



New Tax Landscape for Unit Trust Funds

5 May 2022

KPMG in Malaysia

Overview and Commentary



Ong Guan Heng
Executive Director
Corporate Tax

Key Message

“The Government action to repeal the tax exemption for foreign sourced income received in Malaysia by any resident person from 1 January 2022 has changed the tax landscape for unit trust funds. In addition, the introduction of new withholding tax obligations has also increased the administrative burden on the fund managers of unit trust funds.”

New Tax Landscape for Unit Trust Funds

The Finance Act 2021 has introduced several amendments to the Income Tax Act 1967 (“the Act”) which would change the tax landscape for the unit trust funds in year 2022. Fund managers will have to look at how the tax changes will impact the unit trust industry especially on operational matters and return of investment to unit holders.



Taxation of Foreign Sourced Income

Prior to 1 January 2022, a tax exemption was accorded to any person, other than a resident company carrying on the business of banking, insurance, sea or air or transport, who derived income from sources outside Malaysia and received in Malaysia. With the amendment to Paragraph 28, Schedule 6 of the Act, effective from 1 January 2022, the income tax exemption on foreign sourced income (“FSI”) received in Malaysia by a Malaysian resident person has been repealed. This effectively covers all FSI received in

Malaysia including FSI derived prior to 1 January 2022, both passively and actively derived from sources outside Malaysia. A transitional tax rate of 3% is accorded on the gross amount received in Malaysia during the period from 1 January 2022 to 30 June 2022. From 1 July 2022, the prevailing tax rate will apply to chargeable income computed in respect of the FSI remitted into Malaysia.

The withdrawal of the FSI tax exemption will impact a resident person in Malaysia including a resident unit trust fund and it is not applicable to a non-resident person.

A unit trust is regarded as a trust body under the Act. A trust body shall be regarded as resident for the basis year of a year of assessment (“YA”) if any trustee member of the trust body is resident for that basis year. A trust body shall not be regarded as resident for that basis year where:

- a. the trust was created outside Malaysia by a person or persons who were not citizens;
- b. the income of that trust body for that basis year is wholly derived from outside Malaysia;
- c. the trust is administered for the whole of that basis year outside Malaysia; and
- d. at least one-half of the number of the member trustees are not resident in Malaysia for that basis year.

Nonetheless, the Ministry of Finance (“MOF”), on 30 December 2021, announced that a FSI exemption will be given to the following categories of resident taxpayers, subject to meeting certain conditions which will be announced later, for a period of 5 years until 31 December 2026:

No	Resident Taxpayers	Type of FSI being Exempted
1	Individuals (apart from those who carry on business through a partnership)	All classes of FSI
2	Companies / Limited Liability Partnerships	Dividend income



Pending a Ministerial exemption order to give effect to the above proposed exemption, it is noted that a unit trust fund is currently not within the radar of the MOF. The unit trust industry will have to wait to see whether the government will extend the tax exemption to certain income or relax the implementation rules further to the request by the industry.

Subject to the release of the exemption order and further announcement by the MOF, unit trust funds that invest in foreign assets and derive foreign investment income will be subjected to

Malaysian income tax, upon remitting the taxable FSI into Malaysia. Depending on the domestic law or the Double Taxation Agreement (“DTA”) with the foreign jurisdiction (if any), a full relief on the Malaysian tax suffered may or may not be given. In turn, any tax suffered will be passed on to the unit holders when the net income of the unit trust fund is distributed to the unit holders. This will essentially reduce the income distributed to the unit holders.

Nevertheless, Paragraph 20 of Schedule 6 of the Act provides exemption on income of any approved scheme. In this respect, the repeal of FSI tax exemption should have no impact to those unit trusts that are approved schemes, which amongst others, include private retirement schemes approved by the Securities Commission in accordance with the Capital Markets and Services Act 2007.

Issues to consider and take note

Similar to companies, unit trust funds are required to furnish an estimated tax payable (“ETP”) for each YA, with two opportunities for making revision, i.e. in the 6th and 9th month of the basis period / financial year. Underestimation penalties would be imposed if the difference between the tax payable under the income tax assessment and the revised ETP (if none, the initial ETP) for a YA exceeds 30% of the tax payable under the income tax assessment of the YA. As such, the timing and quantum of the remittance of the taxable FSI into Malaysia will impact the submission of the ETP by the unit trust funds.

If the FSI is kept overseas and not remitted into Malaysia, it will not be taxed. Unit trust funds have to monitor the timing and amount of FSI to be remitted into Malaysia to observe the 30% threshold for the underestimation penalty.

