post-shipment proceeds; whichever is earlier For indirect exporter: – payment from the buyer's bank or – upon maturity of the loan, whichever is earlier	Upon receipt of: – export proceeds and/or post-shipment proceeds or – upon maturity of the loan whichever is earlier	Upon: – receipt of export proceeds; or – maturity of the post-shipment bill whichever is earlier

Future details on the ECR scheme are available in the "Guideline on Export Credit Refinancing (ECR)" issued by Exim Bank.

E2. Malaysia Export Credit Insurance Berhad

Malaysia Export Credit Insurance Berhad (MECIB), incorporated in 1977 is a wholly owned subsidiary of Bank Industri & Teknologi Malaysia Berhad, a Government development financial institution.

MECIB's objective is to help promote Malaysian exports and foreign investments by providing a range of export credit insurance and financing guarantee facilities. MECIB provides protection, whereby it undertakes to indemnify its policyholders for their losses arising from any of the following risks inherent in international trade.

Risks Covered

(i) Commercial Risks

- (a) Buyer's insolvency;
- (b) Buyer's default; and
- (c) Buyer's non-acceptance of goods

(ii) Political Risk

- (a) Blockage or delay in transfer of payments to Malaysia;
- (b) War, revolution and other annoyances, including war between buyer's and exporter's country;
- (c) The imposition of import restrictions;
- (d) Cancellation of import licenses;
- (e) Default of a foreign Government buyer.

Facilities Offered

(a) Short Term Facilities

(i) Comprehensive Policy (Shipments)

This policy covers non-payment resulting from commercial and political risks in respect of goods and commodities exported on credit terms of not more than 180 days. The cover commences from the date of shipment. Percentage of cover is up to 95% of the amount of loss.

(ii) Comprehensive Policy (Contracts)

This policy covers the risks of non-payment for goods specifically produced under a contract of sale for overseas buyers especially where loss can be sustained in the event of the contract being frustrated in the pre-shipment period. Hence, cover commences from the date of the contract. Percentage of cover is up to 95% of the amount of loss.

(iii) Comprehensive Policy (Service)

This policy covers export of services other than tangible goods to overseas clients or principals such as technical or professional assistance; repairs; refits conversion carried out on ships; and payment under royalty agreement etc; on credit terms of not more than 180 days. Cover is effective from date of invoice. Percentage of cover is up to 95% of the amount of loss.

(iv) Bank Letter of Credit Policy (Bank LC Policy)

Bank LC Policy is offered to commercial banks providing post-shipment financing to the exporters selling on LC terms of payment. With the policy, the LC negotiating bank's concerns about the credit standing of the LC issuing bank and/or the political and economic conditions prevailing in the buyers' country are mitigated.

The policy insures the LC negotiating bank for non-reimbursement by the LC issuing bank up to 95% of the face value of the LC.

This policy aims to promote Malaysian export to non-traditional and difficult markets by enabling the commercial banks to finance the exports to these regions.

(b) Medium and Long-Term Facilities

(i) Specific Policy

This policy covers export of capital or semi-capital goods and/or services with lengthy manufacturing and/or payment periods and high contract values. It is tailored to the needs and features of each project or manufacturer in Malaysia. The credit terms must be for a minimum of two years and the policy is issued on a one-off project basis. Percentage of cover is up to 95% of the amount of loss.

(ii) Supplier Credit Guarantee

This guarantee applies to loans given by the financial institutions to finance a Malaysian supplier/exporter/contractor of Malaysian goods and services or Malaysian turnkey contractor undertaking an overseas project.

Without the loan, the Malaysian exporter or turnkey contractor may not be able to implement the project.

To mitigate its balance sheet exposure to political risks in the buying country, the Malaysian exporter or turnkey contractor can insure these risks with MECIB under the Specific Policy.

The percentage of cover for the Supplier Credit Guarantee is determined on case-by-case basis up to a maximum of 100%. The loan, in turn, could provide financing for up to 85% of the Malaysian contract value related to the overseas project

or export transaction. If the contract contains goods other than Malaysian goods and services, a Malaysian content and value added requirement of 30% is necessary.

(iii) Buyer Credit Guarantee

This guarantee is provided to financial institutions lending to a foreign sovereign, public or private buyer for financing the purchase of Malaysian goods and services typically capital goods or turnkey projects whereby disbursement is made directly to the exporter in accordance with the supply contract.

Without the loan, the foreign buyer may not be able to purchase the Malaysian goods and services.

Percentage of cover is on case-by-case basis, but generally, for a loan to a sovereign buyer, a 100% comprehensive coverage is extended. The loan, in turn, could provide financing for up to 85% of the Malaysian contract value related to the overseas project or export transaction. If the contract contains goods other than Malaysian goods and services, a Malaysian content and value added requirement of 30% is necessary.

(iv) Project Finance Guarantee

This guarantee applies to loans given by financial institutions to companies undertaking overseas privatisation projects e.g. Build-Operate-Transfer or Build-Own-Operate-Transfer on limited recourse financing basis where the source of repayment is from the cashflow of the project itself.

Guarantee provided can be in the form of political risks cover only or both political and commercial risks coverage. The extent of commercial risk coverage is determined on case-by-case basis

subject to maximum of 100%. The project is normally required to be financed through injection mix of debt and equity, and, typically a 70:30 mix is ideal for an infrastructure project.

(v) Overseas Investment Insurance

This insurance protects Malaysian investors of their investment typically related to an overseas project either in the form of equity commercial bank loan or shareholder's loan against losses arising from political risks such as restrictions or blockage in repatriation of profits, dividend, loan repayment etc., expropriatory acts by the host government whether directly or indirectly and damages to tangible assets due to war and civil disturbances. On a case-by-case basis, where concession has been awarded to an investor, extended coverage of repudiation of contract by host government may be considered.

Standard coverage of 90% of any investment losses arising from the aforementioned political risks is available.

(vi) Bond Facility

MECIB can either issue bonds or provide guarantee to commercial banks to encourage the issuance of bonds on behalf of the Malaysian companies to meet the requirement of the overseas buyers of Malaysian goods and services.

The types of bonds typically covered are tender bond, advance payment bond and performance bond. Coverage is 100%.

An unfair calling of bond is also available providing protection to Malaysian companies against unfair calling of the bond by the overseas buyer/principal. Standard coverage of 95% is available.

For further information, please contact MECIB at the nearest office:

Kuala Lumpur

Malaysia Export Credit Insurance Berhad
(32522-U)
Level 17, Bangunan Bank Industri, Bandar Wawasan
No 1016, Jalan Sultan Ismail,
P.O. Box 11048
50734 Kuala Lumpur
Tel : 03 - 26910677
Fax : 03 - 26910353
E-mail : mecib@mecib.com.my
Website : www.mecib.com

Penang

Malaysia Export Credit Insurance Berhad
(32522-U)
2nd Floor, 53 Jalan Selat, Taman Selat
P.O. Box 157,
12000 Butterworth,
Penang
Tel : 604 – 3321862
Fax : 604 – 3322172
E-mail : ron@mecib.com.my

Johor

Malaysia Export Credit Insurance Berhad
(32522-U)
2nd Floor, No 95, Jalan Damai
Taman Setia, Off Jalan Stulang Darat
80300 Johor Bahru,
Johor Darul Takzim
Tel : 607 – 2231191
Fax : 607 – 2240370
E-mail : ros@mecib.com.my

E3. Industrial Technical Assistance Fund (ITAF)

The Industrial Technical Assistance Fund (ITAF) was initially set up by the Government with an allocation of RM50 million for the purpose of providing grants to small and medium-scale industries (SMIs). On depletion of the original allocation, an additional RM70 million has been

injected into the fund to be utilised for the following schemes:

- (i) Business Planning and Development Scheme (ITAF1);
- (ii) Process Improvement and Product Development Scheme (ITAF 2);
- (iii) Productivity and Quality Certification Scheme (ITAF 3); and
- (iv) Market Development Scheme (ITAF 4).

SMIs that operate in the manufacturing sector or services directly-related to manufacturing activities and fulfil the following conditions are eligible to apply for assistance:

- (i) Incorporated under the Companies Act 1965;
- (ii) Annual sales turnover not exceeding RM25 million with full-time employees not exceeding 150;
- (iii) At least 70% of their equity are held by Malaysians of which not more than 25% held by large companies;
- (iv) Companies which are not yet in commercial production but possess production facilities or have access to facilities approved by the Government such as the Incubator Scheme or the Technology Park Scheme;
- (v) Priority will be given to SMIs manufacturing products(s) or providing manufacturing-related services promoted under the Promotion of Investments Act (PIA) 1986; and
- (vi) Companies appointed under the Industrial Linkage Programme (ILP).

Assistance is given in the form of a matching grant whereby 50% of the project cost is borne by the Government and the remaining 50% is borne by the applicant company subject to a maximum grant as stipulated for each scheme.

Further information on ITAF can be obtained from:

ITAF Secretariat,
Perbadanan Pembangunan Industri Kecil dan
Sederhana Malaysia (SMIDEC)
701 D, Level 7, Tower D,
Uptown 5,
Jalan SS 21/39,
Damansara Uptown,
47400 Petaling Jaya,
Selangor Darul Ehsan.

Telephone No : 03 – 7660 8585
Fax No : 03 – 7660 1919

II. THE INDUSTRIAL CO ORDINATION ACT, 1975

The objective of the Industrial Co-ordination Act 1975 (ICA) is to ensure orderly development and growth in the manufacturing sector. The ICA requires person(s) engaging in any manufacturing activity to obtain a licence from the Licensing Officer in respect of such manufacturing activity. Only manufacturing companies with shareholders' funds of RM2.5 million and above or engaging 75 or more full-time employees need to apply for a licence under the ICA.

All applications for manufacturing licences should be made in the prescribed form to the Director-General of the Malaysian Industrial Development Authority (MIDA) in Kuala Lumpur, Malaysia. MIDA is the Government's principal agency for the promotion and coordination of industrial development in Malaysia.

The relevant definitions in the ICA are as follows:

- (a) The "Licensing Officer" is the Secretary-General of the Ministry of International Trade and Industry (MITI).
- (b) "Manufacturing activity" means the making, altering, blending, ornamenting, finishing or otherwise treating or adapting any article or substance with a view to its use, sale, transport, delivery or disposal and includes

the assembly of parts and ship repairing but shall not include any activity normally associated with retail or wholesale trade.

- (c) "Shareholders' funds" means the aggregate amount of a company's paid-up capital (in respect of preference shares and ordinary shares and not including any amount in respect of bonus shares to the extent they were issued out of capital reserve created by revaluation of fixed assets), reserves (other than any capital reserve which was created by revaluation of fixed assets and provisions for depreciation, renewals or replacements and diminution in value of assets), balance of share premium account (not including any amount credited there in at the instance of issuing bonus shares at premium out of capital reserve by revaluation of fixed assets) and balance of profit and loss appropriation account.
- (d) "Full-time paid employees" means all persons normally working in the establishment for at least six hours a day and at least 20 days a month for 12 months during the year and who receive a salary. Persons such as traveling sales, engineering, maintenance and repair personnel, or who are paid by and are under the control of the establishment are also included. Full-time paid employees also include directors of incorporated enterprises except those paid solely for the attendance at Board of Directors meetings. Family workers who receive regular salaries or allowances and who contribute to the Employees Provident Fund (EPF) or other superannuation funds are also included in the definition.

1. Guidelines for Approval of Industrial Projects

Malaysia's rapid industrial growth over the past decade has created a high demand for labour in the manufacturing sector. The last few years has seen a tightening in the labour market situation.

In view of this, the Government has set down guidelines for the consideration of industrial project

based on the Capital Investment Per Employee (C/E) Ratio. With effect from 26 August 1995, projects with a C/E Ratio of less than RM55,000 will be defined as labour-intensive and will not be considered for a manufacturing licence or for tax incentives by MITI.

However, projects which fulfil one of the following criteria will be exempted from the above guideline:

- (a) If value-added is more than 30%.
- (b) If the Managerial, Technical and Supervisory (MTS) Index is more than 15%.
- (c) If the project undertakes activities or products listed as promoted activities and products of high technology.
- (d) If the project is located in the Eastern Corridor* of Peninsular Malaysia, Sabah and Sarawak.

2. Expansion of Production Capacity and Diversification of Products

An existing licensed company which proposes to undertake an expansion of production capacity for its approved products or diversification to manufacture additional products is required to submit an application for the expansion or diversification in the prescribed form to MIDA.

III. GUIDELINES ON FOREIGN INVESTMENT

1. Equity Policy In The Manufacturing Sector

The Malaysian Government welcomes foreign investment in the manufacturing sector. In keeping with the objective of increasing Malaysian participation in manufacturing activities, it is the policy of the Government to encourage projects to be undertaken on a joint-venture basis between Malaysians and foreign entrepreneurs.

* The Eastern Corridor of Peninsular Malaysia covers Kelantan, Terengganu, Pahang and the district of Mersing in Johor.

