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Tax Incentives for Principal Hub 3.0 and Global Trading Centre

Following the tax proposals in Budget 2021 to encourage more companies to relocate to Malaysia as a regional and global hub to conduct strategic management, control and support functions, the Malaysian Investment Development Authority (**MIDA**) has recently published the following guidelines:

- Guidelines for Principal Hub Incentive 3.0
- Guidelines on Incentive for Setting Up a Global Trading Centre

The Principal Hub Incentive 3.0 is revised and replaces Principal Hub Incentive 2.0 to encourage further establishment of Principal Hub in Malaysia. The incentive pertaining to trading activities which was previously covered under Principal Hub 2.0 has been removed and is now covered under incentive for setting up a Global Trading Centre. Both guidelines are applicable for applications received by MIDA from 1 January 2021 until 31 December 2022.

1. Guidelines for Principal Hub Incentive 3.0

1.1 What is a 'Principal Hub'?

"Principal Hub" is defined as a locally incorporated company that uses Malaysia as a base for conducting its regional or global businesses and operations to manage, control, and support its key functions including management of risks, decision-making, strategic business activities, finance, management and human resource.

1.2 How to qualify as a 'Principal Hub'?

In order to qualify for the Principal Hub Incentive 3.0, the applicant company must satisfy the following criteria:

- Must be locally incorporated and resident in Malaysia;
- Has paid-up capital of more than RM2.5 million; and
- Serves/controls a minimum number of network companies, which are defined as:
 - related companies or entities within the same group including subsidiaries, branches, and joint ventures; and
 - non-related companies that have a contractual agreement of at least two years with the applicant or applicant's ultimate holding company with regard to the

applicant's business or supply chain.

The core income-generating activities of a Principal Hub must also include providing the compulsory services, Regional P&L/Business Unit Management and Strategic Business Planning & Corporate Development, and additionally, a minimum of two other qualifying services. As listed in the guidelines, the qualifying services include certain strategic services, business services and shared services.

1.3 What are the tax benefits?

The incentive benefit for qualifying Principal Hubs is a reduced tax rate depending on the nature of the applicant company as follows:

- For qualifying new manufacturing and services companies, tiered tax rates on services income derived from qualifying Principal Hub activities are provided based on the level of commitment of the company in terms of the number of high-value jobs and key positions, the amount of annual operating expenditure, and the number of network companies:
 - Tier 1 — 0% rate for five years plus extension of another five years
 - Tier 2 — 5% rate for five years plus extension of another five years.
- For existing manufacturing/services companies, a 10% tax rate is provided on qualifying service income for five years of assessment.

Tax exemption is only applicable for service income. Royalties and other income derived from intellectual property rights are excluded from the incentive.

Depending on the nature of the applicant company, different incentive commitments apply. This includes the requirements to increase high-value jobs and annual operating expenditure for tier 1 and 2 companies to qualify for the five-year extension.

2. Guidelines on Incentive for Setting Up a Global Trading Centre (GTC)

2.1 What is a Global Trading Centre?

A Global Trading Centre (**GTC**) is a locally incorporated company that uses Malaysia as its international trading base for undertaking strategic sourcing, procurement and distribution of raw materials, components and finished products to its related and unrelated companies in Malaysia and abroad.

2.2 What are the tax benefits?

As an approved company with GTC incentive, the company may enjoy a tax incentive of a concessionary corporate tax rate of 10% for five years. The period of incentive may be extended for another five years. The company may only enjoy the GTC incentive if it undertakes GTC activities and complies with the eligibility criteria.

2.3 Who is eligible?

To qualify for the GTC incentive, a company must fulfil the eligibility criteria:

- (a) Newly incorporated and resident in Malaysia
- (b) Using Malaysia as its international trading base for undertaking strategic sourcing, procurement and distribution of raw materials, components and finished products to its related and unrelated companies in Malaysia and abroad.
- (c) Paid-up capital of RM1 million
- (d) Annual sales turnover of RM300 million from qualifying activity
- (e) Annual operating expenditure of RM1.5 million from qualifying activity
- (f) Minimum 15 high-value jobs with basic monthly salary of at least RM5,000 (at least 50% of the high-value jobs must be filled by Malaysians)
- (g) Must operate in a Licensed Manufacturing Warehouse (LMW), Free Zone (FZ) and/or Bonded Warehouse.
- (h) Must have usage of Malaysian ports and airports.

The issuance of the Guidelines for Principal Hub Incentive 3.0 and GTC is timely and in line with the government's aim to attract more multinational corporations to position Malaysia as a regional and global operation hub and thereby create more job opportunities. The effort to attract and retain multinational corporations can be seen as the application period for the incentives has been extended to 31 December 2022. Further, in relation to tax incentives for Principal Hub 3.0, current qualifying conditions relating to the number of value-added jobs, annual operating expenditure and number of key posts are relaxed for the second five-year period of the incentive. By introducing the new GTC incentives for trading activities, more specific and targeted conditions are also introduced.

Nevertheless, multinational corporations that qualify for these incentives should also closely scrutinise the conditions and requirements imposed by the government. In recent years, tax authorities have had the tendency of retrospectively revoking tax incentives and clawing back taxes if there is any non-compliance of the conditions and requirements.

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