In addition, a unit trust fund has to submit an initial ETP with an amount of not less than 85% of the revised ETP (if none, the initial ETP) of the immediately preceding YA. Where the quantum of FSI received in Malaysia fluctuates from one YA to another, it may create cash flow problems for the unit trust funds unless the Inland Revenue Board (“IRB”) will grant an approval to submit a lower ETP on appeal. High monthly tax instalment payments before the 6th month of the basis period / financial year to revise down the ETP, may trap some cash with the IRB which could only be refunded after submission of the tax return for that YA.

There is no clarity in the Act on the definition of “received in Malaysia”, which may be an area of dispute between the IRB and the taxpayers. One question that many may have raised is: Whether remittance of proceeds from the disposal of foreign investments into Malaysia, where the acquisition of the investments was previously financed by FSI or reinvestment of FSI, is taxable. It is noted that the existing Act does not contain any deemed or constructive remittance provisions. The IRB has previously clarified that income received in Malaysia refers to income remitted into Malaysia in the form cash and/or fund transfer. Some light might be shed when the IRB releases its guidelines to provide clarity on the operational issues.

Based on Section 61(1) of the Act, gains from the realisation of investment by a unit trust will not be subject to tax in Malaysia. However, such gains may be subject to tax in the country of derivation. Unit trust funds must keep proper records of the income and gains from the realisation of their foreign investments.

Further, tax deductions should be available for expenses incurred in the production of FSI. As the tax liability only arises when the said FSI is received in Malaysia, the timing of deductions for the



corresponding expenses incurred would need to be reviewed in computing the chargeable income in respect of the FSI when remitted into Malaysia.

Where the same FSI is taxed in both Malaysia and a foreign country, a tax credit in the form of bilateral relief under a DTA or unilateral relief under the domestic law (if there is no available DTA or a limited DTA without a relief Article) may be given on such income, to eliminate / minimise double taxation. Certain DTAs even allow underlying tax credit i.e. foreign tax payable by the foreign company in respect of the income out of which the dividend is paid, if the conditions are met. However, this poses practical issues in calculating the underlying tax credit, especially for multiple tier dividend paying companies. It would be important for the IRB to provide guidance on how to determine out of which year's profits dividends are deemed to be paid by the foreign company. Another uncertainty which we hope the IRB could clarify is whether the tax relief is to be calculated on a source-by-source, country-by-country, or on a consolidated basis. Nonetheless, the total tax relief should not exceed the total Malaysian tax payable on chargeable income for that YA. The bilateral or unilateral credit for a YA has to be claimed within 2 years after the end of that YA in which the FSI is received in Malaysia.



Distribution from Retail Money Market Funds (“RMMFs”) to Unit Holders



Paragraph 35A of Schedule 6 of the Act was introduced effective from YA 1999, to exempt a unit trust fund from tax on interest income derived from Malaysia and paid or credited by a licensed bank or Islamic bank. This was subsequently expanded to cover interest paid or credited by a development financial institution regulated under the Development Financial Institutions Act 2002 from YA 2015. With effect from YA 2017, a wholesale money market fund is restricted from enjoying the said exemption, unless it complies with the criteria as set out in the

relevant guidelines of the Securities Commission Malaysia. The exemption is completely withdrawn for wholesale money market funds from 1 January 2019, even though the criteria are complied with.

The distribution of the above exempt interest income by unit trust funds is generally tax exempted in the hands of all unit holders, pursuant to Section 61(1A) of the Act. However, amendment has been made in the Finance Act 2021 that, effective 1 January 2022, the distribution of said income by a RMMF to non-individual unit holders will be subject to tax. A new withholding tax (“WHT”) mechanism under Section 109DA of the Act has also been introduced on the income distributed as follows:

Type of Non-individual Unit Holders	Resident	Non-resident
WHT rate	24%	
WHT mechanism	Income distribution carries a tax credit, which can be utilised to set off against the tax payable by the unit holders.	WHT deducted will be regarded as a final tax.

RMMFs have to deduct and remit the WHT within one month of the distribution of the interest income to non-individual unit holders. Penalties will be imposed if the WHT is not remitted to the IRB within the stipulated deadline.

The WHT is applicable on distributions made to non-individual unit holders from 1 January 2022, even if the distribution is made out of income earned by RMMFs before 1 January 2022. The IRB has clarified that the WHT also applies to distribution made to another unit trust fund and a trustee or nominee, regardless whether such income belongs to a beneficiary who is an individual. A tax credit may be claimed by the beneficiary recipient of the income who is a resident individual.