1.1 Equity Policy Applicable to New Investments, Expansion or Diversification

Foreign equity participation in manufacturing projects has been governed by the level of exports. Effective from 31 July 1998, the Malaysian Government has liberalised the equity policy for the manufacturing sector in respect of new investments, expansion or diversification as follows:

- (a) Foreign investors can now hold 100% equity irrespective of the level of exports.
- (b) This relaxation is applicable for all applications received from 31 July 1998 until 31 December 2003 to set up manufacturing projects with the exception of specific activities and products where Malaysians small and medium scale companies have the capabilities and expertise. These activities and products are paper packaging; plastic packaging (bottles, films, sheets and bags); plastic injection moulded components; metal stamping, metal fabrication; wire harness; printing and steel service centres. For these activities and products, the prevailing specific equity guidelines are applicable.
- (c) This policy will apply to all applications received from 31 July 1998 to 31 December 2003, as well as applications already received, but for which decisions are pending.
- (d) All projects approved under this policy will not be required to restructure their equity after the period.
- (e) The Government will review this policy after 31 December 2003.

1.2 Equity Policy Applicable to Existing Companies

- (a) Companies which have been licensed before 31 July 1998 have to comply with the equity condition as stated in the licence. However, for existing

companies undertaking expansion or diversification, the equity policy as in para 1.1 above applies to the expansion and diversification projects.

The equity policy as in para 1.1 above also applies to the following companies:

- (b) Companies previously exempted from the Manufacturing Licence but whose shareholders' funds have now reached RM2.5 million or have engaged 75 or more full-time employees; and
- (c) Existing licensed companies exempted from the equity condition which are required to inform MITI when their shareholders' funds reach RM2.5 million.

1.3 Relaxation of Export Conditions for Existing Manufacturers

To encourage greater levels of industrial linkages and local sources, the Government has relaxed the export conditions imposed on manufacturing companies effective from 1 January 1998 to 31 December 2003. With this relaxation, all existing companies with export conditions can apply to MIDA for an approval to sell in the domestic market as follows:

- up to 100% of their output for those products with nil duty or not produced locally.
- Up to 80% of their output, if the domestic supply is inadequate; or the imports from ASEAN for products with CEPT duties of 5% and below have increased.

The above temporary relaxation of export condition will not affect the current equity structure and incentives of existing companies.

2. Protection Of Foreign Investment

2.1 Equity Ownership

A company that has been approved with a certain equity participation will not be required to restructure its equity at any time, provided that the company continues to comply with the original conditions of approval and retains the original features of the project.

2.2 Investment Guarantee Agreements

Malaysia's readiness to conclude Investment Guarantee Agreements (IGAs) is a testimony of the Government's desire to increase the confidence of foreign investors in Malaysia.

An IGA will provide the foreign investor with the following:

- (a) Protection against nationalisation and expropriation.
- (b) Prompt and adequate compensation in the event of nationalisation or expropriation.
- (c) Free transfer of profits, capital and other fees.
- (d) Settlement of investment disputes under the Convention on the Settlement of Investment Disputes of which Malaysia has been a member since 1966.

Malaysia has concluded Investment Guarantee Agreements with the following countries (in order of precedence): United States of America, Germany, Canada, Netherlands, France, Switzerland, Sweden, Belgo-Luxembourg, United Kingdom, Sri Lanka, Romania, Norway, Austria, Finland, Organisation of Islamic Countries (OIC), Kuwait, Association of South-East Asian Nations (ASEAN), Italy, South Korea, China, United Arab Emirates, Denmark, Vietnam, Papua New Guinea, Chile, Laos, Taiwan, Hungary, Poland, Indonesia, Albania,

Zimbabwe, Turkmenistan, Namibia, Cambodia, Argentina, Jordan, Bangladesh, Croatia, Bosnia Herzegovina, Spain, Pakistan, Kyrgyz Republic, Mongolia, India, Uruguay, Peru, Kazakhstan, Malawi, Czech Republic, Guinea, Ghana, Egypt, Botswana, Cuba, Uzbekistan, Macedonia, North Korea, Yemen, Turkey, Lebanon, Burkina Faso, Republic of Sudan, Republic of Djibouti, Republic of Ethiopia, Senegal and State of Bahrain, Algeria and Saudi Arabia.

2.3 Convention on the Settlement of Investment Disputes

In line with the national policy of promoting and protecting foreign investment, the Malaysian Government in 1966 ratified the provisions of the Convention on the Settlement of Investment Disputes established under the auspices of the International Bank for Reconstruction and Development (IBRD).

Facilities for international conciliation or arbitration are established by the Convention through the International Centre for Settlement of Investment Disputes which is located at the principal office of the IBRD in Washington.

2.4 Regional Centre for Arbitration

The Kuala Lumpur Regional Centre for Arbitration was established in 1978 under the auspices of the Asian-African Legal Consultative Committee (AALCC) - an inter-governmental organisation in cooperation with and with the assistance of the Government of Malaysia.

The Centre serves the Asian and Pacific region. It is a non-profit organisation and has been established with the objective of providing a system for the settlement of disputes for the benefit of parties engaged in trade and commerce and investments with and within the region.

IV. MALAYSIAN INDUSTRIAL DEVELOPMENT AUTHORITY (MIDA)

The Malaysian Industrial Development Authority (MIDA) is the first point of contact for investors who intend to set up projects in the manufacturing and related support services sector in Malaysia. MIDA has established a global network of overseas offices covering North America, Europe and the Asia-Pacific and a local network of branch offices in the various states to assist investors in the initial stages to the implementation and operation of their projects.

Since 1 October 1988, the Malaysian Industrial Development Authority (MIDA) has been designated as the Coordinating Centre on Investment. Investors need only to approach MIDA to obtain most of the approvals required at the Federal level. This measure is aimed at further streamlining the administrative procedures in respect of investment at the Federal level.

The major functions of MIDA are:

- (a) Promote foreign and local investments in the manufacturing and related services sector;
- (b) Undertake planning for industrial development in Malaysia;
- (c) Recommend to the Minister of International Trade & Industry policies and strategies on industrial promotion and development;
- (d) Evaluate various types of applications relating to the set up and implementation of industrial and related projects;
- (e) Assist companies in the implementation and operation of their projects and other assistance through direct consultation and cooperation with the relevant authorities at both the federal and state levels;
- (f) Facilitate the exchange of information and coordination among institutions engaged in or connected with industrial development.

Applications evaluated cover the following:

- (a) Manufacturing licences;

- (b) Tax incentives for manufacturing activities, agriculture projects, hotel and tourism projects, R&D, technical or vocational training institutions and software development;
- (c) Expatriate posts;
- (d) Import duty exemption on raw materials and components;
- (e) Import duty and sales tax exemption on machinery and equipment;
- (f) Tariff protection;
- (g) Approvals of technology transfer agreements; and
- (h) Asean Industrial Cooperation (AICO) Scheme

To further enhance MIDA's role in assisting investors, senior representatives from various key Ministries, departments and relevant corporations are emplaced within the MIDA Headquarters in Kuala Lumpur to assist and advise investors and coordinate applications for approvals and other matters under the purview of these bodies. The 3 representatives are from:

- (a) Ministry of Finance;
- (b) Ministry of Human Resources;
- (c) Immigration Department;
- (d) Royal Customs and Excise Department;
- (e) Department of Occupational Safety and Health;
- (f) Department of Environment;
- (g) Tenaga Nasional Berhad; and
- (h) Telekom Malaysia Berhad.

On the 3rd May 1999, an Industry Support Division was set up in MIDA with the following functions:

- (a) Assist companies in the implementation and operation of new projects;
- (b) Extend support to existing companies in their expansion, diversification and reinvestment projects;

- (c) Undertake periodic reviews of issues and formulate appropriate measures for the smooth implementation and operation of industrial projects;

Investment Centre at State Level

At the state level, investment centres have also been formed to provide efficient services to investors. Presently, nine states have set up such centres. These are Johor, Kelantan, Melaka, Negeri Sembilan, Pahang, Perak, Sabah, Selangor and Terengganu. The State Government of Sarawak has also agreed in principle to set up a similar centre. The three other states of Kedah, Perlis and Pulau Pinang are still operating under this existing systems where applications are submitted directly to the respective agencies for approval. If complications or delays should arise in the granting of certain approvals, the State Economic Development Corporations (SEDCs) of Kedah and Perlis and the Penang Development Corporation (PDC) will then convene a meeting among the agencies concerned to expedite the granting of such approvals.

The investment centres at the state level are either at the SEDCs as in Johor, Kelantan, Melaka, Pahang and Perak or at the State Economic Planning Units (SEPUs) as in the case of Negeri Sembilan, Selangor and Terengganu. In Sabah, the centre is at the Department of Industrial Research and Development (DIRD). In Sarawak, the State Government has agreed that the centre be based at the Ministry of Industrial Development (MID).

To assist these centres to function effectively, Special Committees have been established. The role of these Committees is to coordinate and decide all matters concerning the issue of licences, permits and approvals and problems faced by investors at the state level. All applications and complaints received are channelled by the centres (which also serve as the secretariats to the Special Committees) to the relevant agencies for consideration. The centres at state level do undertake different functions but they are generally very similar and their functions relate more to expediting the necessary approvals for the implementation of their projects.

The essential Terms of Reference of the centres at the state level are as follows:

- (a) to establish an investment information centre for collecting, updating and providing relevant information or data to investors;
- (b) to receive, process and convey decisions on applications for licences, permits and approvals required by investors at the state level for the implementation and operation of their projects;
- (c) to monitor the progress of projects with the view to assisting investors in the implementation of their projects; and
- (d) to advise the State Governments from time to time on all matters pertaining to the development of the industrial sector in the state.

With the establishment of the investment centres at the state level, the administrative procedures involved in the granting of approvals, permits and licences required for the implementation and operation of the projects at the respective state level have been streamlined. It would not only make it easier for the investors as they would have to deal only with the centres in respect of most, if not all, of the problems they would encounter at the state level, but the time taken to secure the necessary approvals would also be reduced. This would save the investors valuable time, effort and resources in their dealings with the State Governments and would consequently enhance the overall investment climate not only of the states but also of the nation as a whole.

Pertaining to the relationship between Federal and State Governments, the joint Industrial Coordination Committee involving Federal and State has been established in every state with the following function:

- (i) Plan industrial development at the state level to ensure that it is in accordance with national planning. State industrial development plans are used as inputs to national industrial to national industrial development plans to ensure effectiveness.

- (ii) Identify investment promotion strategies to ensure efficient distribution of industries. For this the committee will emphasize:

- (a) identifying new industrial zones evaluating infrastructure elements such as roads, water supply, electricity, transportation, communications, storage and disposal of industrial wastes;
- (b) evaluating the feasibility of setting up specific industrial zones, specifically for SMI's
- (c) identifying and solving problems faced by companies operating in industrial zones; and
- (d) identifying industries which need to be emphasized in the different states.

- (iii) Plan and monitor linkages in industrial sub-sectors in order to ensure the presence of critical supporting industries at the state level. Industrial development is to be more integrated. Synergy in industrial development to be achieved by the different states.
- (iv) Promote Skills Development Centres at the state level to ensure a sufficient supply of skilled workers for industry.
- (v) Identify weaknesses in procedures hindering project implementation and recommend remedial action.
- (vi) Plan export promotions so that industrial producers explore international markets.
- (vii) Provide feedback and references to help the private sector solve their problems.

V. TRANSFER OF TECHNOLOGY

All manufacturing projects licensed under the industrial Coordination Act 1975 must obtain the prior written approval of the Ministry of International Trade and Industry (MITI) before entering into any technology transfer agreement involving foreign partners.

This is done to ensure that the agreement will not impose unfair and unjustifiable restrictions or handicaps on the local party, the agreement will not be prejudicial to national interest, and the payment of fees (if applicable) will be commensurate with the level of technology to be transferred.

Types of Agreements

Technology transfer agreements cover licence rights over specific processes, formulae or manufacturing technology (may be patented or unpatented), other knowledge and expertise necessary for the setting up of a plant, and provision of various technical assistance and supporting services.

Under these arrangements, a specific agreement entered into could be in the form of:

- (i) Joint-Venture Agreement. An agreement to set up a joint-venture company between two or more parties involving locals and foreigners.
- (ii) Technical Assistance and Know-How Agreement. An agreement between two or more parties where one party will provide the technical assistance and know-how for the manufacture of certain products for a certain amount of fee or royalty.
- (iii) Licence Agreement. An agreement between two or more parties where the licensor grants a licence/right to the licensee to use its patents, trademarks and other industrial/intellectual properties for the manufacture of certain products for a certain amount of fee or royalty.
- (iv) Patent and Trademark Agreement. An agreement between two or more parties where one party gives the right to the other to use its patents and trademarks for the manufacture of certain products for a certain amount of fee.
- (v) Turnkey Contract. A contract between two or more parties where the contract is awarded to one of the parties to perform all stages from the initial to the final stage, inclusive of consultancy, managerial,

technical and other services, until the contractual project is ready for immediate commercial production or final use.

- (vi) Management Agreement. An agreement between two or more parties where one party will provide management services to the other for a management fee.

Guidelines on Transfer of Technology

Agreements on transfer of technology must define in detail the following:

- (i) technological content and principal features of technology or process;
- (ii) anticipated production;
- (iii) quality and specification of products; and
- (iv) particulars of technical assistance, services and manner in which they are to be provided.

The transfer of technology must be effected through the following:

1. Access to Improvements

The technology to be supplied should incorporate:

- (i) the latest development know-how of the supplier; and
- (ii) access to innovations or breakthrough in technology, including new patents applied for or registered.

