INTERNATIONAL BAR ASSOCIATION

Malaysian Shipping Tax
The current tax structures used in Malaysian shipping
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MALAYSIAN SHIPPING TAX

STRUCTURES IN USE

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Introduction
Good afternoon everybody.

I have to apologise, from the beginning, for my topic, of what must be, the driest subject ever: Malaysian shipping tax.

So to eleviate the dreariness, I thought it would be helpful, to know that Malaysian shipping tax, does not only involve Malaysian tax. Like all cross jurisdictional practices, it also incorporates, other tax jurisdictions, into its structures.

I have also peppered my talk, with lots of pictures, to help envision, these jurisdictions.

*I like to quote Frank Sinatra, who once told a new singer: "They only remember, your first song and your last song". Following Frank Sinatra, here is my first song: a slide of Kuala Lumpur.

Kuala Lumpur, in case you don't know, is the financial centre of Malaysia. It used to be known, for its Petronas Twin Towers, here in the slide, and its tourism advertisement of being "Malaysia truly Asia".

Today, it is known for corruption scandals, involving other Ms: 1MDB, missing Mongolian models, and the new leader of the opposition – Mahathir Mohammad.

Hence its tax structures, too have become similarly creative. I am not here today, to comment on, the alleged political corruption, or multinational criminal investigations, on supposedly, USD11 billion of funds.

I am here to comment, on how the funds, might have been disposed of – um, transferred – because chances are, (I wouldn't have any personal knowledge of this) the tax structure, would have been similar to, cross jurisdictional tax structures, generally used, in Malaysian shipping today.

These jurisdictions, include the Malaysian onshore tax regime, the Labuan Malaysia offshore tax regime, the Singapore tax regime, the Jersey & Guernsey British offshore tax regime, and the Cayman Islands British offshore tax regime.

So I have quite, a few jurisdictions to cover. I hope you will forgive me, for whizzing through.

Malaysia – onshore and offshore tax systems
I shall start, as can be expected, with the Malaysian tax regime.

*First, here is a slide, of a map of Malaysia, to show the location of Kuala Lumpur, relative to Labuan. As you can see, Kuala Lumpur, the capital of Malaysia, is in West Malaysia. Labuan, although a Federal territory as well, is in East Malaysia. The South China Sea is in the middle.

Kuala Lumpur, and the rest of Malaysia, apply, the onshore Malaysian tax regime, pursuant to, the Income Tax Act of 1967. Labuan, applies the offshore, Malaysian tax regime, pursuant to, the Labuan Business Activity Tax Act 1990.

Malaysian Income Tax Act 1967
*The main provision, governing the shipping tax regime, is Section 54A(1) & (2) of the Income Tax Act 1967, as amended by, Section 11 of the Finance Act 2012.

*So Section 54A now, exempts **70%** of **shipping profits,** from tax for **residents,** that "*transport passengers or cargo by **sea,** on a **Malaysian ship**; or residents, that let out on **charter,** a Malaysian ship, **owned** by Malaysian residents, on a voyage, or time chartered basis".* So ships that are bareboated, do not qualify for the exemption.

***Prior** to the Year of Assessment 2014, the exemption was 100%. The applicable regulation for that, was Public Ruling No. 10/2012. It was issued by the Inland Revenue Board of Malaysia, to explain the Tax Treatment, of a Malaysian Ship, and 100% exemption, of shipping income, of a Malaysian resident, prior to 2014.

Malaysian ship
*What then, constitutes, a Malaysian ship, since coming, under the definition, of a Malaysian ship, is key, to obtaining, the 70% tax exemption? The requirements, are set out, in the Merchant Shipping Ordinance 1952.

A Malaysian ship, has to be, a **sea-going** ship. It can't be a ferry, barge, tug-boat, supply vessel, crew boat, lighter, dredger, fishing boat or other such vessel. Above all, it must be registered, as a Malaysian ship, under Section 11, of the Merchant Shipping Ordinance 1952.

You can only register a Malaysian ship if it is wholly owned by Malaysian citizens, or a company incorporated in Malaysia, with its principal office in Malaysia, its management is mainly in Malaysia, and the majority of the shareholding is held by Malaysian citizens free from any trust or obligation in favour of foreigners. (nobody really knows what **that** means) because it has not been tested. What the Registry of Ships does is to look into the corporate forms to see majority Malaysian shareholding & directorships.

Labuan Business Activity Tax Act 1990 (LBATA)
*The Labuan offshore tax regime, can involve, the leasing of the ship, on a **bareboat** charter basis.

*This leasing must be **licenced**, pursuant to the Labuan Financial Services and Securities Act 2010.

It must be categorized, as a Labuan **business activity**, pursuant to the Labuan Business Activity Tax Act 1990.