With the amendment to Section 61(1A) of the Act, the disparity in the tax treatment between corporate investors that invest directly in deposits with licensed financial institutions and indirectly via RMMFs has been removed. This amendment may result in non-resident investors placing their deposits directly

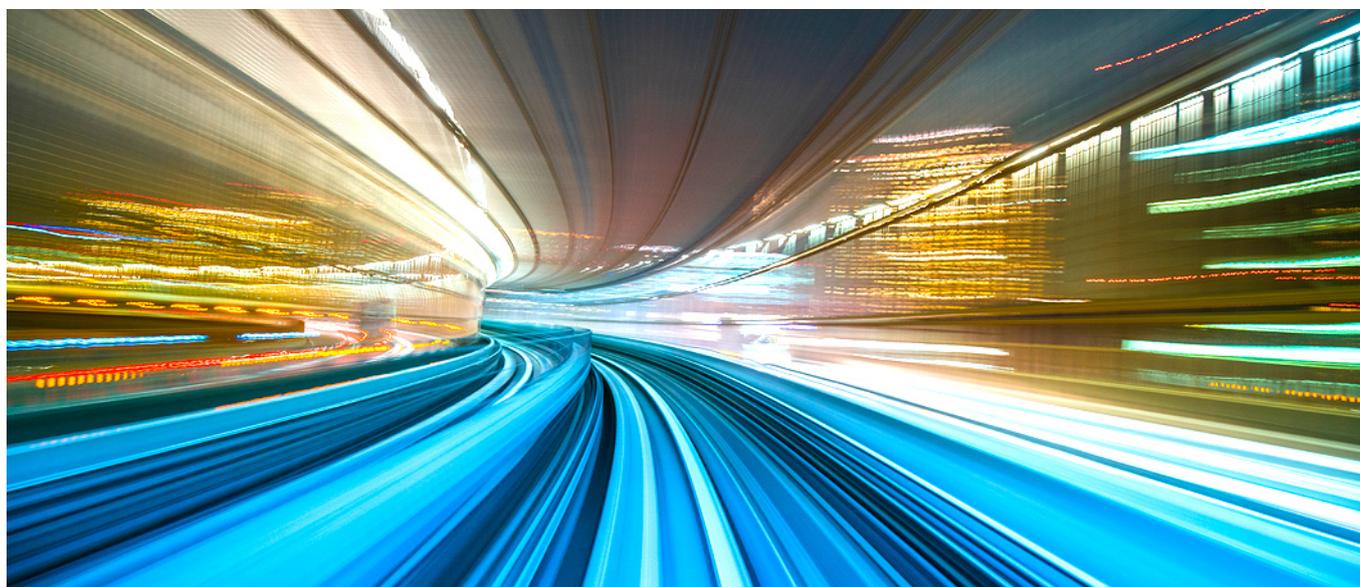
with Malaysian licensed banks instead of RMMFs where the interest income derived therefrom (other than interest income accruing to a place of business in Malaysia) is tax exempt in Malaysia.

The IRB has released two types of WHT remittance form under Section 109DA, which are categorised into distribution made to residents [Form CP37E(R)] and non-residents [Form CP37E(NR)] respectively. This may create administrative burden to RMMFs in collating information on the residence status of unit holders. The RMMFs are not required to provide a breakdown of the distribution to each individual unit holders upon submission of the WHT remittance form. However, the RMMFs must ensure that the relevant information and supporting documentation, such as the name, address and identification number of the unit holders, are kept for 7 years from the date the WHT is remitted to the IRB.

Other WHT obligation introduced

The Finance Act 2021 also introduced a new WHT provision under Section 107D of the Act on payments made by a company to its authorized resident individual agents, dealers or distributors, if certain thresholds are met. This is effective from 1 January 2022 and will mainly impact fund managers who pay commission to authorized resident individual agents for drawing investors to invest in the unit trust funds.

Year 2022 – The Way Forward



In view of the above changes, affected unit trust funds will need to consider the following operational issues, to navigate through the new tax landscape:

1. Review the tax impact on remittance of any taxable FSI from outside Malaysia into Malaysia, which is particularly important for revising the estimated tax payable for a YA to avoid any underestimation penalty.

2. Re-evaluate the impact on the net return on investment on foreign assets. Relook into prospectuses and information memorandums to reflect the latest legislation position.
3. Consider the need to modify / update accounting systems and / or keep records to keep track of the following:

Foreign investments by any unit trust funds

- differentiate the funds repatriated back to Malaysia from 1 January 2022 into gains from realisation of investment and investment income including those gains and income derived before 1 January 2022;
- the source countries where the investment income was derived from for the purpose of claiming bilateral or unilateral relief; and
- keep track of the net tax suffered on the foreign investment income received and obtain evidence of the foreign tax suffered to claim the bilateral or unilateral relief.