2. Remuneration for Technology

Payment for technology can be in the form of a 'fixed lump sum fee' or a 'running royalty' or a combination of lump sum fee and running royalty for a specified period. Lump sum payments are usually allowed in cases where the know-how can be fully and completely transferred and absorbed within a specified period. The method of payment that is preferable is the running royalty based on net sales. Initial lump sum payments in addition to royalties are not encouraged by MITI. Where such payments are requested, it

should be only for the recovery of actual expenses incurred by the Licensor for preliminary services provided to the Licensee.

3. Method of Payment

- (a) Royalty is imputed in relation to the level of technology and principal elements of transfer. Depending upon the merits of each case, a rate of 1% to 5% of net sales can be considered. Net sales are defined as gross sales less sales discounts or returns, transport costs (including freight), insurance, duties, taxes and other charges including where applicable, costs of raw materials, parts and components imported from the foreign licensor concerned or its subsidiaries or affiliated companies.
- (b) The Government has liberalised the present policy for regulating technology transfer agreements by allowing automatic approval of the following:
 - (i) Technology transfer agreements signed between 100% foreign-owned companies in Malaysia and any foreign party or foreign holding company.
 - (ii) All technical assistance, licence and know-how agreements signed between Malaysian-owned/ Malaysian joint-venture companies and any foreign party where the royalty payment is as follows:
 - (a) running royalty not exceeding 3% of net sales; or
 - (b) lump sum payment not exceeding RM500,000; or
 - (c) lump sum payment and running royalty in total not exceeding 3% of net sales.
 - (iii) Trade mark and patent agreements signed between Malaysian-owned/ Malaysian joint-venture companies and any foreign party involving royalty payments not exceeding 1% of net sales for each category.

Practice of itemisation of service under separate agreements is discouraged.

- (c) Capitalisation of know-how fees or royalty is not encouraged.

4. Duration and Renewal

- (a) Duration of the agreement should be adequate for full absorption of technology. The life of any patent relating to the technology is also taken into consideration.
- (b) An initial period of five years is normally approved and any renewal is subject to the prior approval of MITI.

5. Training

A provision for adequate training of the local company's personnel in the technology supplier's plant facilities as well as in-house training in the local company's plant should be incorporated and clearly specified. In the case of the former, the number of personnel to be trained, the areas of training and its duration, together with arrangements and the facilities to be made available for the training should also be defined. The costs of training should be borne by the technology supplier but all expenses related to salaries, wages, living and travelling allowances should be borne by the local company.

6. Patents and Trade Marks

Patents and trade marks may come as one of the components of the whole technology transfer package. In the case of patents, it is of utmost importance that those patents involved in any process know-how be explicitly defined in the agreements and the local company is granted user rights over all such patents. Where the life of the patents extends beyond the duration of the agreement concerned, an arrangement should be made for the continued use of the patents after the expiry of the agreement.

7. Confidentiality/Secrecy

Confidentiality of information should be confined to the duration of the agreement only.

8. Guarantee/Warranty

The agreement should define a guarantee with respect to the production capacity, product quality and specifications and other features of the manufacturing process.

9. Infringement of Third Party's Right

The technology supplier should undertake to indemnify the local company against any claims in the event that legal proceedings are taken by a third party against the local company for infringement upon any industrial property rights arising out of the use by the local company of any of the technical assistance furnished by the technology supplier.

10. Termination Clause

Either party should have the right to terminate the agreement.

11. Taxes

A withholding tax of 10% is levied on payments made to foreign suppliers of technology and this tax has to be borne by the foreign recipient. Exemption under the Double Taxation Agreement, where applicable, has to be made to the Ministry of Finance separately.

12. Sales Territory

The local company should be free to sell its produce (manufactured with the licensed technology) in the whole of Malaysia and all other countries except where the foreign technology supplier is manufacturing directly or where he has given exclusive rights to others or where he is legally not empowered to allow sales based on his technology.

13. Governing Laws and Arbitration

The governing laws for any technology transfer arrangement should be Malaysian laws and

arbitration proceedings must be conducted in Malaysia in accordance with either the Malaysian Arbitration Act, 1952 (Revised 1972) or the United Nations Commission on International Trade Law (UNCITRAL) Rules and conducted at the Asian-African Legal Consultative Committee (AALCC) Regional Centre for Arbitration, Kuala Lumpur.

The requirement does not apply to agreements signed between 100% foreign-owned companies in Malaysia and any foreign party or foreign holding company.

VI. INTELLECTUAL PROPERTY PROTECTION

Intellectual property system in Malaysia provides protection for patents, trademarks, industrial designs, copyright, **layout designs of integrated circuit and geographical indications**. Malaysia provides adequate protection in the field of intellectual property for both local and foreign investors. Malaysia is a member of the World Intellectual Property Organization and signatories to two conventions administered by the world body, namely, Paris Convention (for the protection of industrial property-patents, trademarks and industrial designs) and the Berne Convention (for the protection of Copyright). Malaysia is also a signatory to the TRIPs Agreement (Agreement on Trade Related Aspects of Intellectual Property Rights), an agreement under the auspices of the World Trade Organization.

1. Patents Act 1983

Patents protection is governed by the Patents Act 1983. An Application for a patent can be filed in Malaysia and upon registration, protection is provided for its exploitation in the country. An invention is patentable if it is new involves an inventive step and is industrially applicable. Besides patent, a utility innovation certificate is also granted for an innovation or a 'minor' invention which does not require to satisfy the test of inventiveness as of patent.

To comply with TRIPS Agreement, the period for patent protection was amended to 20 years from the date of filing of an application and subject to yearly renewal from the date of grant. A Utility Innovation is protected for 10 years from the date of filing of an application, and may be extended for another 5 years plus 5 years, subject to use. The proprietor of the patent has the right to exploit the patented invention, to assign or to license the use of a patent.

2. Trade Marks Act 1976

Trademarks protection is governed by the Trade Marks Act 1976 which provides effective and adequate protection for registered trademarks in Malaysia. **The Act is applicable to goods as well as services. To comply with TRIPS Agreement, the Act was amended in 2000 to give protection for well-known marks and to make provision for border measures.**

The period of protection, is 10 years which is renewable for a period of every 10 years thereafter.

The proprietor of the trademark has the right to assign as well as to licence the use of a trademark.

The protection of a trademark is not limited in time, provided its registration is periodically renewed.

3. Copyright Act 1987

Copyright protection in Malaysia is governed by the Copyright Act 1987 which came into force on 1 December 1987. The Act provides for the protection of literary works, artistic works, musical works, films, sound recordings, broadcasts and published editions. Computer software and compilation of data is protected as literary works. Copyright generally subsists during the life of the author and 50 years after his death. Duration of protection of films, sound recordings, broadcasts and published editions is 50 years.

The Act also provides for civil as well as criminal sanctions. A unique feature of the Act is the

inclusion of provisions for enforcement which provides the power to enter premises suspected of having infringing copies and contrivances and the appointment of a special team of officers to enforce the Act. The Act accords similar protection to local and foreign works.

To comply with TRIPS Agreement the Act was amended in 2000 to provide protection for performers.

4. Industrial Designs Act 1996

The Industrial Designs Act 1996 which was enforced on 1 September 1999, replaced the United Kingdom Design (Protection) Act 1949 of West Malaysia, the United Kingdom Designs (Protection) Ordinance Chapter 152 of Sabah and the Designs (United Kingdom) Ordinance, Chapter 59 of Sarawak, for the registration of industrial designs in Malaysia.

The industrial designs is granted for 5 years upon registration from the date of filing, and is renewable for further two consecutive terms of five years each. The owner of a registered design has the right to institute legal proceedings against any person who has infringed or is infringing any of the rights conferred by the industrial design's registration.

5. Layout-Designs of Integrated Circuits Act 2000

The Layout-Designs of Integrated Circuits Act 2000 came into force on 15 August 2000. The Act provides protection for layout-designs of integrated circuits (without any registration) for ten years from the date of its commercial exploitation in Malaysia or elsewhere.

6. Geographical Indications Act 2000

The Geographical Indications Act 2000 came into force on 15 August 2001. The Act provides protection, upon registration, to goods following the name of the place where the goods are produced. Protections are applicable to goods like wine, agricultural products, handicrafts and

others. Geographical indications which are contrary to public order or morality shall not be protected under the Act.

VII. LABUAN LOFSA

To further enhance the role of Malaysia as a financial centre, the Federal Territory of Labuan was launched as an International Offshore Financial Centre (IOFC) on 1 October 1990. Labuan as an IOFC will complement the onshore financial system in Kuala Lumpur. The business and activities promoted in Labuan IOFC are:

- (i) Offshore banking including investment banking;
- (ii) Offshore insurance and offshore insurance-related businesses;
- (iii) Trusts business;
- (iv) Investment holdings;
- (v) Mutual funds, units trust and fund management;
- (vi) Leasing;
- (vii) Venture capital;
- (viii) Company management;
- (ix) Money broking;
- (x) Money market, Corporate Treasury; and
- (xi) Islamic financing.

The Administration of Labuan IOFC

The businesses and activities of Labuan IOFC are administered by the Labuan Offshore Financial Services Authority (LOFSA) – a Single Regulatory Agency which was established on 15 February 1996. The purpose of LOFSA is to act as a one-stop agency to streamline and rationalise the Government administrative machinery in supervising the activities and operations of the

offshore financial services industry in Labuan, and be responsible for setting national objectives, policies and priorities for the orderly development and administration of the Labuan IOFC. However, matters relating to taxation continue to be administered by the Inland Revenue Board.

Legislation

The legislation governing the conduct of offshore businesses and investment activities in Labuan IOFC is as follows:

- (a) Offshore Companies Act, 1990;
- (b) Labuan Trust Companies Act, 1990;
- (c) Offshore Banking Act, 1990;
- (d) Offshore Insurance Act, 1990;
- (e) Labuan Offshore Business Activity Tax Act, 1990;
- (f) Labuan Offshore Financial Services Authority Act, 1996;
- (g) Labuan Offshore Trust Act, 1996;
- (h) Labuan Offshore Limited Partnership Act, 1997; and
- (i) Labuan Offshore Securities Industry Act, 1998.

Investment/Mutual Fund Business

The investment/mutual fund business is a new activity which has been promoted in Labuan and is regulated under the Labuan Offshore Securities Industry Act, 1998 (LOSIA). The LOSIA provides the necessary legal framework for the creation and management of offshore investment funds, including Islamic funds as well as the provision of fund administration services. The Act also allows for the setting-up of the Labuan International Financial Exchange (LFX) which can be used for the listing of mutual funds and other permitted offshore instruments. As

investment opportunities in the South East Asian region are plentiful, Labuan offers an attractive domicile to foreign funds seeking to undertake investments in the region.

The main features of the LOSIA are described below:

- (i) Two types of funds can be established under LOSIA, namely, a private and a public fund. A private fund is defined as a fund which has either not more than 100 subscribers whose each first time investment is not less than RM100,000 or any number of subscribers whose each first time investment is not less than RM500,000. On the other hand, a public fund is a fund in which its shares are offered for subscription to the general public.
- (ii) While both type of funds need to be registered with LOFSA in accordance with the procedures provided under the Act, private funds are accorded more flexibility. Minimal requirements are imposed for establishing private funds in Labuan. For example, private funds need not apply to LOFSA for approval of their prospectus, fund manager and fund administrator.
- (iii) LOSIA only allows a person who is licensed or registered with LOFSA to manage or administer a fund duly registered under the Act. However, in certain circumstances, LOFSA may allow a fund manager outside Labuan and licensed in a recognized country to manage or administer any fund established in Labuan.
- (iv) The offshore banks and Labuan trust companies are allowed to be the custodian of any fund launched in Labuan. LOSIA also provides that only a Labuan trust company may be appointed as the trustee of the fund. However, LOSIA allows an authorized trustee under the laws of any recognised country or jurisdiction to carry out similar functions in Labuan.

- (v) A public fund is statutorily required to keep proper accounting records and prepare annual financial statements. These documents must be kept in Labuan and may be inspected by LOFSA, potential investors or the public.
- (vi) No public fund shall be offered to the public unless a prospectus pertaining to the fund has been published and filed with the Authority. This would ensure that potential investors have adequate information about the fund.
- (vii) The Act provides that if a person has subscribed to a fund and the fund did not comply with the provisions of LOSIA, the person may rescind the subscription contract or claim damages from the fund operator. It is an offence under LOSIA to issue any misleading prospectus.
- (viii) Any public fund which conducts any business outside Labuan is required to file with LOFSA a certificate to be issued by a competent Authority who is responsible for the regulation and supervision of the conduct of its business in that recognised country or supervision. The certificate shall state the fund is carrying on or engaged in a lawful business.
- (ix) LOSIA provides for the establishment of LFX. The purpose of the establishment of LIFE is to provide listing facilities to a fund launched in Labuan or abroad.

Tax System

An offshore company must be incorporated or registered under the Offshore Companies Act 1990 to carry on offshore business activities in or from Labuan and to enjoy the preferential tax treatment under the Labuan Offshore Business Activity Tax Act, 1990 (LOBATA). The LOBATA provides for the imposition, assessment and collection of tax on offshore business activities carried on by an offshore company in or from Labuan, effective from the year of assessment 1991. An offshore company includes an offshore trust created in Labuan.

