

Client Alert

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Remote Working in the Age of COVID-19: Malaysian Tax Implications

In response to the global outbreak of COVID-19, employers around the world are moving rapidly to implement remote working arrangements to comply with mandates and orders imposed by governments or as part of their business continuity strategies.

With the shift from a physical workforce to a remote workforce, the result is that employees may choose to relocate to their home country for personal reasons, or may work remotely elsewhere in a different country due to international travel restrictions and quarantine measures.

The rise of a remote workforce will give rise to significant tax issues and in this alert, we address the potential Malaysian tax implications of a remote workforce.

Potential Tax Implications for Foreign Employers

Risk of creating a permanent establishment ("PE")

A remote workforce may create PE risks for a foreign enterprise, resulting in the foreign enterprise being subject to tax exposure in Malaysia.

The PE risk may arise as a result of having (a) a fixed place of business or (b) through a dependent agent. Depending on the applicable double tax agreement ("**DTA**"), a PE risk may also arise as a result of other activities performed by the enterprise's employees.

Fixed Place of Business ("**FPOB**") PE

Where an employee is temporarily based in a different jurisdiction from his employer, the presence of the employee may trigger a PE for the employer in that jurisdiction.

Where there is a comprehensive DTA, a FPOB PE means any fixed place of business through which the business of an enterprise is wholly or partly carried on.

The OECD Model Tax Convention on Income and on Capital clarifies that a FPOB PE will be triggered where:

- a) a place of business exists in the jurisdiction, i.e., a facility such as premises or, in certain circumstances, machinery or equipment;
- b) the place of business is fixed, i.e., it must be established at a distinct place with a certain degree of permanency (generally more than 6 months); and
- c) the business of the enterprise is carried on through the fixed place of business.



As such, there may be a FPOB PE risk if an employee of a foreign enterprise in a jurisdiction which has a DTA with Malaysia, is marooned in Malaysia for an extended period, and has premises at his disposal in Malaysia (e.g., an office) with a degree of permanency to perform his work activities during this time.

Dependent Agent PE

A PE can also be created through a dependent agent. A person is a dependent agent if that person acts on behalf of the foreign enterprise and has, and habitually exercises, in a different jurisdiction an authority to conclude contracts in the name of the foreign enterprise.

Where there is a comprehensive DTA, an enterprise may be deemed to have a dependent agent PE if a person, other than an agent of independent status, acts on behalf of the enterprise, and habitually exercises in a contracting state an authority to conclude contracts in the name of the enterprise. In these circumstances, there may be a dependent agent PE risk for example if a sales employee of a foreign enterprise in a jurisdiction which has a DTA with Malaysia is in Malaysia for an extended period, and exercises an authority to conclude contracts on behalf of the foreign enterprise during this time.

Profit allocation if PE is found

If a PE is found in Malaysia and there is a comprehensive DTA in place, the profits attributable to this PE will be subject to tax in Malaysia.

The OECD guidance on the Authorized OECD Approach recommends that the profits are profits which the PE is expected to make if it were a separate and independent enterprise engaged in the same or similar activities under the same or similar conditions, taking into account the functions performed, assets used and risks assumed through the PE and through other parts of the enterprise. However, as Malaysia has not adopted the AoA approach, the PE rules in the comprehensive DTA will govern the treatment of profits attributable to the PE in Malaysia.

Tax residency

Directors of a company may also find themselves being subject to international travel restrictions. As such, it may also be the case that there is risk of a company losing its tax residency status in Malaysia.

A company is tax resident in Malaysia for a basis year if at any time during that basis year, the management and control of its affairs are exercised in Malaysia. Where the directors of a company are working remotely in a foreign country, there may be a risk that the management and control of its affairs will not be deemed to be exercised in Malaysia (e.g., because board meetings are not held in Malaysia) and the company will thus not be deemed to be tax resident in Malaysia. The Inland Revenue Board of Malaysia will not issue a certificate of residency if board meetings are held virtually instead of convening physical meetings in Malaysia.



To manage this risk, it may be the case that companies will have to consider appointing more local directors so as not to compromise on the company's tax residency status in Malaysia.

Potential Tax Implications for Employees

Personal income tax

Where an employee relocates to Malaysia to work remotely, the employee may be subject to personal income tax in Malaysia on his employment income where the employment is deemed to be exercised in Malaysia. Generally, any income arising from an employment exercised in Malaysia will be subject to tax in Malaysia if the period or periods of employment in Malaysia amount to 60 days or more in aggregate in the year.

Recommendations

As employers manage an increasingly global and remote workforce in the face of COVID-19, employers must take care to manage the tax risks that may arise from employees working remotely in another country.

As such, employers should review their employees' cross-border remote working arrangements in order to ascertain the potential Malaysian tax implications for the employer and the employee. It would also be prudent for employers to monitor any cross-border remote working by their employees and ensure that such employees adhere to corporate guidelines in order to avoid any adverse tax consequences.

What We Can Help With

Our dedicated team of tax lawyers can help you navigate the complexities of the evolving global landscape to stay competitive and compliant and we can support you through some of these ways:

- a) we can review, analyse and advise on remote working arrangements and ways to manage and mitigate Malaysian tax risks;
- b) we can assist with assessing the circumstances and nature of the business activities undertaken by your remote workforce;
- c) we can assist with preparing guidelines or a specific framework that can be shared with your employees to manage your tax risks.

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