WHT on distribution of exempt interest income under Paragraph 35A of Schedule 6 of the Act by RMMFs

- segregate the Malaysian income into that exempted under Paragraph 35A of Schedule 6 of the Act or otherwise;
 - keep records of tax information of the new and existing unit holders such as the residency status, whether they are individuals or non-individuals, to comply with the WHT provision under Section 109DA; and
 - keep track of the date of distribution of the said income to ensure timely remittance of the relevant WHT to the IRB.
4. Consider the deferred tax accounting implications.
 5. Conduct a briefing / training for the relevant department or personnel on the requirements of WHT remittance and its deadline.
 6. Get ready all the supporting documentation to substantiate the nature of the foreign funds, i.e. gains from realisation of investment or investment income, the relevant foreign tax suffered, and tax relief claimed. However, unit trusts may have difficulty in retrieving such documentation, especially if the funds have been maintained outside Malaysia for a long period of time.

Authors



Ong Guan Heng
Executive Director
Corporate Tax
ganhengong@kpmg.com.my



Wan Yan Yoong
Executive Director
Corporate Tax
yanyoongwan@kpmg.com.my



Lim Fang Ching
Director
Corporate Tax
fangchinglim@kpmg.com.my

Contact Us

Petaling Jaya Office

Soh Lian Seng

Executive Director –
Head of Tax and Head of Tax Dispute Resolution
lsoh@kpmg.com.my
+603 7721 7019

Tai Lai Kok

Executive Director – Head of Corporate Tax
ltai1@kpmg.com.my
+603 7721 7020

Bob Kee

Executive Director – Head of Transfer Pricing
bkee@kpmg.com.my
+603 7721 7029

Long Yen Ping

Executive Director –
Head of Global Mobility Services
yenpinglong@kpmg.com.my
+603 7721 7018

Ng Sue Lynn

Executive Director – Head of Indirect Tax
suelynng@kpmg.com.my
+603 7721 7271

Outstation Offices

Penang Office

Evelyn Lee

Executive Director – Penang Tax
evewflee@kpmg.com.my
+604 238 2288 (ext. 312)

Kota Kinabalu Office

Titus Tseu

Executive Director – Kota Kinabalu Tax
titustseu@kpmg.com.my
+6088 363 020 (ext. 2822)

Ipoh Office

Crystal Chuah Yoke Chin

Tax Manager – Ipoh Tax
ycchuah@kpmg.com.my
+605 253 1188 (ext. 320)

Kuching & Miri Offices

Regina Lau

Executive Director – Kuching Tax
reglau@kpmg.com.my
+6082 268 308 (ext. 2188)

Johor Bahru Office

Ng Fie Lih

Executive Director – Johor Bahru Tax
flng@kpmg.com.my
+607 266 2213 (ext. 2514)

KPMG Offices

Petaling Jaya

Level 10, KPMG Tower,
8, First Avenue, Bandar Utama,
47800 Petaling Jaya, Selangor
Tel: +603 7721 3388
Fax: +603 7721 3399
Email: info@kpmg.com.my

Penang

Level 18, Hunza Tower,
163E, Jalan Kelawei,
10250 Penang
Tel: +604 238 2288
Fax: +604 238 2222
Email: info@kpmg.com.my

Kuching

Level 2, Lee Onn Building,
Jalan Lapangan Terbang,
93250 Kuching, Sarawak
Tel: +6082 268 308
Fax: +6082 530 669
Email: info@kpmg.com.my

Miri

1st Floor, Lot 2045,
Jalan MS 1/2,
Marina Square, Marina Parkcity,
98000 Miri, Sarawak
Tel: +6085 321 912
Fax: +6085 321 962
Email: info@kpmg.com.my

Kota Kinabalu

Lot 3A.01 Level 3A,
Plaza Shell,
29, Jalan Tunku Abdul Rahman,
88000 Kota Kinabalu, Sabah
Tel: +6088 363 020
Fax: +6088 363 022
Email: info@kpmg.com.my

Johor Bahru

Level 3, CIMB Leadership Academy,
No. 3, Jalan Medini Utara 1,
Medini Iskandar,
79200 Iskandar Puteri, Johor
Tel: +607 266 2213
Fax: +607 266 2214
Email: info@kpmg.com.my

Ipoh

Level 17, Ipoh Tower,
Jalan Dato' Seri Ahmad Said,
30450 Ipoh, Perak
Tel: +605 253 1188
Fax: +605 255 8818
Email: info@kpmg.com.my

Some or all of the services described herein may not be permissible for KPMG audit clients and their affiliates or related entities.

kpmg.com.my/Tax



facebook.com/KPMGMalaysia



twitter.com/kpmg_malaysia



linkedin.com/company/kpmg-malaysia



instagram.com/kpmgmalaysia

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2022 KPMG Tax Services Sdn. Bhd., a company incorporated under Malaysian law and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organization.