



## FINAL EXAMINATION NOVEMBER 2023

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**COURSE TITLE**            **INTERNATIONAL AND DOUBLE TAXATION**

**COURSE CODE**            **BTAX3313B**

**DATE/DAY**                **17 FEBRUARY 2024 / SATURDAY**

**TIME/DURATION**        **09:00 AM - 12:00 PM / 03 Hour(s) 00 Minute(s)**

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### INSTRUCTIONS TO CANDIDATES :

1. Please read the instruction under each section carefully.
2. Candidates are reminded not to bring into examination hall/room any form of written materials or electronic gadget except for stationery that is permitted by the Invigilator.
3. Students who are caught breaching the Examination Rules and Regulation will be charged with an academic dishonesty and if found guilty of the offence, the maximum penalty is expulsion from the University.

(This Question Paper consists of 7 Printed Pages including front page)

**\*\*\*DO NOT OPEN THE QUESTION PAPER UNTIL YOU ARE TOLD TO DO SO\*\*\***

This question paper consists of FOUR (4) questions. Answer ALL questions in the answer booklet provided. [80 MARKS]

**QUESTION 1**

**(20 Marks)**

- a) Article 5 on Permanent Establishment states that an enterprise of a residence state can create a permanent establishment (PE) in another state through THREE (3) types of business activities, i.e. (i) Asset-type PE, (ii) Construction type PE and (iii) Agency PE.
- i) Define how the Asset-type PE is created and the conditions that must be satisfied to constitute a PE under this rule. (6 marks)
- ii) Types of assets that would prima facie constitute a PE (2 marks)
- b) Some business activities as stated under Article 5(4) do not constitute a PE even if they are performed through a fixed place of business.

Kotra Pharma Co is resident in Country R and operates in the pharmaceutical field. The manufacturing of medicines is performed in Country R by Kotra Pharma Co itself. The other processes are taken care of by different branches in four countries as follows:

**Country A:**

Contractor 1 is a branch responsible for purchasing raw materials such as plants used in the production of medicines to be sold by Kotra Pharma Co. The latter has a facility in Country A used for storing the purchased plants. The ownership of the raw material is at the level of the parent company in Country R.

**Country B:**

Contractor 2 is a branch running a laboratory that conducts research and development activities in Country B. Such activities led to developing intellectual property (IP) that the parent company (Kotra Pharma Co) owns. The know-how is used to manufacture the medicine in Country R.

**Country C:**

Contractor 3 is a branch responsible for storing and delivering the final products (medicines) destined to be sold worldwide.

**Country D:**

Kotra Pharma Co has a fixed place where an employee carries out surveys by interviewing patients about symptoms they show and side effects they experience after using the medicine manufactured by Kotra Pharma Co. In Country D, the only activity undertaken is the collection of data by completing the questionnaires. The employee responsible for the task collects and sends the raw information (the questionnaires) to be analyzed in Country R.

**Required:**

State whether the activity performed by the contractors in each Country A, B, C and D in each of the cases above would constitute a PE in that country and explain your basis to support your argument. (12 marks)

**Reference: UN Model Tax Convention**

**Article 5: PERMANENT ESTABLISHMENT**

1. For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on.
2. The term "permanent establishment" includes especially:
  - a) A place of management;
  - b) A branch;
  - c) An office;
  - d) A factory;
  - e) A workshop;
  - f) A mine, an oil or gas well, a quarry or any other place of extraction of; g) Natural resources.
3. The term "permanent establishment" also encompasses:
  - a) A building site, a construction, assembly or installation project or supervisory activities in connection therewith, but only if such site, project, or activities last more than six months.
  - b) The furnishing of services, including consultancy services, by an enterprise through employees or other personnel engaged by the enterprise for such purpose, but only if activities of that nature continue (for the same or a connected project) within a Contracting State for a period or periods aggregating more than 183 days in any 12-month period commencing or ending in the fiscal year concerned.
4. Notwithstanding the preceding provisions of this Article, the term "permanent establishment" shall be deemed not to include:
  - a) The use of facilities solely for the purpose of storage or display of goods or merchandise belonging to the enterprise;
  - b) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage or display;
  - c) The maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;
  - d) The maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise;

- e) The maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character.
  - f) The maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs (a) to (e), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.
5. Notwithstanding the provisions of paragraphs 1 and 2, where a person—other than an agent of an independent status to whom paragraph 7 applies—is acting in a Contracting State on behalf of an enterprise of the other Contracting State, that enterprise shall be deemed to have a permanent establishment in the first-mentioned Contracting State in respect of any activities which that person undertakes for the enterprise, if such a person:
- a) Has and habitually exercises in that State an authority to conclude contracts in the name of the enterprise, unless the activities of such person are limited to those mentioned in paragraph 4 which, if exercised through a fixed place of business, would not make this fixed place of business a permanent establishment under the provisions of that paragraph; or
  - b) Has no such authority, but habitually maintains in the first-mentioned State a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise.
6. Notwithstanding the preceding provisions of this Article, an insurance enterprise of a Contracting State shall, except regarding re-insurance, be deemed to have a permanent establishment in the other Contracting State if it collects premiums in the territory of that other State or ensures risks situated therein through a person other than an agent of an independent status to whom paragraph 7 applies.
7. An enterprise of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that other State through a broker, general commission agent or any other agent of an independent status if such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted wholly or almost wholly on behalf of that enterprise, and conditions are made or imposed between that enterprise and the agent in their commercial and financial relations which differ from those which would have been made between independent enterprises, he will not be considered an agent of an independent status within the meaning of this paragraph.
8. The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other.