(a) Offshore Companies

An offshore company carrying on an offshore trading activity (which includes banking, insurance, trading, petroleum operations, management activities, chartering and leasing of ships) for the basis period for a year of assessment will be taxed at a rate of 3% of its net profits or at a fixed rate of RM20,000 upon election by the company for that year of assessment payable to the Inland Revenue Board. An offshore company carrying on an offshore non-trading activity (which refers to an activity relating to the holding of investments in securities, stocks, shares, loans, deposits and immovable properties by an offshore company on its own behalf) for the basis period for a year of assessment is not subject to tax for that year of assessment. However, where an offshore company is carrying on both offshore trading and non-trading activity, it is deemed to be carrying on offshore trading activity.

(b) Companies other than Offshore Companies/Residents and Non-Resident Individuals

Companies operating in Labuan, incorporated or registered under the Companies Act 1965, are not recognised as offshore companies and do not enjoy the preferential tax treatment under the LOBATA. Such companies continue to be taxed under the Income Tax Act, 1967. Tax incentives under the LOBATA are also not applicable to companies carrying on industrial and/or manufacturing activities but instead they may apply for incentives under the Promotion of Investments Act 1986. Non-resident and resident individuals in Labuan will continue to be taxed under the Income Tax Act, 1967.

(c) Preferential Tax Treatment Accorded Under Income Tax, 1967 and Stamp Act, 1949

The preferential tax treatments are:

(i) Treatment on Dividends

Dividends received by an offshore company from a Malaysian resident

company are not subject to income tax and no refund or set-off is given in respect of tax deducted from such dividends. Dividends paid by an offshore company out of income derived from an offshore business activity or out of exempt income is not subject to income tax in the hands of the recipient. Such dividends will be paid gross without any tax deduction at source.

(ii) Treatment on Distribution By Offshore Trust

Distribution made by an offshore trust is not subject to income tax in the hands of the beneficiary.

(iii) Treatment on Royalty

Royalty paid by an offshore company to a non-resident person or another offshore company is not subject to income tax and hence is not subject to withholding tax.

(iv) Treatment on Interest

Interest paid by an offshore company to a non-resident person or another offshore company is not subject to income tax. However, where the interest accrues to a banking, finance company or insurance business carried on by a non-resident person in Malaysia, that interest will be subject to income tax as part of business income. Interest paid by an offshore company to a resident person, other than a person carrying on a banking, finance company or insurance business in Malaysia, is not subject to income tax.

(v) Treatment on Technical Or Management Fees

Technical or management fees paid by an offshore company to a non-resident or another offshore company is not subject to income tax.

(vi) Exemption from Stamp Duty

All instruments made in connection with an offshore business activity by an offshore company are not subject to stamp duty under the Stamp Act 1949.

(vii) Abatement of Tax for Professional Services

Income derived from qualifying professional services rendered to an offshore company in Labuan is exempted from tax up to an amount equivalent to 65% of the statutory income from that source. This incentive is applicable until year of assessment 2004.

(viii) Abatement of Tax for Employment

Income derived by a non-citizen individual from an employment exercisable in a managerial capacity of an offshore company in Labuan and a non-citizen trust officer in a Labuan Trust Company is exempted from tax up to an amount equivalent to 50% of the gross income from that employment until year of assessment 2004 and 2005, respectively.

VIII. PETROLEUM DEVELOPMENT ACT, 1974

The Petroleum Development Act, 1974 came into force on 1 October 1974. The purpose of the Act is to regulate the petroleum and petrochemical industries. The power to regulate all activities in the upstream petroleum sector is vested in the Petroleum Nasional Berhad or PETRONAS. The Petroleum Regulations 1974, which were amended on 14 January 1991, vested powers to the Ministry of Domestic Trade and Consumer Affairs and the Ministry of International Trade and Industry (MITI) to regulate all activities in the downstream sector of the petroleum industry.

The Ministry of Domestic Trade and Consumer Affairs has been given the powers to issue licences for the marketing and the distribution of petroleum

and petrochemical products. MITI is vested with the powers to issue licences for the processing and refining of petroleum as well as the manufacture of petrochemical products.

In addition, the Petroleum (Income Tax) Act 1967 was amended in 1976 to bring the structure in line with the production sharing contracts signed between PETRONAS and the various oil companies. Effective from the year of assessment 1998, income tax on the petroleum industry was reduced from 40% to 38% while the export duty for crude oil and condensate was reduced from 20% to 10% with effect from 1 January 1998.

IX. GAS SUPPLY ACT 1993

The Gas Supply Act, 1993 was gazetted on 4 February 1993 to safeguard the interests of consumers supplied with gas through pipelines and from storage tanks or cylinders specifically used for reticulation of gas. Gas was reticulated to commercial and industrial outlets as well as residential consumers.

The Gas Supply Act 1993 came into effect simultaneously with the gazetting of the Gas Supply Regulations 1997 on 17 July 1997. The Regulations include procedures for the issuance of a license to supply, installation of gas pipelines, inspection, tests and maintenance of gas installations as well as the certification and registration of competent persons to undertake the relevant work in such a manner as to ensure public safety. Both the Act and its Regulations are enforced by the Director General of the Electricity and Gas Supply Department.

With the gazetting of the Gas Supply Act 1993, the relevant sections in the Petroleum Development Act 1974 pertaining to the gas reticulation process have also been amended to prevent duplications between the two Acts. This is to ensure that all gas reticulation and related transmission and supply activities will be conducted in accordance with the Gas Supply Regulations 1997.

X. SECURITIES COMMISSION

The Securities Commission (SC) was established and started operations on 1 March 1993 with the coming into force of the Securities Commission Act 1993. With the coming into force of the Securities Commission Act 1993, the functions of the Capital Issues Committee (CIC) established under the Securities Industry Act 1983 and those of the Panel on Take-overs and Mergers under the Companies Act 1965 were transferred to the SC.

The SC comprises the following nine members appointed by the Minister of Finance:

- (a) SC a Chairman, who shall be an Executive Chairman;
- (b) Four members representing the Government, including the Deputy Chief Executive; and
- (c) Four other persons from the private sector.

A member of the SC shall hold office for a term not exceeding three years and is eligible for reappointment.

Functions of the Securities Commission

The functions of the SC as stipulated in the Securities Commission Act 1993, are as follows:

- (a) to advise the Minister of Finance on all matters relating to the securities and futures' industries;
- (b) to regulate all matters relating to securities and futures contracts;
- (c) to ensure that the provisions of the securities laws are complied with;
- (d) to regulate the take-overs and mergers of companies;
- (e) to regulate all matters relating to unit trust schemes;
- (f) to be responsible for supervising and monitoring the activities of any exchange, clearing house and central depository;

- (g) to take all reasonable measures to maintain the confidence of investors in the securities and futures' markets by ensuring adequate protection for such investors;
- (h) to promote and encourage proper conduct among members of the exchanges, clearing houses, central depository and all licensed persons;
- (i) to suppress illegal, dishonourable and improper practices in dealings in securities and trading in futures contracts and the provision of investment advice or other services relating to securities or futures contracts;
- (j) to consider and make recommendations for the reform of the law relating to securities and futures contracts;
- (k) to encourage and promote the development of securities and futures' markets in Malaysia including research and training in connection thereto;
- (l) to encourage and promote self-regulation by professional associations or market bodies in the securities and futures industries;
- (m) to license and supervise all licensed persons as may be provided for under any securities law; and
- (n) to promote and maintain the integrity of all licensed persons in the securities and futures' industries.

In addition, the SC is also the sole regulator of the private debt securities market and the registering authority for prospectuses in respect of all securities other than shares and debentures issued by unlisted recreational clubs.

Governing Acts and Guidelines

The SC is responsible for the administration and enforcement of the following Acts:

- (a) Securities Commission Act 1993;
- (b) Securities Industry Act. 1983;
- (c) Futures Industry Act 1993; and

- (d) Securities Industry (Central Depositories) Act 1991.

The following are some of the Guidelines, Codes and Regulations issued and administered the SC:

- (a) Policies and Guidelines on Issue/Offer of Securities;
- (b) Guidelines for Public Offerings of Securities of Infrastructure Project Companies;
- (c) Guidelines for Public Offerings of Securities of Closed-End Funds;
- (d) Guidelines for the Public Offering of Securities of Foreign-Based Companies with the Listing and Quotation on the Kuala Lumpur Stock Exchange;
- (e) Prospectus Guidelines;
- (f) Guidelines on the Offering of Private Debt Securities;
- (g) Guidelines on Contents of Prospectus for Debentures;
- (h) Securities Commission (Shelf Registration Scheme for Debentures) Regulations 2000;
- (i) Guidelines on the Minimum Contents Requirements for Trust Deeds;
- (j) Malaysian Code on Take-overs and Mergers;
- (k) Guidelines on Asset Valuations for Submission to the Securities Commission;
- (l) Guidelines on Unit Trust Funds;
- (m) Guidelines on Property Trust Funds;
- (n) Guidelines on the Establishment of Foreign Fund Management Companies;
- (o) Guidelines for Application for Fund Manager's and Fund Manager's Representative's Licence under the Securities Industry Act 1983;
- (p) Guidelines For Application For Futures Fund Managers and Futures Fund Manager's Representative's Licence Under The Futures Industry Act;

- (q) Guidelines for the issue of Call Warrants;
- (r) Guidelines on Securities Borrowing and Lending in Malaysia;
- (s) Guidelines for Application of Licence under the Futures Industry Act 1993;
- (t) Statutory Declaration by a Person Pursuant to an Application for a Licence under the Futures Industry Act 1993/ Securities Industry 1983.

Applications For Corporate Proposals

A public company is required to seek the approval of the SC, as required by the Securities Commission Act 1993, before undertaking any of the following proposals:

- (a) Make available, offer for subscription or purchase, or issue an invitation to subscribe for or purchase securities in Malaysia.
- (b) Make available, offer for subscription or purchase, or issue an invitation to subscribe for or purchase, outside Malaysia, securities of a public company or to list such securities on a securities exchange outside Malaysia;
- (c) Make a bonus issue of securities of a public company other than by way of capitalisation of unappropriated profits.
- (d) By way of issue of securities effect:
 - (i) a compromise or arrangement whether or not for the purposes of or in connection with a scheme, compromise or arrangement for the amalgamation of any two or more corporations or for reconstruction of any corporation; or
 - (ii) an employee share or employee share option scheme; or
 - (iii) an acquisition of securities or assets.
- (e) Apply for the listing of a corporation or for the quotation of securities on a stock market of a stock exchange.

- (f) Distribute assets of a public company to its members other than distribution in cash or distribution of assets to members of the public company on its winding up.
- (g) Acquire or dispose of assets (whether or not by way of issue of securities) which results in a significant change in the business direction or policy of a listed public company.

In considering the proposals stipulated above, the SC may have regard to any of the following matters:

- (a) whether or not there will be adequate disclosure of such information that investors and their professional advisers would reasonably require and reasonably expert to find in the prospectus for the purpose of making an informed assessment of:
 - (i) the assets and liabilities, financial position, profits and losses and prospects of the issuer, and in the case of a unit trust scheme or prescribed investment scheme, of the scheme;
 - (ii) the rights attaching to the securities; and
 - (iii) the merits of investing in the securities and the extent of the risk involved in doing so.
- (b) whether the enquiries (if any) of the corporation concerned, its officers, underwriters and advisers provide adequate verification of the accuracy and completeness of information disclosed;
- (c) whether the persons in respect of whom a proposal has been made, need protection through the process of approval and disclosure pursuant to Part IV of the Securities Commission Act 1993.
- (d) the type of business in which the corporation is engaged and the risks associated with it;
- (e) the record of the corporation and the character, skills and experience of its management;

- (f) the purpose for which the company is raising funds;
- (g) the suitability of permitting the proposal or permitting trading in securities on the stock market of a stock exchange or any stock market outside Malaysia;
- (h) interests of the public; or
- (i) whether the operation of the market forces, including those with respect to price, provide an adequate mechanism for dealing with risks and merits of the proposal.

Regulatory Framework for Fundraising

Major changes to the regulatory framework for fundraising were introduced with effect from 1 July 2000 when the Securities Commission (Amendment) Act 2000 (SCA) came into force. The rationale for the amendments is to create a fully rationalized and efficient regulatory regime for capital raising in Malaysia. Under the SCA, the SC is the approving and registering authority for prospectuses in respect of all securities other than shares and debentures issued by unlisted recreational clubs whilst the Registrar of Companies (ROC) retains all responsibilities relating to the lodgment of prospectuses.

The existing provisions in the Companies Act 1965 that deal with prospectuses will apply to any offer of shares or debentures by unlisted recreational clubs and in respect of “interests” which are regulated under Division 5 of Part IV of the Companies Act 1965. The ROC would also continue to regulate all public offers of shares and debentures by unlisted recreational clubs under Division 4 of Part IV of the Companies Act 1965 administered by the Registrar of Companies.

The SC is the single regulatory body for all corporate bond issuance except for bonds which are issued by unlisted recreational clubs. The SC is responsible for the regulation of trustees, trust deeds, borrowers’ and guarantors’ obligations in relation to debenture issues which are considered to be integral to the regulation of corporate bond market.

A company undertaking fundraising activities may be required to prepare and registered with the SC a document known as a prospectus. The SCA specifies when a prospectus must be registered and what its contents must include.

Division 3 Part IV of the SCA set out the provisions regulating the requirement for prospectuses in relation to any issue of, offer for subscription or purchases of or invitation to subscribe for or purchase securities. Other forms of fundraising include debt securities e.g. debentures, mortgage debentures and unsecured notes. These forms of fundraising are also governed by the prospectus requirements set out in the SCA and other specific requirements in relation to debentures set out in Division 4 of Part IV of the SCA, such as the requirement for a trustee and trust deed, the duties of a trustee, duties of a borrower and the duties of a guarantor.

