



# Regional Headquarters?

**Malaysia, Singapore, Hong Kong – where would you wish to locate your regional headquarters? A comparison of the tax benefits for regional headquarters locations.**

It goes without saying that globalisation has spurred the demand for regionally controlled coordination functions in multinational corporations (MNCs).

Today, the MNCs are increasingly looking to centralise global and regional functions such as finance, technology, bulk procurement, human capital, research and to address regional customer requirements.

The global economic shift towards Asia and its growing economies has also given rise to increased interest in setting up of regional headquarters in Asia to capitalise on the strategic importance of this region.

The choice of a regional headquarters (RHQ) location is dependent on many factors, including the overall eco-system, the availability of financial services, human capital, infrastructure, accessibility, the legal framework, political stability, cost of living, and last but not least, the tax regime.

Hong Kong and Singapore have

historically been successful in attracting RHQs to their shores with Malaysia not far behind.

One of the considerations for MNCs is the availability of tax incentives for the establishment of a RHQ. This article broadly compares the tax benefits offered in Malaysia, Singapore and Hong Kong for RHQs and also addresses other tax factors, which are important.

## **RHQ INCENTIVES MALAYSIA**

In Malaysia, the key tax incentive for attracting RHQs is the Operational Headquarters (OHQ) incentive. To be eligible for the OHQ incentive, a company must be incorporated in Malaysia, it must incur RM1.5 million annual business spending and it is required to have a paid up capital of RM500,000.

The OHQ must offer at least three

qualifying services to three or more related companies outside Malaysia. The qualifying services mainly comprise business management and administration, procurement, marketing, data management, training, research and development, treasury and corporate financial advisory services.

An OHQ will be able to enjoy a 10-year tax exemption on the following sources of income:

- Business income arising from qualifying services rendered to its offices or related companies outside of Malaysia. However, where such services are also provided to related companies in Malaysia, in order to enjoy the full tax exemption, the income derived from Malaysian related companies should be capped at 20%. Otherwise, only a portion of the income from the provision of services to related companies in



also an incentive for Treasury Management Centres (TMCs).

This incentive is aimed at attracting global or regional companies to locate their treasury operations in Malaysia.

This would be attractive to groups who have carved out or are looking to carve out their treasury activities into a separate treasury company. The incentive is similar to the OHQ incentive but only exempts 70% of the income from qualifying treasury activities from tax for a 5-year period.

Further, the incentive provides for an exemption from Malaysian withholding tax on interest payments from the TMC, and expatriates will be taxed in the same manner as those employed by OHQs.

### SINGAPORE

Singapore offers RHQ and International Headquarters (“IHQ”) tax incentives to attract MNCs to use Singapore as their base for their regional headquarter activities in managing and overseeing their businesses both in the region and globally. The RHQ and IHQ tax incentives are awarded to companies incorporated or registered in Singapore.

For the RHQ incentive, similar to the Malaysian OHQ requirement, the RHQ must provide at least three qualifying headquarter services to at least three group companies outside Singapore. Qualifying headquarters services include general management and administration, intellectual property management, shared services, and corporate finance advisory services.

By the end of the third year of the incentive period, the company should have a minimum paid-up capital of S\$500,000 and an incremental annual local business expenditure of S\$2 million.

An approved RHQ company can enjoy a reduced income tax rate of 15% on incremental qualifying activities for a period of up to 5 years.

For an approved IHQ company, customised incentive packages with lower concessionary income tax rates, typically at 0%, 5%, or 10% on its qualifying income may be offered.

The requirements for this incentive are modelled on the RHQ incentive, but are more stringent and require the IHQ

to exceed the minimum requirements imposed on RHQs. The IHQ incentive is also generally given for a longer period of time and can be for up to 20 years.

The level of support or tax incentives given would generally be aligned to the proposed investment and level of commitment dedicated to Singapore.

Aside from these incentives, the corporate tax rate of 17% in Singapore in itself is attractive to MNCs, where the incentive criteria cannot be met.

### HONG KONG

Unlike Malaysia and Singapore, Hong Kong does not offer targeted incentive regimes for headquarters operations, and yet, it has been one of the favourite picks amongst the MNCs since the early 1990s.

Its major attractions lie with it being one of the world’s leading financial and business centres, its simple and low tax regime, as well as its close geographical proximity to Mainland China. In line with its free market policies, Hong Kong also has flexible foreign exchange policies.

Notwithstanding the absence of specific RHQ incentives, Hong Kong has been very successful in attracting RHQs.

Clearly therefore, tax incentives alone are not the sole attraction – although Malaysia and Singapore offer similar incentives, Singapore has the larger share of RHQs than Malaysia.

From a tax perspective alone, Singapore and Hong Kong offer lower corporate tax rates as compared with Malaysia. With tax rates of 17% and 16.5% respectively, as compared with Malaysia’s 25% rate, they have a head start.