*It must be carried out, in Labuan or outside Malaysia, but **not** in Malaysia, unless it is additionally licenced. In which case, an additional RM60,000.00 in licencing fees, or about USD13,500.00, is payable.

*Once all these requirements are fulfilled though, similar to Malaysian onshore tax exemptions, Labuan shipping business activities, are not entirely tax exempt.

*A Labuan business activity, is either subject to tax, of **3%** of net profits, as reflected in the audited accounts, or to a **fixed** amount of tax, of **RM20,000** (whichever the company elects). Today, this is about, the equivalent of, USD4,500.00 – probably the amount of our conference fees!

Therefore Labuan companies, essentially pay, tax and leasing licencing fees, of RM20,000.00, being USD4,500.00, or RM60,000.00, being USD13,500.00, a year per ship, depending if the ship, is bareboated into, or out of Malaysia.

Alternatively, the company can also opt for the Malaysian Income Tax Act 1967 to apply. Pursuant to Section 3B of the Malaysian Income Tax Act 1967 and Section 2(3) of the Labuan Business Activity Tax Act 1990, the Malaysian Income Tax Act 1967 does not apply to Labuan companies, unless they opt to be taxed pursuant to the Malaysian Income Tax Act 1967.

However, the option, that Labuan companies have, to be taxed under the Malaysian Income Tax Act 1967, became less popular, when the 100% tax exemption, was reduced to 70%, as they then were taxed, **25%**, of 30% of their income.

Labuan ship
*Like Labuan tax, Labuan ships are also the opposite of Malaysian ships. They must be at least 51% **foreign** owned, whereas Malaysian ships, must be at least 51% **Malaysian** owned. They are registered under the same statute, the Merchant Shipping Ordinance 1952, but under a different part, Part IIC.

Malaysian companies
What Malaysian ships and Labuan ships have in common is that they must be owned by Malaysian incorporated companies. These can be either Malaysian companies incorporated pursuant to the Malaysian Companies Act 1965, or the Labuan companies incorporated pursuant to the Labuan Companies Act 1990.

So the upshot of it is, Malaysian ships can be owned by Labuan companies, so long as they are at least 51% **Malaysian** owned.

The Labuan company, would be taxed, pursuant to the Labuan Business Activity and Tax Act 1990, though it owns, a Malaysian ship. The tax structure would look like this slide here.

Trend: Labuan company owning Malaysian ship
In fact the trend, is for ship-owning companies, to incorporate in Labuan, with 100% Malaysian shareholding, and register their ships, as Malaysian ships. This way, the ship-owning structure, qualifies for the RM20,000 / or USD4,500 flat corporate tax rate, as well as, for domestic shipping licences, pursuant to, the Merchant Shipping Ordinance 1952, and Petronas licencing, under the Petroleum Development Act 1974.

Singapore
*We come now, to the role of Singapore, in a Malaysian shipping tax structure. How Singapore, comes into the picture, of a Malaysian shipping tax structure, is by way of a supply of services, into the Malaysian shipping industry. This can be in a myriad of ways, in financing, in ship owning, in specialized shipping legal services, even in crew supply. Above all though, Singapore, is where Malaysian shipping money eventually finds its way to, no matter where it travels to first. All roads lead to Singapore, for Malaysian shipping money - or rather, all shipping lanes.

*Many international shipping banks and specialised international shipping lawyers – including Singapore shipping lawyers, are based in Singapore. Indeed, many Singapore ship owners, supply ships into the Malaysian industry. In more than one Malaysian shipping tax structure, that I have been involved in, the **Ultimate Beneficial Owner** is **Singaporean**.

What is the tax regime for shipping in Singapore then? How is it incorporated into the Malaysian shipping tax structure?

Singapore tax
*In general, income derived, by a company, is taxable in Singapore, at the corporate income tax rate, of **17**%. However, there are specific tax incentives, for the maritime sector, under the Maritime Sector Incentive scheme-award:

They are:

(a) Either **International Shipping Operations**, where the income, of a shipping enterprise, derived from the operation of a Singapore registered ship, (other than within limits of the port of Singapore), for the carriage of passengers, mails, livestock or goods, towing or salvage operations, charter or ships or use of the ship as a dredger, seismic ship or vessel, used for offshore oil or gas activity, is **100% exempt** from Singapore tax;

(b) Another tax incentive, for the maritime sector, is the **Approved International Shipping Enterprise Scheme**, which also exempts 100% from tax, income derived from the operation/charter, of the shipping company's, fleet of foreign ships, and income derived from leasing, and bareboat charter, of an **approved** ship leasing company.

(c) There is also **withholding tax exemption** for all bareboat, voyage and time charter payments to non-residents (excluding permanent establishments in Singapore for use of ships).