Initial Public Offering of Securities with Listing and Quotation on a Stock Exchange

The general policies and principles adopted by the SC on public companies intending to undertake initial public offerings of securities with listing and quotation on the Kuala Lumpur Stock change are stipulated in the “Policies and Guidelines on Issue/Offer of Securities” (Issues Guidelines), which became effective on 1 January 1996 and replaced the previous “Guidelines for the New Issue of Securities and the Valuation of Public Limited Companies” issued by the then CIC.

The amendments made to the Issues Guidelines in April 1999 involved the revision of the requirements for listing on both the Second Board and Main Board of the KLSE and the requirements for reverse take-overs/back-door listings. The revised requirements were aimed at strengthening listing standards to provide added comfort to the investing public in their investment opportunities as well as to promote the growth and orderly development of the Malaysian capital market.

More amendments were made to the Issues Guidelines in December 1999 to further facilitate the progressive move towards disclosure-based

regulation (DBR). The revisions, which marked the commencement of Phase 2 of DBR, generally focussed on liberalisation of the requirements on pricing of securities; valuation of assets, and utilisation of proceeds. Under Phase 2 of the DBR programme, the SC would minimise its assessment in these areas as long as the broad requirements/guidelines are complied with.

In evaluating an applicant's suitability for listing, the SC will take into consideration a number of factors including adherence to quantitative and qualitative requirements as well as other requirements set out in the Issues Guidelines. Some of the more pertinent requirements that would have to be met are as follows:

1. Issued and Paid-up Capital

(a) Listing on Main Board

A public company seeking listing of and quotation for its securities on the Main Board should have an issued and paid-up capital of not less than RM 60 million, comprising ordinary shares with a par value of not less than 10 cent per share.

(b) Listing On Second Board

A public company seeking listing of and quotation for its securities on the Second Board should have a minimum issued and paid-up capital of RM40 million, comprising ordinary shares with a par value of not less than 10 cent per share.

2. Historical Profit Performance

(a) Listing on Main Board

The company should have an uninterrupted profit record of either three to five full financial years, with an aggregate after-tax profit of not less than RM30 million over the said three to five years, and at least RM8 million after-tax profit for the latest financial year.

(b) Listing on Second Board

The company should have an uninterrupted profit record of either three to five full financial years, with an aggregate after-tax profit of not less than RM12 million over the said three to five years, and at least RM4 million after-tax profit for the latest financial year.

3. Pricing

The company should have an uninterrupted profit record of either three to five full financial years, with an aggregate after-tax profit of not less than RM12 million over the said three to five years, and at least RM4 million after-tax profit for the latest financial year.

Flexibilities in Listing Criteria for Bumiputera Companies

Flexibilities in compliance with the listing requirements for applications on proforma accounts are given by The SC for Bumiputera-controlled companies that have pooled together for listing on the Kuala Lumpur Stock Exchange (KLSE).

Paragraph 10.10(1)(e) of the Issues Guidelines pertaining to the use of proforma accounts for the purpose of listing state the following:

“Where a group of companies is seeking listing on the stock exchange, at least one (1) company (which is the qualifying company) within the group, should be able to fulfil the profit track record requirements. If no one company qualifies, listing based on the strength of the group’s proforma accounts may be considered provided that all the companies within the group:

- (a) are involved in the same or complementary business activities;
- (b) have common directors; and
- (c) have common shareholders with controlling shareholding, on a collective basis’

over the profit track record period.

For the purpose of determining controlling shareholding, only legal or registered ownership will be accepted, and control is taken as more than 50% of the voting rights.”

With these flexibilities, a group of Bumiputera-controlled companies applying for listing based on the strength of the group’s proforma accounts would only have to comply with the first criterion of being involved in the same or complementary business activities and not the other two criteria of having common directors and common controlling shareholders.

However, in order to qualify for the flexibility, the Bumiputera group of companies must fulfil the following conditions:

- (a) The group must have a genuine pooled arrangement;
- (b) The company which is the single largest contributor, on an average basis for the past three full financial years, to profits within the proforma group should have been incorporated and have been in business operating the same or complementary business for at least 5 full financial years prior to making submission to the SC;
- (c) Each company to be pooled together must have been a Bumiputera-controlled company under the control of the same Bumiputera shareholders with controlling shareholding for at least 3 full financial years prior to making submission to the SC (or throughout the duration of the company if the company has been incorporated for a period of less than 3 financial years); and
- (d) The company used as the listing vehicle must, upon and subsequent to listing, be a Bumiputera-controlled company.

The purpose of the flexibilities is to provide Bumiputera companies with the opportunities to access the capital market.

Regulations Relating to Take-overs and Mergers

Persons involved in any take-over and merger exercise are required to observe the provisions relating to take-overs and mergers contained in sections 33 to 33E of the Securities Commission Act, 1993 (SCA) and the Malaysian Code on Take-overs and Mergers 1998 (Code). In administering the Code, the SC will take into account the desirability of ensuring that the acquisition of voting shares or control of companies takes place in an efficient, competitive and informed market.

Pursuant to section 33B(2) of the SCA, an acquirer who has obtained control in a company is required to make a take-over offer, other than in respect of voting shares of the company which at the date of the offer are already held by the acquirer of which the acquirer is entitled to exercise. In this regard, control, in relation to an acquisition of shares, is defined under section 33 of the SCA as the acquisition or holding of, or entitlement to exercise or control the exercise of, voting shares of more than 33% in a company.

Pursuant to section 33B(3) of the SCA, an acquirer who has obtained more than 33% of the voting shares in a company but less than 50% of voting shares in that company shall not acquire any additional voting shares in that company, except in accordance with the provisions of the Code. In this regard, section 6(1) (b) of the Code provides that an acquirer who holds more than 33% but less than 50% of the voting shares of a company and such person acquires in any period of six months more than 2% of the voting shares of the company, such person shall be subjected to the provisions in the Code relating to mandatory offers.

A person who fails to comply with the mandatory offer requirement shall be guilty of an offence and shall, upon conviction, be punished with a fine not exceeding one million ringgit or imprisonment for a term not exceeding 10 years or both pursuant to section 33B(4) of the SCA.

Additionally, where any documents or information is required to be submitted to the SC, in relation to or in connection with a take-

over offer or merger and a person submits or causes to be submitted any document or information that is false or misleading, the person shall be guilty of an offence and shall upon conviction, be punished to a fine not exceeding three million ringgit or to imprisonment not exceeding 10 years or both pursuant to section 33E(3) of the SCA.

Certain restrictions are imposed on both the acquirer as well as persons who sell their shares to an acquirer. Pursuant to section 7 of the Code, acquirers who are subject to the mandatory offer requirement are restricted from appointing any director to the board of the offeree company or exercising the voting rights attached to the voting shares which have been acquired before the acquirer sends out an offer document to the offeree shareholders. Section 10 of the Code provides that persons who intend to sell his or its voting shares to an acquirer are not allowed to resign as director or cause a director who is accustomed to act in accordance to his or its directions or instructions to resign from the board of the offeree until the first closing date of the take-over offer or the date when the take-over becomes or is declared unconditional as to acceptances, whichever is later.

Practice Notes attached to the Code provide guidance on the interpretation of certain provisions of the Code. Amongst others, it provides for instances where the mandatory offer obligation would be deemed to be incurred as well as circumstances under which a person may apply for exemption from mandatory offer provisions.

XI. MALAYSIA DERIVATIVES EXCHANGE BHD (“MDEX”)

The futures industry in Malaysia commenced with the establishment of the Kuala Lumpur Commodity Exchange (KLCE), a commodity futures exchange, which was the first futures exchange in Southeast Asia in July 1980.

On 15 December 1995, the birth of KLOFFE heralded a significant event in the development of the nation's capital market with the launch of KLOFFE's stock index futures contract. With its

introduction, Malaysia became the third Asian economy after Hong Kong and Japan to offer domestic equity derivatives products. KLOFFE as a financial futures and options exchange offers an efficient price discovery mechanism and a risk transfer capability that has become indispensable to both corporate and individual investors.

In its early days, KLOFFE has already become a member of the International Options Market Association (IOMA), the International Finance and Commodities Institute (IFCI) and a signatory to the Windsor Agreement. This is an indication of its commitment to be a part of the international derivatives industry. In recognition of its strive to achieve premier exchange status, KLOFFE was awarded “The 1996 Derivatives Exchange of the Year” by World Equity, a renowned international equity investors magazine within the first year of operations.

It was also in May 1996, the Malaysian Monetary Exchange (MME) was set up to provide fixed income derivatives, namely three-month KLIBOR futures. In December 1998, the KLCE merged with the MME and changed its name to the Commodity and Monetary Exchange of Malaysia (COMDEX Malaysia) to reflect the diversity of its products. In January 1999, a Sales and Purchase agreement was finalised between the Kuala Lumpur Stock Exchange (KLSE) and shareholders of KLOFFE Capital Sdn Bhd. KLOFFE thus became a subsidiary of the KLSE Group of Companies.

Subsequently, both KLOFFE and COMDEX Malaysia signed a Memorandum of Understanding to merge both exchanges in December 2000. All details were finalised in May 2001 and the new exchange renamed to Malaysia Derivatives Exchange Berhad (MDEX) was launched on 11 June 2001. This is in-line with the recommendation in the Securities Commission’s Capital Market Masterplan which aimed at establishing a single exchange that is able to offer a multitude of products for investors.

It is MDEX’s mission to be the catalyst in the development of the derivatives industry in Malaysia. MDEX will continually strive to provide safe and effective risk management tools to both

the commodity and financial communities. As a futures and options exchange, MDEX has established a reputation for being a market with the necessary capacity and capabilities for servicing the needs of the international trading community.

Regulatory Framework

The basis for the regulatory framework for the futures industry is provided for by the Futures Industry Act 1993 (FIA). Under the FIA, approval of the Minister of Finance is required before a futures exchange can be established and start to operate. To ensure that the public interest objective is served by the establishment of the futures exchange, the Minister is also empowered under the FIA to appoint the Executive Chairman and two other members of the Board of the exchange.

The FIA also provides for the supervision of the futures industry to be undertaken by the Securities Commission (SC), including licensing of market intermediaries such as:

- (a) Futures broker and its representatives
- (b) Futures fund manager and its representatives
- (c) Future trading adviser and its representatives

Membership of MDEX

The merged exchange has various classes of membership, namely:

(a) Trading Members

Trading Membership is available to companies incorporated under the Companies Act 1965. These companies are set-up specifically to carry out a futures broking business and must be licensed as a futures broker under the FIA. The membership depending on the class of membership, enables a company to trade in equity related, non-equity related and commodity products. The

companies are permitted to trade for itself and also on behalf of its clients. Application for admission as a Trading Member is by way of subscription of one class “A”, “B” or “C” Preference Share issued by the MDEX which has attached to it all the rights and obligations of a Trading Member.

(b) Local Members

Local Membership is offered to individuals who wish to trade for their own account. These individuals are not permitted to trade on behalf of clients. Local Members are not required to be licensed under the FIA as they are not considered to be intermediaries in the industry. However, they are required to be registered with MDEX. Local Members have access to the trading facility of MDEX for the purpose of executing their own trades of which matched trades must be cleared through any of the Clearing Members.

(c) Trading Permit Holders

Trading permits may be issued to individuals or corporations which enable them to trade on MDEX for a limited period of time. These permits are renewable upon expiration, subject to the approval of the exchange. Trading Permit Holders may not transfer their rights to another individual or corporation.

(d) Associate Members

Associate Members are corporations that have been granted the option to be a Clearing Member. These companies do not own any Preference Shares. Associate Members are required to nominate a Trading Member who will execute trades on their behalf.

(e) Members Representatives

A Trading Member requires individuals to act on its behalf. These individuals are required to be licensed as futures broker representatives (FBR) by the SC

under the FIA. They typically carry out the following functions on behalf of the Trading Members—

- (i) Execution of trades;
- (ii) Collection of margins from customers;
- (iii) Provide basic accounting records; and
- (iv) Advise customers in their trading programmes.

Products

The following 4 products are currently traded on the exchange—

- (a) Crude Palm Oil (CPO) Futures
- (b) Kuala Lumpur Stock Exchange Composite Index (KLSE CI) Futures
- (c) Kuala Lumpur Stock Exchange Composite Index (KLSE CI) Options
- (d) 3-Month Kuala Lumpur Interbank Offered Rate (KLIBOR) interest rate Futures

The Crude Palm Oil Futures contract was launched in October 1980 and remains the most successful commodity futures contract to-date. On the financial side, the first contract to be launched was the KLSE CI Futures contract in December 1995. This was followed by the 3-Month KLIBOR Futures contract in May 1996, and subsequently the KLSE CI Options contract in December 2000.

Trading Mechanism

KLSE CI Futures and Options employ the electronic system for trading known as the KLOFFE Automated Trading System (“KATS”). KATS is based on the Eurex Deutschland trading system and has been substantially enhanced to meet Malaysian market requirements.

The CPO Futures and KLIBOR Futures still employ the open-outcry system for trading. However, this will change soon when all contracts will be traded using the KATS electronic trading

system. The open-outcry system requires all floor traders to call out their bids and offers in a loud and audible manner within the respective trading pits on the trading floor. It is through the constant process of bidding and offering that a particular price is reached where both buyer and seller agree to transact. This process constitutes the 'price discovery' mechanism of futures market.

