

GUIDELINES FOR APPLICATION FOR INCENTIVE BY CONTRACT RESEARCH AND DEVELOPMENT COMPANIES OR RESEARCH AND DEVELOPMENT COMPANIES;

OR

APPLICATION FOR THE FULFILLMENT OF DEFINITION AS CONTRACT RESEARCH AND DEVELOPMENT COMPANIES, AND RESEARCH AND DEVELOPMENT COMPANIES UNDER THE PROMOTION OF INVESTMENTS ACT (PIA) 1986

(31.03.2021)

A. Tax Incentive

I. Tax Incentive for Contract Research and Development Company (Contract R&D Company)

A Contract R&D Company is eligible to apply for:

- Pioneer Status (PS) with income tax exemption of 100% of statutory income for five (5) years. Unabsorbed pioneer losses after the end of pioneer period are allowed to be carried forward for seven (7) consecutive year of assessments; **or**
- Investment Tax Allowance (ITA) of 100% of qualifying capital expenditure incurred within ten (10) years. The ITA can be offset against 70% of the statutory income in each year of assessment. Unutilised allowances can be carried forward until fully absorbed.

II. Tax Incentive for Research and Development Company (R&D Company)

- A R&D Company is eligible to apply for ITA of 100% of the qualifying capital expenditure incurred within ten (10) years. The ITA can be offset against 70% of the statutory income for each year of assessment. Unutilised allowances can be carried forward until fully absorbed.
- The related companies concerned will not enjoy double deduction for payments made to the R&D Company for the use of its services, unless the R&D Company opts not to avail itself of the ITA.

B. Definition

- **Contract R&D Company** means a company which provides R&D services in Malaysia only to companies other than its related companies.
- **R&D Company** means a company which provides R&D services in Malaysia to its related companies or to any other company.

- i) **R&D** means any **systematic, investigative and experimental study that involves novelty or technical risk carried out in the field of science or technology with the object of acquiring new knowledge or using the results of the study for the production or improvement of materials, devices, products, produce, or processes.**

- ii) However, the R&D activities **does not include:**
 - a) quality control or routine testing of materials, devices or products;
 - b) research in the social sciences or the humanities;
 - c) routine data collection;
 - d) efficiency surveys or management studies;
 - e) market research or sales promotion;
 - f) routine modifications or changes to materials, devices, products, processes or production methods; or
 - g) cosmetic modifications or stylistic changes to materials, devices, products, processes or production methods.

- iii) **Related company** has the same meaning assigned to it in Section 2 of the Promotion of Investments Act, 1986.

C. Eligibility Criteria

- i. The R&D activities undertaken must comply with the definition of R&D under the Promotion of Investments Act, 1986;
- ii. The R&D activities undertaken must be in accordance with the needs of the country and bring benefits to the Malaysian economy;
- iii. At least 70% of the income of the company should be derived from its R&D services activities. **Only R&D services income is to be exempted and income generated from Intellectual Property (IP)¹ if any, is excluded.**
- iv. **For manufacturing-based research and development**, the company must have **adequate² number of full-time employees working in Malaysia** with degree or diploma in technical fields with relevant experience. Those employees must perform research and technical functions and comprise of **at least 50%** of the company's total workforce.

¹ *IP income refers to any income derived from the ownership or licensing of rights to use IP assets (such as royalties, capital gains and other income from the sale of an IP asset) and from embedded IP income (from the sale of products and the use of processes directly related to the IP asset).*

² *Proposals submitted by companies will be evaluated in detail by MIDA and will be deliberated in the National Committee on Investments (NCI) for decision.*

- v. For **agricultural-based research and development**, the company must have **adequate² number of full-time employees working in Malaysia** with degree or diploma in technical fields with relevant experience. Those employees must perform research and technical; functions and comprise of **at least 5%** of the company's total workforce.
- vi. The company must incur **adequate² amount of operating expenditure annually to support the company in conducting its R&D services activities/business operation in Malaysia. The operating expenditure should include local services for insurance, legal, banking, ICT and transportation; if those services could be sourced from local/domestic service providers.** However, this amount shall not include the cost of goods sold, depreciation, interest on borrowings and expenses that are not directly involved in the company's proposed activities.

D. Malaysia's participation in the Organisation for Economic Cooperation and Development (OECD) taxation initiatives

Malaysia had joined the Inclusive Framework (IF) on Base Erosion and Profit Shifting (BEPS) in January 2017 and became a BEPS Associate under the IF. As a BEPS Associate and a member of the Forum on Harmful Tax Practices (FHTP), Malaysia has to comply with the 'Base Erosion Profit Shifting (BEPS) Action 5: Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance' Report.

Contract R&D incentive is one of the incentives evaluated by the FHTP in 2017 and has been categorised under **Non-IP Regime** where companies must ensure **substantial activity requirements** are undertaken in the country to enjoy the incentive.

For Non-IP Regime, **substantial activities** are defined as having **adequate number of full-time employees working in Malaysia with necessary qualifications and incurring adequate amount of operating expenditure in such activities.**

Treatment of tax incentive approvals

- Approvals **before** 16 October 2017
Companies **approved before 16 October 2017 can continue to enjoy the existing incentive without the imposition of substantial activities requirements as mentioned in paragraph (iv), (v) and (vi) of Section C (Eligibility Criteria) until 30 June 2021.**
- Approvals **starting from** 16 October 2017
Companies **approved starting from 16 October 2017 without the substantial activities requirements as mentioned in paragraph (iv), (v) and (vi) of Section C (Eligibility Criteria) can only enjoy the existing incentive until 27 December 2018.**

In both scenarios, companies are required to comply with the new substantial activities requirements and submit their applications to MIDA if they wish to continue enjoying the incentive.

E. Expatriate Post(s)

Contract R&D Companies and R&D Companies which undertake R&D projects may also apply for expatriate post(s). However, the company should endeavour to train Malaysians in the same field.

F. Qualifying Capital Expenditure

- i. For the purpose of ITA in relation to manufacturing-based research, qualifying capital expenditure means capital expenditure incurred on factory or any plant and machinery used in Malaysia in connection with and for the purposes of an activity relating to research and development.
- ii. For the purpose of ITA in relation to agriculture-based research, qualifying capital expenditure means capital expenditure incurred in respect of the clearing and preparation of land, the planting of trial crops, the provision of irrigation or drainage systems, the provision of plant and machinery used in Malaysia in connection with and for the purposes of an activity relating to research and development, the construction of access roads including bridges, the construction or purchase of buildings (excluding those provided for the welfare of people or as living accommodation) and structural improvements on land for the purposes of activity relating to research and development.

G. Procedure for Application

- i. Applications should be made online through MIDA e-TRANS portal at URL <https://investmalaysia.mida.gov.my>
- ii. Application with incomplete information will not be accepted and will be returned to the company.
- iii. For enquiries and clarification, please refer to:

Website : www.mida.gov.my
Tel : (603) 2267 3633
Fax : (603) 2274 7970
E-mail : investmalaysia@mida.gov.my

H. Effective Date of This Guideline

This Guideline is **effective starting from 27 December 2018 (in line with the Finance Bill 2018)**. This new guideline will supersede the earlier Contract R&D guideline issued by MIDA.