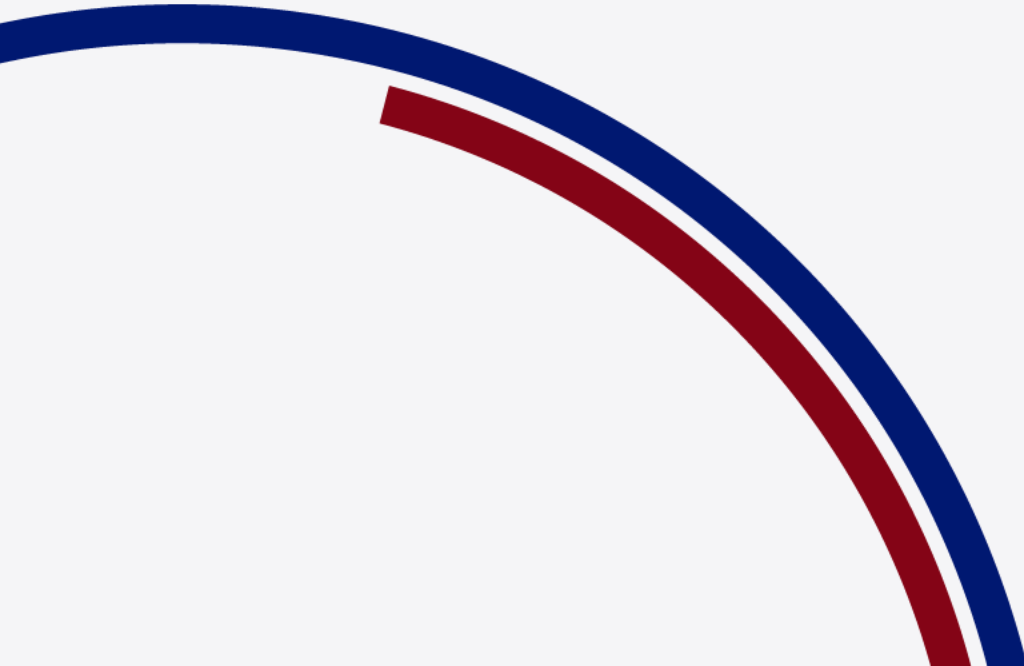


LEGAL UPDATES AND CASE LAW :
Latest Developments | 8 APRIL 2021
in Labuan IBFC | 4:00PM (GMT +8)



LEGAL UPDATES AND CASE LAW :
Latest Developments | 8 APRIL 2021
in Labuan IBFC | 4:00PM (GMT +8)



**Nabors Drilling (Labuan) Corp v Lembaga Perkhidmatan
Kewangan Labuan [2020]**

William Lim
Partner
Ariff Rozhan & Co

A NEW FIRM FOR THE 21ST CENTURY

LEGAL UPDATES AND CASE LAW: LATEST DEVELOPMENTS IN LABUAN IBFC

Nabors Drilling (Labuan) Corp v Lembaga Perkhidmatan Kewangan
Labuan [2020] 12 MLJ 54

PRESENTATION AGENDA

 Case Summary

 Court Proceedings

 Issues

 Arguments by Parties

 Court's Findings

 Key Takeaways

CASE SUMMARY



On 22.5.2012, the appellant, a Labuan licensed entity, leased an offshore oil rig drilling platform (“**Rig 503**”) to a Malaysian company resident in Labuan (“**subsequent leasing transaction**”), without obtaining Labuan FSA’s prior approval and without payment of the requisite fees.



Some 20 months later, on 24.1.2014, the appellant applied for the retrospective approval of the subsequent leasing transaction. However, the same was rejected by Labuan FSA.



Their action breached Item 8.2 of Labuan FSA’s ‘*Guidelines on the Establishment and Operation of Labuan Leasing Business 2013*’ (“**the Guidelines**”), which stipulates that subsequent leasing transactions with Malaysian residents are subject to Labuan FSA’s prior approval and payment of the requisite fees.

Court Proceedings

A R
& C

9.7.2015

After failing to obtain Labuan FSA's retrospective approval for the leasing of Rig 503, the appellant filed a judicial review application in the Labuan High Court on, *inter alia*, the grounds that (i) the Guidelines have no force of law and (ii) Item 8.2 of the Guidelines contradicts section 7(6) of the Labuan Companies Act 1990 ("**LCA 1990**"), and is therefore, ultra vires and unlawful.