To further facilitate communication among traders in the pits, hand signals are used to complement the calling out of bids and offers. This is especially helpful during hectic trading periods where the 'noise' level can be rather high within the trading pits.

All bids to buy and offers to sell, as well as traded prices, are captured on MDEX Malaysia's price reporting system known as e-XPRESS, and the information is disseminated instantaneously to all market participants worldwide via newswires such as Reuters, Bloomberg, Bridge News, etc. Plans are underway to enhance transparency further by providing real-time information over the information super-highways of the Internet.

Malaysian Derivatives Clearing House

The Malaysian Derivatives Clearing House Bhd (MDCH) is the clearing house for exchange traded derivative contracts in Malaysia. Its primary function is to ensure that the financial obligations under the futures contracts entered into on the exchange are performed in a timely manner. It carries out this function by becoming the counterparty to these contracts, assuming the credit risk of its Clearing Members and managing that centralised risk.

MDCH was formed in December 1995 to clear stock index futures, and in May 1996 it began clearing interest rate futures. In November 1997 it merged with the clearing house for commodities futures, Malaysian Futures Clearing Corporation Bhd (MFCC). MDCH now clears:

- (a) Stock index futures and options;
- (b) Interest rate futures; and
- (c) Palm oil futures.

In protecting the financial integrity of the marketplace, MDCH adopts a financial and operational safeguard system that is comparable to the best international practices. This system is designed to provide the highest level of safety with very early detection of unsound practices on the part of any member. Protection against market defaults is imperative and remains the ultimate goal of the clearing system.

Financial performance of all contracts traded on MDEX is guaranteed, initially by the Clearing Members, and thereafter by the MDCH, once the contract has been matched and accepted for clearing. All participants of the MDEX must have their trades cleared through a Clearing Member of the MDCH to ensure themselves of a financially strong party behind their contracts as soon as they are transacted.

Once a contract has been accepted for clearing, the MDCH substitutes itself as the buyer to the seller and vice versa. MDCH will then hold each Clearing Member accountable for every position it carries regardless of whether the position is carried for the account of another member, for the account of a non-member client, or for the Clearing Member's own account. In short, the MDCH looks solely to the Clearing Member carrying and guaranteeing the account to secure all payments and performance obligations.

XII. COMMODITY AND MONETARY EXCHANGE OF MALAYSIA (COMDEX MALAYSIA)

Commodity and Monetary Exchange of Malaysia (COMDEX Malaysia) is a membership owned futures exchange which was incorporated on 14 July 1980 as The Kuala Lumpur Commodity Exchange. In 1992 The Kuala Lumpur Commodity Exchange formed a wholly-owned subsidiary Malaysia Monetary Exchange in order to offer trading in financial futures. The business operations of Malaysia Monetary Exchange was merged with that of COMDEX Malaysia on 7 December 1998.

COMDEX Malaysia operates under the jurisdiction and supervision of the Securities

Commission and is governed by the Futures Industry Act 1993 (FIA), thus offering investors the security of trading on a regulated Exchange with proven procedures and standards which conform to international standards.

COMMEX Malaysia provides and regulates the facilities and place for trading of both commodity and financial futures contracts pursuant to the business rules of the exchange. All futures contracts traded on the exchange are guaranteed by the clearing house, Malaysian Derivatives Clearing House Bhd.

Management of COMMEX Malaysia

The powers of management of the exchange are vested in the Management Board of the Exchange. As stipulated in section 5 of the FIA, the Management Board comprises of:

- (i) An Executive Chairman and two other directors appointed by the Minister of Finance; and
- (ii) Six directors elected by the members.

Membership

The membership structure of Commodity and Monetary Exchange of Malaysia has two distinct futures markets namely the commodity and financial futures markets. Members of the Exchange Company are corporations (brokers and non-brokers), categorised as General Members, Commodity Members and Financial Members. Members of the Exchange are individual Local Members, Local Lessees, Trading Permit Holders and corporate Trade Affiliates.

A broker member of COMMEX Malaysia is a corporate member holding a futures broker license issued by the Securities Commission (SC) under the Futures Industry Act (FIA) 1993, to carry on futures brokering business. Consequently, under the FIA, every director and relevant employee of a futures broker member are required to be licensed by the SC as futures broker's representatives (FBR).

Seats

The trading rights of members of the Exchange are attached to Seats, (minimum 1 seat) which are either owned or leased. As for the Members of the Exchange Company, they must at least own 2 seats, a prerequisite to their trading rights. Seats are categorised as Commodity Seats, Financial Seats and Individual Seats.

Seats may be purchased from the Exchange or from Members wishing to sell in the secondary market, subject to the approval and in accordance with the Business Rules of the Exchange.

Market Safeguards

COMMEX Malaysia has many safeguards of high standards to protect the integrity of the markets. They are as follows:

(i) The Clearing House

In protecting the financial integrity of the marketplace, COMMEX Malaysia together with its clearing house, the Malaysian Derivatives Clearing House Berhad (MDCH), adopts a financial and operational safeguard system that is comparable to the best international practices. This system is designed to provide the highest level of safety with very early detection of unsound practices on the part of any member. Protection against market defaults is imperative and remains the ultimate goal of the clearing system.

Financial performance of all contracts traded on the floor of COMMEX Malaysia is guaranteed, initially by the Clearing Members, and thereafter by the MDCH, once the contract has been matched and accepted for clearing. All participants of the Exchange must have their trades cleared through a Clearing Member of the MDCH to ensure themselves of a financially strong party behind their contracts as soon as they are transacted.

Once a contract has been accepted for clearing, the MDCH substitutes itself as the buyer to the seller and vice versa. MDCH will then hold each Clearing Member accountable for every position it carries regardless of whether the position is carried for the account of another member, for the account of a non-member client, or for the Clearing Member's own account. In short, the MDCH looks solely to the Clearing Member carrying and guaranteeing the account to secure all payments and performance obligations.

(ii) The Audit, Compliance & Surveillance (ACS) Division

The ACS division has an overall responsibility of upholding the integrity of COMMEM Malaysia's futures markets. The Division carries out a wide range of duties through its highly dedicated and competent audit staff which include daily and regular monitoring of the market and members, regular visits to members' offices for field audits and monitoring of the activities on the trading floor of the Exchange.

The duties of the ACS Division can be classified into the following major areas:

(a) Audit and Compliance

The Division is responsible for detecting violation of the Rules and the Act. It conducts routine and surprise audits on Broker Members as well as reviewing the adequacy of their internal controls.

(b) Financial Surveillance

The Division is also responsible for detection of any failure by Members to meet the minimum financial requirements of the Exchange. It conducts regular monitoring of Members' financial positions and clients' funds in segregation. Early warning levels

are established to facilitate more intensive monitoring where necessary, on the Broker Members' financial positions.

(c) Market Surveillance

The Division is responsible for detection of any adverse situations that may threaten the orderly trading or liquidation of contracts on any COMMEM Malaysia's futures markets avoiding possible market disruptions. It conducts daily monitoring of the futures prices and prices of the underlying commodity in the cash and forward markets, and the prices of substitutes of the underlying commodity of the futures contracts, as well as the open positions of large traders.

(d) Floor Surveillance

The Division is also responsible for detecting any fraudulent trading practice, abuse, and any other violation of COMMEM Malaysia's Business Rules or the objects contained in COMMEM Malaysia's Floor Procedures Manual. Their duties include ensuring all traders on the Floor maintain a high standard of conduct and professionalism, conduct regular audits on Members pertaining to Floor Rules violation, investigate complaints officially received from Members, Locals, the Clearing House, and other sources, and carry out special audits at the request of the Compliance Committee of the Exchange.

A CCTV (closed-circuit television) Surveillance System is in place to enhance the Division's performance. The system includes cameras located at strategic positions within the trading floor, microphones, television monitors,

videocassette recorders, and a scanner with pan, tilt and zoom capabilities.

Other than carrying out its responsibilities of detecting violations that may affect the integrity of the market, the division also adopts a proactive approach to assist Members in complying with the Rules. Members are strongly encouraged to consult the division on regulatory issues. Early warnings to Members in some situations where Members face some risks of violating the Rules are also provided. In addition, the Division regularly initiates amendments to the Rules in steering towards a more efficient marketplace.

In addition to the above, the Division also acts as the Secretariat to the Dispute Committee of the Exchange in settling disputes between Members and clients. The framework for enforcing the Rules is firmly established and well-tested, with the Compliance Committee of the Exchange having some limited disciplinary powers like imposing compound fines for some specific minor violations, and ordering Broker Members to trade for liquidation only for failure to meet minimum financial requirements. All major and serious violations detected are referred to the Business Conduct Committee for a full disciplinary hearing.

(iii) Registration of Brokers

A Member of the Exchange, who handles clients' futures accounts must be registered as a Futures Broker with the Securities Commission (SC) under the Futures Industry Act (FIA), 1993. The SC is an independent national regulatory agency responsible for the regulation and supervision of both commodity futures and financial futures trading in Malaysia.

A Futures Broker must also ensure that all its employees, who handle clients, are registered as Futures Broker's Representatives (FBRs) and are registered with the SC.

(iv) Reportable Position and Speculative Position Limits

Members are required to report to the Exchange when its proprietary account, or any of its client's, has a position equal to or in excess of the reportable level set by the Exchange for each contract.

Reportable position for Crude Palm Oil futures contract is set at 100 or more open contracts, either long or short, in any one delivery month. As for the Three-month KLIBOR futures contract, an open position of 100 or more Contracts in any one (1) delivery month which is owned or controlled by a Member or Client, alone or in conjunction with any other person or corporation, at the close of the Afternoon Session on any Business Day shall constitute Reportable Position.

Speculative position limits are also set for all contracts. For CPO futures, the limit is 500, net long or short, in any delivery month or in all months combined. This limit is set at 2,000 contracts, nett gross open positions for all delivery months of the contract for KLIBOR futures.

Exemptions from position limits can be obtained for bona fide hedging trades. These limits are enforced strictly to prevent price manipulation or cornering of the market, hence protecting the integrity of the Exchange.

(v) Segregation of Clients' Funds

Members are required to maintain a separate bank account for all clients' funds. Clients' funds cannot be withdrawn from the segregated account except for the purposes of payment of deposits and margins, payment of debts due to the Member from the clients, and monies

drawn on clients' authority. Members are also not permitted to use monies belonging to one client for margining or financing the trades and positions of another client or the Member itself.

COMMEX Malaysia's Products

COMMEX Malaysia, Malaysia's premier and first multi-product futures exchange, currently offers two futures contracts.

The Crude Palm Oil (CPO) Futures contract, launched in 1980, caters to the price risk management needs of the oils and fats' industry. Over the last few years, the market has gained tremendously in stature. Prices discovered on the trading floor are now recognised as the pricing benchmark for palm oil and its products worldwide.

The Three-Months Kuala Lumpur Interbank Offered Rate (3-month KLIBOR) futures contract was launched in 1996. This contract caters to the hedging and trading needs of financial institutions and large corporations with Ringgit-based assets. Major users of the contract currently include the commercial banks, large corporations and many others with risk exposure to interest rate movements.

XIII. REGULATION OF ACQUISITION OF ASSETS, MERGERS AND TAKE-OVERS

The Foreign Investment Committee (FIC) Guidelines of 1974 were formulated to establish a set rules regarding the acquisition of assets or any interest, mergers or take-overs of companies and business. The Guidelines may be viewed as a means of restructuring the pattern, ownership and control of the corporate sectors in line with the objectives of the New Economic Policy (NEP) of 1970-90. Through these Guidelines, the Government endeavours to reduce the present imbalances in the distribution of the corporate wealth and to encourage those forms of private investment that would contribute to the development of the country in consonance with the objectives of the NEP. Since efforts

made in restructuring the equity ownership in the corporate sector will continue under the National Development Policy for the period after 1990, the 1974 FIC Guidelines will continue to apply regarding the acquisition of assets or any interest, mergers and take-overs of companies and businesses in furtherance of the restructuring objectives.

Rules and Regulations Regarding Acquisition, Mergers and Take-Over

The Guidelines for the acquisition of assets, mergers or take-overs by foreign or Malaysian interests are governed among others by the following rules:

- (a) Against the existing pattern of ownership, the proposed acquisition of assets or any interest, mergers or take-overs should result directly or indirectly in a more balanced Malaysian participation in ownership and control.
- (b) The proposed acquisition of assets or any interest, mergers or take-over should lead directly or indirectly to net economic benefits in relation to such matters as the extent of Malaysian participation, particularly Bumiputera participation, ownership and management, income distribution, growth, employment, exports, quality, range of products and services, economic diversification, processing and upgrading of local raw material, training, efficiency, and research and development.
- (c) The proposed acquisition of assets or any interest, mergers or take-overs of companies and businesses should not have adverse consequences in term of national policies in such matters as defence, environmental protection or regional development.
- (d) The onus of proving that the proposed acquisition of assets or any interest, mergers or take-overs of companies and businesses is not against the objectives of the NEP is on the acquiring parties concerned.

