

**GUIDELINE FOR APPLICATION BY CONTRACT RESEARCH AND DEVELOPMENT COMPANIES OR RESEARCH AND DEVELOPMENT COMPANIES FOR:**

- I. RESEARCH AND DEVELOPMENT STATUS COMPANY; OR**
- II. TAX INCENTIVE FOR RESEARCH AND DEVELOPMENT SERVICES**

**UNDER THE PROMOTION OF INVESTMENTS ACT, (PIA) 1986**

**A. Definition of Research and Development (R&D) in the PIA 1986**

- 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 objective 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) Contract R&D Company means a company which provides R&D services in Malaysia only to companies other than its related companies and approved as a R&D Status Company.**
  
- iv) R&D Company means a company which provides R&D services in Malaysia to its related companies or to any other company and approved as a R&D Status Company.**
  
- v) Related company has the same meaning assigned to it in Section 2 of the Promotion of Investments Act, 1986.**

## **B. R&D Status Company**

- i) The Promotion of Investments Act (PIA) 1986 defines "**Contract R&D Company**" and "**R&D Company**" as companies that have been approved as an **R&D Status Company** with effect from **1 January 2022**, in accordance with the amendments made via the **Finance Bill 2021**. According to the amendment, only R&D Status Companies are eligible for the following:
  - a. **Tax incentive** for Contract R&D Company or R&D Company
  - b. The clients who use the services of a Contract R&D Company or an R&D Company are eligible for the **R&D Double Deduction Incentive**.
- ii) The Finance Bill 2021 also states that **existing companies that have been granted approval in fulfilling the definition of Contract R&D Company or R&D Company prior to 1 January 2022 and intend to be granted R&D Status Company under the PIA 1986 must notify MIDA within the grace period of 1 January 2022 to 30 June 2022 for consideration. Companies that fail to notify MIDA within the grace period will cease to be approved companies** fulfilling the definition of Contract R&D Company or R&D Company.
- iii) **Starting from 1 January 2022, the approval of R&D Status Company is granted for a period of five (5) consecutive years starting from the date of approval or any other date as may be determined by the Minister.**
- iv) Companies approved with this status **may apply for extension subject to compliance** of all criteria and conditions. The **extension of R&D Status Company will be granted for another five (5) consecutive years starting from the end date of the previous approval. Companies are required to provide information and documents on their compliance to the conditions** imposed previously in their approval letters by filling up the '**Forms on Compliance of Conditions for R&D Status Companies**' which is available in MIDA's website.
- v) **The approval of R&D Status Company will be ceased at the end of five (5) years should MIDA does not received any application for extension of R&D Status Company. This may cause double deduction could not be claimed by company's clients.**
- vi) **For new/existing companies that have yet to begin operations at the time of submission to MIDA**, these companies **must notify MIDA on their starting date of operation by completing the 'Notification Form on Business Operation' (available on MIDA's website)**, and MIDA will issue an acknowledgement letter for the purpose of claiming double deduction by the company's clients.
- vii) **Unrelated companies incurring expenses for using the R&D Status Company's services are eligible for the double deduction incentive under Section 34B** of the Income Tax Act of 1967, subject to the condition of eligible expenditure. Meanwhile, the **double deduction incentive is only eligible to related companies after the R&D Status Company's incentive period has ended (if there is tax incentive approved to the R&D Status Company).**

## C. Tax Incentive

### i) New Contract R&D Company / R&D Company:

#### a) Tax Incentive for 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.

#### b) Tax Incentive for 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.

#### ***Note on submission of applications:***

- *The application for Pioneer Status must be submitted to MIDA **before commencing operations***
- *The application for Investment Tax Allowance must be submitted to MIDA **before commencing operations and not later than three years from the date of first qualifying capital expenditure is incurred***

### ii) Existing Contract R&D Company / R&D company:

**Existing Contract R&D Company / R&D Company** is eligible for the **second round of tax incentives (PS/ITA)** which includes:

- The existing company has not enjoyed PS/ITA for R&D activities; or
- The existing company has been granted PS/ITA for R&D activities and the PS/ITA has expired, and
- The existing company plans to undertake reinvestment for the following R&D activities:
  - a) expansion of existing R&D activities - reinvestment (by way of additional expenditure on plant, machinery and building); or

- b) engaged in new research projects/research methodology/ processes/products (without additional investments) - applicable only for Contract R&D company applying for PS

**Note on submission of applications:**

➤ **Contract R&D company**

*The application for Pioneer Status must be submitted to MIDA:*

- *Before commencing operations of the expansion project or engagement of new project, and after the expiry date of existing PS/ITA.*

*The application for Investment Tax Allowance must be submitted to MIDA:*

- *Before the date of first qualifying capital expenditure is incurred, and after the expiry date of existing PS/ITA.*

➤ **R&D Company**

*The application for Investment Tax Allowance must be submitted to MIDA:*

- *Before the date of first qualifying capital expenditure is incurred, and after the expiry date of existing ITA.*

**D. Eligibility Criteria**

- i. The company must be incorporated under the Companies Act 2016 and resident in Malaysia.
- ii. The R&D activities undertaken must comply with the definition of R&D under the Promotion of Investments Act, 1986;
- iii. The R&D activities undertaken must be in accordance with the needs of the country and bring benefits to the Malaysian economy;

***Criteria (i), (ii) and (iii) must be complied upon submission of application for R&D Status in MIDA***

- iv. **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)<sup>1</sup> if any, is excluded.**
- v. **For manufacturing-based research and development**, the company must have **adequate<sup>2</sup> number of full-time employees working in Malaysia** performing research and technical functions with:
  - a) Degree in science and technical field; or
  - b) Diploma in science and technical field with minimum experience of 5 years in relevant field.

Those employees must and comprise of **at least 50%** of the company's total workforce.

- vi. **For agricultural-based research and development**, the company must have **adequate<sup>2</sup> number of full-time employees working in Malaysia** performing research and technical functions with:
  - a) Degree in science and technical field; or
  - b) Diploma in science and technical field with minimum experience of 5 years in relevant field.

Those employees must and comprise of **at least 5%** of the company's total workforce.

- vii. The company must incur **adequate<sup>2</sup> 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.** 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.

#### **E. 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.**

<sup>1</sup> *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).*

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

## **F. 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.

## **G. 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.

## **H. Procedure for Application**

- i. Applications must be submitted online at <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](http://www.mida.gov.my)  
Tel : (603) 2267 3633  
Fax : (603) 2274 7970  
E-mail : [investment@mida.gov.my](mailto:investment@mida.gov.my)

## **I. Effective Date of This Guideline**

This Guideline is **effective starting from 1 January 2022 (in line with the Finance Bill 2021)**.