**QUESTION 2**

**(20 Marks)**

Teguh Insurance Bhd, a Malaysian resident company, carries on a general insurance business. The company's annual accounts close on 31 December and the information extracted from the accounts for the year ended 31.12.2023 are as follows:

	RM
Net premiums	140,000,000
Allowable expenses	100,000,000
<b>Investment income:</b>	
Rental	34,000,000
Dividend (Single Tier)	28,000,000
Interest (Malaysia)	9,000,000
Interest (UK) (taxed in UK RM100,000)	1,000,000

**Required:**

Compute tax payable for Teguh Insurance Bhd

**QUESTION 3**

**(20 Marks)**

Maju Biru Logistic Sdn Bhd ('MBL') is in the business of providing logistic services for both sea and air transport services. Since June 2018, MBL began operations in tandem with its related company, Denmark Logistics Limited ('DL'), a company incorporated and resident in Denmark, to handle the logistics in the Far East with regards to cargoes moving in this region. To assist with the local operations, DL allowed MBL the use of its proprietary software which is essentially an electronic data processing system (EDP) for use in MBL's logistics operations, but not exploit any of the intellectual property rights in the system. Payment for the use of the EDP is to be made quarterly to DL, and the first of such payments is due in September 2018. The quarterly payments will be in force so long as MBL continues to use the EDP under a contract arrangement.

DL does not have a permanent establishment in Malaysia; and the payments received from MBL are treated as its 'business income' on which income tax is paid in Denmark. The contract for the use of the EDP is signed for five years with effect from 1 June 2018.

The EDP charges are not defined as 'royalty' in the Malaysian double tax agreement with Denmark. The newly appointed Financial Controller of MBL is a little uncertain about withholding tax matters and has written to you for advice.

**Required:**

- i) Explain to the Financial Controller of MBL whether withholding tax should be deducted from the payment to DL for the use of the proprietary software. (13 marks)

Note: You should refer to the extract of the Double Taxation Agreement with Denmark provided below in drawing up your advice, briefly explaining the interpretive approaches to tax legislations.

- ii) Would your answer in (i) above differ if the disbursement to DL is made in one single lump sum upfront payment? (7 marks)

**QUESTION 4**

**(20 Marks)**

Ruth Sdn Bhd (Ruth) is a wholly owned subsidiary of Naomi Ltd (Naomi). Ruth exports its products overseas and to Naomi at the price of RM38 per unit, which was significantly below the price Ruth sells to all its other customers. During a tax audit exercise, the Inland Revenue Board of Malaysia (IRBM) made an assessment against Ruth by disregarding the price it had used in its transactions with Naomi and substituted it with price like what Ruth had sold to other customers. The IRBM argued that the present selling price of the sales to Naomi was not set at arm's length price.

**Required**

- i) Explain why the IRBM was allowed to adjust the selling price for transactions between Ruth and Naomi and what was the rationale behind this power given to the IRBM. (7 marks)
- ii) Article 9 of the OECD Model Convention and the Malaysian Transfer Pricing Guidelines have advocated the use of "arm's length method or principle".  
  
Briefly describe the arm's length principle and the guidance used by taxpayer in adopting it. (4 marks)
- iii) There are FIVE (5) transfer pricing methodologies used in determining the arm's length price. Describe briefly any THREE (3) method on how each method is used. (9 marks)

**\*\*\* END OF QUESTION PAPER \*\*\***

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## APPENDIX

### Extract of the Malaysia Denmark DTA

#### DOUBLE TAXATION AGREEMENT (MALAYSIA – DENMARK)

##### Article XII

1. Royalties derived from one of the Contracting States by a resident of the other Contracting State who is subject to tax in that other Contracting State in respect thereof shall be exempt from tax in the first-mentioned Contracting State provided that such royalties are approved after the signature of this Agreement by the Government of the Contracting State from which they are derived.
2. The term "royalties" as used in this article means a payment of any kind received as consideration for the use of, or the right to use, any copyright, any patent, trade mark, design or model, plan, secret formula or process or for the use of, or the right to use, industrial, commercial or scientific equipment or for information concerning industrial, commercial or scientific experience but does not include any royalty or other amount paid in respect of literary or artistic copyrights or of motion picture films or of tapes for television or broadcasting or of the operations of a mine, oil well, quarry or other places of extraction of natural resources or of timber or forest produce.
3. Sums derived by a resident of one of the Contracting States from the other Contracting State the payment of which is approved after the signature of this Agreement by the Government of that other Contracting State, from the alienation of any right or property from which royalties (as defined in paragraph 2 of this article) are or may be derived, shall be exempt from tax in that other Contracting State.
4. The provisions of paragraphs 1 and 3 of this articles shall not apply if the recipient of the royalties, or sums, being a resident of one of the Contracting States, has in the other Contracting State from which the royalties or sums are derived a permanent establishment with which the rights or property giving rise to the royalties is effectively connected. In such a case, the provisions of article VII shall apply.