The above guidelines will apply to the following:

- (a) any proposed acquisition by foreign interests of any substantial fixed assets in Malaysia;
- (b) any proposed acquisition of assets or any interest, mergers and take-overs of companies and businesses in Malaysia by any means, which will result in ownership or control passing to foreign interest;
- (c) any proposed acquisition of 15% or more of the voting power by any one foreign interest or associated group or by foreign interests in the aggregate of 30% or more of the voting power of a Malaysia company or business;
- (d) control of Malaysian companies or businesses through any form of joint-venture agreement, management agreement and technical assistance agreement or other agreement;
- (e) any merger and take-over of any company or business in Malaysia whether by Malaysians or foreign interests; and
- (f) any other proposed acquisition of assets or interests exceeding in value of RM5 million whether by Malaysians or foreign interests.

The guidelines, however, do not apply to specific projects approved by the Government comprising the following:

- (a) acquisition by Ministries and Government Departments;
- (b) acquisition by Minister of Finance Incorporated, Menteri Besar Incorporated and State Secretary Incorporated; and
- (c) privatisation projects approved by the Federal or State Government.

Foreign Investment Committee

For the purpose of implementing the guidelines, the FIC was established and is responsible for

major issues on foreign investment. The functions of the FIC are:

- (a) to formulate policy guidelines on foreign investments in all sectors of the economy to ensure the fulfillment of the objectives of the NEP;
- (b) to monitor the progress and help resolve problems pertaining to foreign private investments and to recommend suitable investment policies;
- (c) to supervise and advise ministries and Government agencies in all matters concerning foreign investments;
- (d) to coordinate and regulate the acquisition of any assets or interests, mergers and take-overs of companies and businesses in Malaysia; and
- (e) to monitor, assist and evaluate the form, extent and conduct of foreign investments in the country and to maintain comprehensive information to foreign investments.

The FIC comprises the following members:

- (a) Director-General of the Economic Planning Unit (as Chairman);
- (b) Secretary-General of the Ministry of Finance;
- (c) Governor of the Central Bank ;
- (d) Secretary-General of the Ministry of International Trade and Industry;
- (e) Chairman of the Securities Commission;
- (f) Chairman of the Malaysian Industrial Development Authority;
- (g) Director-General of the implementation and Coordination Unit;
- (h) Secretary-General of the ministry of Domestic Trade and Consumer Affairs;
- (i) Secretary-General of the Ministry of Entrepreneur Development; and
- (j) Registrar of Companies.

Further details on the Guidelines and procedures for submission of proposals to the FIC are obtainable from:

The Secretary
Foreign Investment Committee (FIC)
Economic Planning Unit
Prime Minister's Department
Block B5 & B6
P.M's Department Complex
62502 Putrajaya.

XIV. EXCHANGE CONTROL POLICY

With the return of stability in the financial markets, Malaysia's selective exchange control measures introduced since 1 September 1998 have been progressively relaxed. The major changes introduced in 2000/2001 were the following -

(a) 10 July 2001

Extension of Ringgit Credit Facilities to Non-residents for purchase of Immovable Property in Malaysia

Resident financial institutions are allowed to extend up to a maximum of 3 property loans in aggregate to non-residents to finance the purchase or construction of any property in Malaysia (excluding the purchase of land only), subject to the banks' internal credit assessment guideline.

(b) 2 May 2001

Abolition of Levy

The 10% levy imposed on profits from portfolio investments that are repatriated within one year of realisation has been abolished. With this measure, there is complete freedom of inflows and outflows of portfolio investments.

(c) 20 December 2000

Ringgit Credit Facilities to Non-residents

Licensed commercial banks and Bank Islam Malaysia Berhad in Malaysia are

freely allowed to extend overdraft facility in aggregate of not exceeding RM200 million on intra-day and not exceeding RM10 million on overnight basis to non-resident stockbroking companies and global custodian banks to facilitate the settlement of trades done on the Kuala Lumpur Stock Exchange (KLSE).

In addition, they can also enter into short-term currency swap arrangement to cover payment for purchase of shares on the Kuala Lumpur Stock Exchange subject to certain conditions.

(d) 1 December 2000

Domestic Credit Facilities Extended to Non-Resident Controlled Companies

Non-Resident Controlled Companies are permitted to source up to 50% of the total amount of their domestic credit facilities from foreign-owned banking institutions in Malaysia.

The exchange control policies of Malaysia are applied uniformly to transactions with all countries, except Israel, Serbia and Montenegro for which special restrictions apply. The exchange control policies, in general, are aimed at monitoring the settlement of payments and receipts as well as encouraging the use of the country's financial resources for productive purposes in Malaysia. For monitoring and compiling balance of payments statistics, residents are required to complete statistical forms, Form P and Form R, for each payment and receipt of more than RM10,00 vis-à-vis non-residents.

The following are the main exchange control rules:

I. Current Account Transactions

(a) Payments for Import of Goods and Services

Payments to non-residents are freely allowed for import of goods and services

irrespective of amount as long as they are made in foreign currency.

(b) Export Proceeds

All export proceeds are required to be repatriated back to Malaysia in accordance to the payment schedule as specified in the sales contract, which in any case should not exceed six months from the date of export.

Export proceeds must be received in foreign currency and must be sold for ringgit or retained in approved foreign currency accounts with resident commercial banks, up to an aggregate overnight limit of between USD1 million and USD10 million.

Resident exporters are required to submit a quarterly report listing all exports exceeding RM100,000 f.ob. per shipment, where payment would be received in full or in part, within 21 days after the end of the quarter being reported.

(c) Import and Export of Currency by Travellers

Resident and non-resident travellers are not required to declare in the Travellers Declaration Form (TDF) as long as they carry currency notes and/or traveller's cheques within the permissible limits. For non-residents, the declaration has been incorporated into the Embarkation Card issued by the Immigration Department.

Declaration in the TDF is no longer required under the following circumstances:-

- Resident carrying any amount of foreign currency notes, including traveller's cheques into Malaysia.
- Resident and non-resident travellers carrying ringgit notes up to RM1,000.

- Resident travellers bringing out foreign currency notes, including traveller's cheques, up to the equivalent of RM10,000.
- Non-resident travellers can bring in any amount of foreign currency notes, including traveller's cheques. They are not required to declare in the TDF as long as the amount brought in is less than the equivalent of USD2,500.

However, for residents, prior written approval from the Controller of Foreign Exchange (the Controller) should be obtained if the amount exceeds the permissible limits. In the case of non-resident travellers, they will only need to seek approval if the amount to be carried abroad exceeds the amount brought into Malaysia, provided the amount to be taken out is more than the equivalent of USD2,500.

II. Capital Account Transactions

(a) Foreign Direct Investment

Foreign direct investors are freely allowed to repatriate their investments, including capital, profits, dividends and interest.

(b) Investment Abroad by Residents

Residents, other than commercial banks and approved merchant banks, are required to seek prior approval from the Controller to remit funds in excess of RM10,000 for overseas investment purposes.

Commercial banks and approved merchant banks are freely permitted to invest abroad as long as they comply with the Banking and Financial Institutions Act, 1989 and their approved net open position limit. Remittance for investments abroad must be made in foreign currency.

(c) Foreign Currency Credit Facilities from Non-Residents

Residents are freely permitted to obtain credit facilities in foreign currency up to the equivalent of RM5 million in the aggregate from licensed banks, licensed merchant banks and non-residents. Any amount exceeding the permitted limit would require the prior approval of the Controller. Where the aggregate amount exceeds the equivalent of RM1 million, the resident must provide the Controller information on the credit facilities.

There is no restriction for repayment of credit facilities obtained as long as such credit facilities have been obtained in accordance with the relevant exchange control policies.

(d) Ringgit Credit Facilities from Non-Residents

Residents are not allowed to obtain credit facilities in ringgit from non-residents without the prior approval of the Controller.

(e) Extension of Credit Facilities to Non-Residents

Foreign Currency Credit Facilities

Commercial banks are freely allowed to extend credit facilities in foreign currency to non-residents for any purpose. However, credit facilities extended for the acquisition or development of immovable property in Malaysia would be subject to similar requirements as in ringgit credit facilities outlined below.

Ringgit Credit Facilities

Resident financial institutions are allowed to extend credit facilities in ringgit to non-residents to finance the purchase or construction of any property in Malaysia (excluding for purchase of land only), subject to their own internal

credit assessment guideline. Resident companies are allowed to extend credit facilities to their non-resident employees subject to the terms and conditions of service to finance the purchase or construction of property (excluding purchase of land only) in Malaysia. A non-resident may only obtain, at any one point in time, a maximum of three property loans in ringgit (including loans obtained from companies under the terms and conditions of service). All purchases are subject to the guideline issued by the Foreign Investment Committee (FIC).

Banking institutions are allowed to extend credit facilities in ringgit up to the aggregate of RM200,000 to a non-resident for purposes other than to finance the acquisition or development of immovable property in Malaysia and purchase of one vehicle for own use. Prior written approval of the Controller is required for the extension of credit facilities exceeding the limit.

Licensed Banks and Bank Islam Malaysia Berhad are allowed to extend overdraft facility in aggregate of not exceeding RM200 million on intra-day and not exceeding RM10 million on overnight basis to non-resident stockbroking companies and non-resident global custodian banks. The conditions are that the facility would be strictly for financing funding gaps due to unforeseen or inadvertent/technical administration errors or time zone delays in relation to settlement of trades on the Kuala Lumpur Stock Exchange (KLSE).

Resident stock-broking companies are allowed to extend margin financing to non-resident clients for the purchase of shares listed on the KLSE, provided they comply with all the relevant rules imposed by KLSE.

Ringgit Swap/Forward

Authorised dealers are allowed to enter into short-term currency swap arrangement with non-resident stockbrokers and non-resident global custodian banks to cover payment for their share purchases on the KLSE. Authorised dealers are also allowed to enter into an outright ringgit forward sale contract with non-residents for the same purpose. The permission is subject to the condition that such contracts are based on firm commitment and not on anticipated purchases, and with maturity period of up to three working days with no rollover option.

(f) Portfolio Investments

Non-residents are freely allowed to repatriate their principal sum and profits out of the country at any time. The exit levy system was abolished on 2 May 2001.

III. Ringgit Credit Facilities to Non-Resident Controlled Companies

A resident is freely allowed to extend credit facilities in ringgit to a Non-Resident Controlled Company (NRCC) operating in Malaysia up to an aggregate limit of RM10 million per corporate group and any amount of short-term trade financing where the tenure does not exceed 12 months. The NRCC is required to obtain prior approval from the Controller for domestic borrowing exceeding RM10 million in aggregate and to comply with the 3:1 gearing ratio requirement between its domestic debt and eligible capital funds.

Of the total amount of credit facilities extended to any NRCC by resident banking institutions in Malaysia, foreign-owned banking institutions may only extend credit facilities up to a maximum of 50%, with the balance from Malaysian-owned banking institutions.

IV. Issuance of Ringgit Private Debt Securities

On 24 April 2000, general permission was granted to NRCCs to raise domestic credit facility through the issuance of ringgit Private Debt Securities regardless of amount, as stated in the Exchange Control Guideline on Private Debt Securities. However, the NRCC must comply with the 50:50 rule and the 3:1 ratio. NRCCs would be exempted from the 50:50 rule if the Private Debt Securities are issued by way of a competitive bidding system. The proceeds from the Private Debt Securities must be utilised for productive purposes. The amount issued would be included as part of the NRCCs' total domestic credit facilities.

V. Foreign Currency Accounts of Residents

Resident exporters are permitted to open foreign currency accounts with resident commercial banks to retain export proceeds in foreign currency of between USD1 million and USD10 million, depending on their export receipts:

Aggregate Overnight Limit	Average Monthly Export Receipts
USD10 million	Exceeding RM20 million
USD5 million	Exceeding RM10 million and up to RM20 million
USD3 million	Between RM5 million and RM10 million
USD1 million	Less than RM5 million

Resident companies with domestic credit facilities are permitted to open foreign currency accounts to retain foreign currency receivables, other than export proceeds, up to an aggregate overnight limit of:

- USD0.5 million with commercial banks in Malaysia; and
- USD0.5 million with Licensed Offshore Banks in Labuan.

Resident companies with no domestic credit facilities are permitted to open foreign currency accounts with commercial banks in Malaysia to retain foreign currency receivables other than export proceeds with no overnight limit specified by Bank Negara Malaysia.

Resident individuals are also allowed to open foreign currency accounts solely to facilitate education and employment overseas up to an aggregate overnight limit of USD100,000 with commercial banks in Malaysia, USD100,000 with Labuan offshore banks and USD50,000 with overseas banks.

VI. Foreign Currency Accounts of Non-Residents

Commercial banks and approved merchant banks are freely allowed to open foreign currency accounts for non-residents.

There are no restrictions on the inflow and outflow of funds through the foreign currency accounts of non-residents.

VII. External Accounts of Non-Residents

Banking institutions are freely allowed to open accounts in ringgit known as External Accounts for non-residents.

Non-residents are allowed to use their ringgit funds in the External Account for the following purposes—

- To purchase foreign currency;
- To purchase ringgit assets;
- To pay for goods and services in Malaysia for own use;
- To pay for administrative and statutory expenses incurred in Malaysia;
- To pay for settlement under a non-financial guarantee (where the non-financial guarantee is called upon against the account holder)

- To extend ringgit credit facilities to staff in Malaysia in accordance to terms and conditions of employment;
- To repay ringgit credit facilities that were extended in accordance to ECM Notice, ECM 6 or the terms and conditions of employment;
- To withdraw ringgit cash of any amount; and
- To pay resident beneficiary for any purpose except for the following purposes—
 - payment for the import of goods and services;
 - extension of ringgit credit facilities to residents not in accordance to the terms and conditions of service;
 - settlement under financial guarantees; and
 - Payments on behalf of a third party.