Additionally, there are concessionary tax rates, for ship lessors, including income derived, from finance leasing of ships, which are wholly tax exempt, and only 5% or 10% tax on certain prescribed qualifying income (for instance **approved shipping investment management activities**, **approved container leasing activities**, etc), as well as, automatic withholding tax exemption, on qualifying payments, made in respect of, qualifying foreign loans, taken to finance the purchase, or construction, of both Singapore-flagged, and foreign-flagged ships, and acquisition, of qualifying containers, and intermodal equipment.

There is a whole range, of supporting shipping services, which also qualify, for a concessionary tax rate, of 10%, including ship management, ship agency, and shipping freight/logistic services, ship broking and freight forwarding, and qualifying corporate services.

Singapore ships
*As for Singapore ships, they are subject to a maximum of S$10,000 registration fees. The criteria to register Singapore ships are they must be Singapore citizens or Singapore permanent residents; alternatively they must be companies incorporated in Singapore.

*They **may** be **either foreign** owned (meaning more than 50% of their equity is owned by non-Singapore citizens) **or locally** owned (more than 50% of its equity owned by Singapore citizens).

For foreign owned companies, they must have a **minimum paid-up capital of SGD50,000**, which is about USD30,000.00, and at least 1,600 GT as well as self-propelled. However, these additional requirements, may be waived, by the Registrar of Ships, in his absolute discretion.

Guernsey
*Now, to explain about Guernsey. It is often, desirable, in a Malaysian shipping tax structure, to choose an additional, layer of ownership, for confidentiality reasons. The usual choice, is a more established, foreign tax friendly offshore jurisdiction, to own the Labuan ship owner.

Information, on Labuan companies, directorships and shareholding, are not publicly available, by way of a search, on the registry, upon payment of a fee, and requires the consent, of the company or the trust. However, an additional layer, increases the distance, of the ultimate beneficial ownership, from the ship, supplied into the Malaysian shipping industry, and increases the secrecy – I mean, confidentiality.

*Guernsey is thereby popular. It fulfils all the requirements, and there is no corporation income tax, on income from businesses, offices and employments and other sources.

No withholding tax applies, to dividends paid, by Guernsey companies, to non-resident shareholders.

Guernsey or Jersey trusts
*It is not just, the favourable tax regimes, of Guernsey or Jersey, to foreign owners, which is useful, in a Malaysian shipping tax structure. As a **trust** jurisdiction, **confidentiality** is **key**. **No** information can be given out **by law** by the administering authority, unless deemed necessary pursuant to the provisions of the Financial Services Commission (Bailiwick of Guernsey) Law, 1987. In Guernsey, the regulatory authority is the Guernsey Financial Services Commission.

Guernsey or Jersey trusts, have other advantages: they can last indefinitely, they can be created for non-charitable purposes, and settlors are allowed a generous amount of powers to reserve or grant to trusted third parties.

Although orphaned trusts, are allowed, under the Guernsey, or Jersey trust legislation, such a trust is not used, in a Malaysian ship owning, or shipping tax structure, because the Ultimate Beneficial Owner, must be either an **individual**, or a **public listed company**. And since there is not much **secrecy** - um **confidentiality** - in a public listed company, the UBO in a Malaysian shipping tax structure, is almost always an **individual**.

Guernsey or Jersey trusts, can have corporate, or individual directors, company secretary, or any other officer of a company, partnership or other unincorporated body, nominee services like nominee shareholders, registered offices or accommodation addresses, executorship services, and the provision of advice in relation to formation, management or administration of trusts as in the acting as or provision of corporate or individual officials. So the Guernsey or Jersey trust regime is very useful for nominee ownerships.

How popular Guernsey trusts, are in shipping tax structures, I believe is reflected in the difficulty we had, in a ship financing transaction, in finding a name, for the Guernsey trust, with a maritime flair. I won't tell you the name, we finally settled with, but I can tell you, that the Kraken was taken, along with Barbosa, and the Black Pearl.

Cayman Islands
Another favoured tax jurisdiction, in Malaysian ship owning tax structures, is the Cayman Islands. It too keeps confidential, all information, relating to Cayman Islands trusts, which will only be released, on consent of the Cayman Islands entity. There is also no direct taxation, on the earnings, of any Cayman Islands corporation. It has one more advantage above Guernsey and Jersey though, in the securing of confidentiality: **distance from Malaysia**.

*I believe that brings me, back to my earlier quote, from Frank Sinatra, that they only remember your first song and your last song. Here is my last song: a slide of Cayman Islands.

It actually looks like Malaysia. I will end on this note. Do enjoy the rest of the conference. Thank you for listening to my paper.

Kuala Lumpur, October 2015