When incentives have expired, domestic corporate tax rates will kick in and in this regard, Malaysia is presently at a disadvantage.

Aside from corporate tax rates, personal tax rates in Singapore and Hong Kong are also lower than Malaysia and this can be an important push factor. In the case of highly paid expatriates, particularly where taxes are borne by employers, personal taxes can amount to a substantial cost.

### TAX FRAMEWORK OF OTHER JURISDICTIONS

In assessing the tax considerations of

Malaysia would be exempt.

- Interest income on foreign currency loans extended by the OHQ to its offices or related companies.
- Royalties received from research and development work carried out in Malaysia by the OHQ on behalf of its offices or related companies.

To attract expatriates to work for an OHQ, the expatriates employed by the OHQ will be taxed only on the portion of their chargeable income attributable to the number of days that the expatriates are in Malaysia.

In addition, the foreign exchange rules imposed by the Central Bank, which are applicable to OHQs, are more flexible and the OHQ status will also facilitate employment of expatriate employees with relative ease.

In addition to the OHQ incentive, there is

RHQs, it is also important to address the tax framework of the jurisdictions to which the RHQ will provide services. In many of these jurisdictions, withholding taxes may be imposed on the payment of services fees, interest and royalties to the RHQ.

Such withholding tax costs will need to be factored against the savings arising from tax incentives enjoyed by the RHQ.

As is usually the case, the RHQ will be exempt from tax (as a result of incentives) and accordingly, no relief will be given in the RHQ location country for the withholding tax suffered at source (in the jurisdictions of the group companies to whom services are provided).

Hence it is generally preferred that the RHQ be located in a jurisdiction which has a favourable tax treaty network offering lower withholding tax rates.

In this regard, both Malaysia and Singapore have wide treaty networks and on balance, the withholding tax rates offered under their treaties do not clearly set one jurisdiction at an advantage against the other.

Hong Kong, historically has had a limited treaty network, but in recent years, it has significantly widened its treaty network as well.

Therefore, depending on the countries that the RHQ will provide services to and derive income from, in deciding the most tax efficient location, it is important to consider the tax treaties concluded by the proposed RHQ location country.

### TRANSFER PRICING

Lastly, in providing services to related companies, transfer-pricing considerations need to be considered.

Where the RHQ has been granted tax incentives, be it in Malaysia, Singapore or Hong Kong, transfer pricing rules must be considered both from the perspective of the RHQ jurisdiction as well as the jurisdiction in which the group companies (to which services will be provided are located).

Gone are the days of charging high fees by RHQs located in tax efficient jurisdictions



to group companies located in the region or indeed globally.

Transfer pricing rules, which are becoming increasingly important both regionally and globally will need to be taken into account in establishing an appropriate fee to be charged by the RHQ. In essence, the fees will need to be at arm's length.

### OTHER CONSIDERATIONS

Overall, tax incentives are still relevant and tax is always an important consideration. However, other considerations are important and often outweigh tax considerations.

These would include political stability and transparency, the financial system, the cost of living, the cost of doing business, the legal framework, ready access to human capital, security factors, the availability of healthcare and international education facilities, etc.

In recent years, the high cost of living including high rental costs, and environmental considerations, such as rising pollution levels have seen Hong Kong diminish its attractiveness as a preferred RHQ location.

Singapore too has seen its escalating costs being viewed as a barrier as compared with Malaysia. However, Singapore has many perceived advantages in relation to several of the other considerations outlined above.

The Singapore government is often one step ahead of the game and its investor and business friendly policies are a challenge to compete with.

Malaysia on the other hand is taking pro-active steps to attract MNCs into the country and to establish investor and business friendly policies.

It still has some way to go in developing its image as a preferred location for MNCs looking to place their RHQs in the region, but its lower costs, its infrastructure, the availability of human capital, the significant growth of world class health care and educational establishments are some of the factors that hold it in good stead.

### CONCLUSION

In this climate of intensified competition, governments around the world are competing for investment and in doing so are proffering tax and other incentives to foreign investors. Each of the locations discussed in this article has its attractions as a RHQ location.

From a tax incentive perspective, there is little to distinguish Malaysia from Singapore, and from the general tax framework, there is little to distinguish Singapore from Hong Kong.

Further, from a tax perspective, it is important to also consider the tax framework in the jurisdictions of the group companies, which will be serviced by the RHQ.

Whilst tax benefits are important, tax is only one of the factors in attracting RHQs to a particular country.

Other factors will often outweigh tax considerations and will be pivotal in determining an MNC's RHQ location. What is clear is that the competition will intensify and as it does so, each country will need to become increasingly innovative in its offerings to MNCs to avoid losing out. **mb**

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