The sources of funds in these ringgit accounts may be from—

- Sale of foreign currencies;
- Sale of own ringgit assets;
- All income derived from Malaysia including salaries, wages, commissions, fees, rental, interest, profits or dividends.
- Proceeds from credit facilities permitted under ECM Notice, ECM 6 or in accordance to the terms and conditions of service;
- Proceeds from repayment of ringgit credit facilities that were in accordance to ECM Notice, ECM 6 or in accordance to the terms and conditions of service;
- Crediting of ringgit cash of not exceeding RM10,000 per day; and
- Transfers from an External Account belonging to the same account holder.

Ringgit funds in the External Accounts are freely convertible and these funds can also be used for permissible purposes mentioned above.

There is no restriction on the operations of the External Accounts of non-residents working in Malaysia (including their spouse, children and/or parents who are currently residing in Malaysia), non-residents studying in Malaysia (including their spouse, children and/or parents who are currently residing in Malaysia), Central Banks, Embassies, Consulates, High Commissions, Supranational or International organisations recognised by the Malaysian Government.

VIII. Special Status Granted to Selected Companies

(a) Offshore Entities in the Labuan International Offshore Financial Centre

Entities established in Labuan International Offshore Financial Centre (IOFC) are declared as non-residents for exchange control purposes after they are incorporated/registered under the Offshore Companies Act 1990, and/or licensed Offshore Banking Act 1990 or Offshore Insurance Act 1990 as the case may be. Offshore entities in Labuan are freely allowed to deal in foreign currency with non-residents.

Licensed Offshore Banks in Labuan are permitted to receive payments in ringgit from residents arising from fees, commissions, dividends, or interest from deposit of funds.

Effective from 30 September 2000, Licensed Offshore Banks in Labuan are permitted to invest in assets/instruments in Malaysia for their own account provided investments are transacted directly with resident banking institutions or resident brokers. The investments must not be financed by ringgit borrowings.

All offshore entities are freely allowed to maintain ringgit accounts with resident banks to facilitate the defrayment of statutory and administrative expenses in Malaysia.

Offshore Insurance Entities in Labuan are permitted to maintain ringgit accounts with resident banks in Malaysia. They can use their ringgit accounts for purposes of defraying their statutory and administrative expenses in Malaysia, including receipt of insurance premiums and for payment of claims arising from insurance and reinsurance of domestic insurance business.

(b) Multimedia Super Corridor Companies

Companies operating in Multimedia Super Corridor (MSCs) which are incorporated as separate legal entities, are given exemption from exchange control regulations upon the companies being awarded the MSC status by the Multimedia Development Corporation. The exemption granted to the MSC company is solely for transactions undertaken on its own account. However, prior approval should be obtained to deal with Specified Persons and in Restricted Currencies of Israel and the Federal Republic of Yugoslavia (Serbia and Montenegro). In addition, the MSC company is also required to submit the necessary statistical forms/reports/statements.

(c) Approved Operational Headquarters

Approved Operational Headquarters (OHQs) are allowed to open foreign currency accounts with commercial banks in Malaysia to retain export proceeds in foreign currency up to an aggregate overnight balance equivalent to USD10 million, regardless of the amount of export receipts.

OHQs are also allowed to open foreign currency accounts with commercial banks in Malaysia, Licensed Offshore Banks in Labuan or overseas banks for crediting foreign currency receivables, other than export proceeds, with no limit on the overnight balances.

OHQs are allowed to obtain domestic credit facilities in ringgit not exceeding RM10 million, provided the ringgit funds are used in Malaysia.

OHQs are allowed to obtain any amount of foreign currency credit facilities from commercial banks and merchant banks in Malaysia, and from any non-residents, provided OHQ does not on-lend to, or raise the funds on behalf of, any resident. Such credit facilities can be extended to their related companies overseas or invested abroad if their aggregate domestic credit facilities in ringgit does not exceed RM10 million.

(d) Approved International Procurement Centres

Approved International Procurement Centres (IPCs) are allowed to retain any amount of export proceeds in foreign currency accounts maintained with resident commercial banks for the approved IPC activities only. IPCs are also allowed to enter into forward exchange contracts with resident commercial banks to hedge exchange risk based on projected volume of trade.

XV. DOUBLE TAXATION AGREEMENTS

Double taxation agreements provide for the avoidance of incidences of double taxation on international income, such as business profits, dividends, interests and royalties, derived in one country and remitted to another country. This

removes the “tax barrier” to international trade and investment. The agreements also provide for the exchange of information on relevant income and this is useful to prevent evasion of taxes on income.

Under double taxation agreements, business profits are taxed only in the country in which the enterprise is situated. Where the enterprise carries on business through a permanent establishment situated in the other contracting country, tax is levied in the other country on profits attributable to or derived by the permanent establishment in the country where it is situated.

Under most double taxation agreements, profits from shipping and air transport operations in international traffic are taxed only in the country where the management and control of the enterprise are exercised.

In most double taxation agreements which Malaysia have entered into, the contracting countries have agreed to provide credit on income tax which have been exempted by Malaysia on a reciprocal basis. In case of dividends paid by companies exempted from tax under the Promotion of Investments Act 1986, the recipients are also exempted from Malaysian income tax on such dividends. If the recipients are also taxed on that dividend income in the contracting countries, then the contracting countries will give credits as if Malaysian tax has been paid.

To date, 55 countries have double taxation agreements with Malaysia, namely:

Country	Date of Signing Agreement
1. Sweden	21.11.1970
2. Denmark	04.12.1970
3. Norway	23.12.1970
4. United Kingdom	30.03.1973
United Kingdom (New Agreement)	10.12.1996
5. Belgium	24.10.1973
Belgium (Protocol)	21.11.1995
6. Switzerland	30.12.1974

Country	Date of Signing Agreement	Country	Date of Signing Agreement
7. France	24.04.1975	37. Vietnam	07.09.1995
France (Protocol)	31.01.1991	38. United Arab Emirates	28.11.1995
8. Federal Republic of Germany)	08.04.1977	39. Kuwait	06.04.1997
9. Poland	16.09.1977	40. Egypt	14.04.1997
10. Romania	26.11.1982	41. Uzbekistan	06.10.1997
11. Italy	28.01.1984	42. Republic of Kyrgyz	19.11.2000
12. Finland	28.03.1984	43. Myanmar	09.03.1998
13. Russia	31.07.1987	44. Bahrain	14.06.1999
14. Netherlands	07.03.1988	45. New Zealand	19.03.1976
Netherlands (Protocol)	04.12.1996	New Zealand (Protocol)	14.07.1994
15. Hungary	24.05.1989	46. Australia	20.08.1980
16. Austria	20.09.1989	47. Papua New Guinea	20.05.1993
17. Albania	24.01.1994	48. Fiji	19.12.1995
18. Malta	03.10.1995	49. Canada	16.05.1976
19. Czech Republic	08.03.1996	50. Mauritius	23.08.1992
20. Ireland	28.11.1998	51. Zimbabwe	28.04.1994
21. Singapore	26.12.1968	52. Namibia	28.07.1997
Singapore (Supplementary)	06.07.1973		
22. Japan	30.01.1970	LIMITED DTA AGREEMENT (In respect of income of Transport Enterprises only)	
Japan (New Agreement)	19.02.1999		
23. Sri Lanka	16.09.1972	53. Saudi Arabia	18.07.1993
Sri Lanka (New Agreement)	16.09.1997	(air transport only)	
24. India	25.10.1976	54. U.S.A (shipping and air transport)	17.04.1989
India (New Agreement)	14.05.2001	55. Republic of Argentina	03.10.1997
25. Thailand	29.03.1982	(shipping and air transport)	
Thailand (Protocol)	10.02.1995		
26. South Korea	20.04.1982	XVI. INVESTMENT GUARANTEE AGREEMENTS	
27. Philippines	27.04.1982		
28. Pakistan	29.05.1982		
29. Bangladesh	19.04.1983		
30. China	23.11.1985		
31. Indonesia	12.09.1991		
32. Iran	11.11.1992		
33. Sudan	07.10.1993		
34. Turkey	27.09.1994		
35. Jordan	01.10.1994		
36. Mongolia	27.07.1995		

The purpose of the Investment Guarantee Agreements (IGAs) is to ensure against non-commercial risks such as expropriation and nationalisation and to allow for remittances and repatriation of capital. For a developing country such as Malaysia, it is hoped that the IGAs will help to quicken the pace of industrialisation by encouraging the inflows of foreign capital. It is generally considered that the IGAs, which prevent arbitrary action by a recipient country, will generate confidence in foreign investors.

Coverage

The IGA normally covers the following:

- (a) A guarantee that there shall be no expropriation or nationalisation except for a lawful or public purpose and under due process of law and with prompt and adequate compensation.
- (b) A permission to remit or repatriate in any freely usable currency, profits or capital on investment.

Beneficiaries

Under most IGAs, the beneficiaries would be:

- (a) nationals or citizens according to the laws of each contracting party; and
- (b) companies which are incorporated in either contracting party's country and substantially owned by, and whose management and control are vested in the nationals of each contracting party.

Arbitration

Under the IGAs, two forms of disputes may arise. First, disputes on the interpretation or the application of the agreement itself and secondly, disputes in connection with the investments in the contracting countries.

- (a) In most of the IGAs that Malaysia has signed, it is provided for that consultations through diplomatic channels shall settle disputes on the interpretation or application of the agreement with the view towards arriving at an amicable solution. Where a dispute fails to be settled in the above manner, it will be submitted to an arbitration board or an arbitration tribunal for settlement. If these measures fail to resolve the dispute, it would be referred to the International Court of Justice.

- (b) Disputes in connection with the investment between the national or company (investor) and the host country shall first be settled by making use of local administrative and judicial facilities. If the above means fail to settle the issue, it should then be submitted for reconciliation or arbitration to the International Centre for Settlement of Investment Disputes (ICSID) which is established under the auspices of the International Bank for Reconstruction and Development (IBRD) or the International Adhoc Arbitral Tribunal established under the Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL).

Status of Investment Guarantee Agreements

Malaysia has signed IGAs with the following countries:

	Country Agreement	Date of Signing
1.	United States of America	21.4.1959 (amended on 24.6.1965)
2.	Federal Republic of Germany ¹	22.12.1960 (amended on 5.11.1965)
3.	Netherlands	15.6.1971
4.	Canada	1.10.1971
5.	France	24.4.1975
6.	Switzerland	1.3.1978
7.	Sweden	3.3.1979
8.	Belgo-Luxembourg	22.11.1979
9.	United Kingdom	21.5.1981
10.	Sri Lanka	16.4.1982
11.	Romania	26.11.1982 (amended on 25.6.1996)
12.	Norway	6.11.1984
13.	Austria	12.4.1985
14.	Finland	15.4.1985

¹ Germany since 3.10.1990.

Country Agreement	Date of Signing	Country Agreement	Date of Signing
15. Organization of Islamic Conference (OIC)	30.9.1987	41. Spain	4.4.1995
16. Kuwait	21.11.1987	42. Pakistan	7.7.1995
17. Association of South-East Asian Nations (ASEAN)	15.12.1987	43. Kyrgyz Republic	20.7.1995
18. Italy	4.1.1988	44. Mongolia	27.7.1995
19. Republic of Korea	11.4.1988	45. Republic of India	3.8.1995
20. People's Republic of China	21.11.1988	46. Oriental Republic of Uruguay	9.8.1995
21. United Arab Emirates	11.10.1991	47. Republic of Peru	13.10.1995
22. Denmark	6.1.1992	48. Republic of Kazakhstan	27.5.1996
23. Socialist Republic of Vietnam	21.1.1992	49. Republic of Malawi	5.9.1996
24. Papua New Guinea	27.10.1992	50. Czech Republic	9.9.1996
25. Republic of Chile	11.11.1992	51. Republic of Guinea	7.11.1996
26. Lao People's Democratic Republic	8.12.1992	52. Republic of Ghana	11.11.1996
27. Taiwan	18.2.1993	53. Arab Republic of Egypt	14.4.1997
28. Republic of Hungary	19.2.1993	54. Republic of Botswana	31.7.1997
29. Republic of Poland	21.4.1993	55. Republic of Cuba	26.9.1997
30. Republic of Indonesia	22.1.1994	56. Republic of Uzbekistan	6.10.1997
31. Republic of Albania	24.1.1994	57. Macedonia	11.11.1997
32. Republic of Zimbabwe	28.4.1994	58. Democratic People's Republic of Korea	4.2.1998
33. Turkmenistan	30.5.1994	59. Republic of Yemen	11.2.1998
34. Republic of Namibia	12.8.1994	60. Republic of Turkey	25.2.1998
35. Kingdom of Cambodia	17.8.1994	61. Republic of Lebanon	26.2.1998
36. The Argentine Republic	6.9.1994	62. Burkina Faso	23.4.1998
37. Jordan	2.10.1994	63. Republic of Sudan	14.5.1998
38. Republic of Bangladesh	12.10.1994	64. Republic of Djibouti	3.8.1998
39. Republic of Croatia	16.12.1994	65. Republic of Ethiopia	22.10.1998
40. Bosnia Herzegovena	16.12.1994	66. Senegal	11.2.1999
		67. State of Bahrain	15.6.1999.
		68. Saudi Arabia	25.10.2000