10.10.2017

The High Court dismissed the judicial review application.

28.9.2018

The Court of Appeal upheld the High Court decision and dismissed the appellant's appeal in relation to the judicial review application.

2.10.2020

The Federal Court upheld the Court of Appeal decision and dismissed the appellant's appeal in relation to the judicial review application.

ISSUES

A **R**
& **C**



Whether the Guidelines carry the force of law?



Whether Item 8.2 of the Guidelines contradicts and is ultra vires Section 7(6) of the LCA 1990?



ARGUMENTS BY PARTIES (1)

A R
& C

APPELLANT

Section 4A of the Labuan Financial Services Authority Act 1996 (“**LFSAA 1996**”) merely allows Labuan FSA to issue guidelines to clarify provisions of Labuan Laws, and the Guidelines carry no force of law.

LABUAN FSA

1. The Guidelines was issued pursuant to the statutory powers conferred upon Labuan FSA by Parliament. It is a piece of subsidiary legislation, having legislative effect and the force of law.
2. In this regard, the powers conferred upon Labuan FSA are wide, and they include power to issue guidelines to facilitate compliance with the law, power to impose conditions and power to collect fees.
3. Section 4A of the LFSAA 1996:-
*“(1) The Authority may, in respect of this Act or the laws specified in the Schedule or any other matter relating to Labuan financial services, **issue guidelines to clarify any provision of this Act or the laws specified in the Schedule to facilitate compliance with the law by a Labuan financial institution or any other matters relating to Labuan financial services.**”*
4. Section 3 of the Interpretation Acts 1948 and 1967:-
"subsidiary legislation" means **any proclamation, rule, regulation, order, notification, by-law or other instrument made under any Act, Enactment, Ordinance or other lawful authority and having legislative effect**"

ARGUMENTS BY PARTIES (1) – cont.

A R
& C

LABUAN FSA

5. Section 40 of the Interpretation Acts 1948 and 1967:-

“Implied Powers

*(1) Where a written law confers a power on any person to do or enforce the doing of any act or thing, **all such powers shall be understood to be also given as are reasonably necessary to enable the person to do or enforce the doing of the act or thing.***

(2) Without prejudice to the generality of subsection (1)-

(a) power to make subsidiary legislation to control or regulate any matter includes power to provide for the same by licensing and power to prohibit acts whereby the control or regulation might be evaded;

*(b) power to grant a licence, permit, authority, approval or exemption **includes power to impose conditions** subject to which the licence, permit, authority, approval or exemption is granted...”*

ARGUMENTS BY PARTIES (2)

A R
& C

APPELLANT

1. The previous requirement that Labuan Company must obtain the permission of Labuan FSA before it can undertake any business with a Malaysian resident (previously appeared in Sections 7(1) & 7(3) of the Offshore Companies Act 1990, now LCA 1990), has been removed by Parliament in 2010 (via Offshore Companies (Amendment) Act 2010 – Act A1367).
2. Moreover, under the current Section 7(6) of the LCA 1990 (introduced via Act A1367), as long as a Labuan Company is licensed to conduct leasing business under the Labuan Financial Services and Securities Act 2010 (“**LFSSA 2010**”), it does not even need to notify Labuan FSA of its Labuan business activities with Malaysian resident, let alone obtaining approval from Labuan FSA for the same.

LABUAN FSA

1. Sections 7(1) & 7(3) of the Offshore Companies Act 1990 concern obtaining permission to transact with Malaysian resident. On the other hand, Item 8.2 of the Guidelines concerns approval to carry on leasing business and the payment of leasing fees. This is a licensing requirement. These are 2 different requirements.
2. Licensed activities conducted in Labuan, including Labuan leasing business, are now governed by the LFSSA 2010 (which was gazetted in 2010, the same time as Act A1367). Thus, Labuan Company carrying on licensed activity with a resident under the LFSSA 2010 is not required to notify Labuan FSA under the LCA 1990, given that the Labuan Company would have notified Labuan FSA of the same when applying for licence or approval under the LFSSA 2010 and/or its subsidiary legislation.
3. In this regard, the introduction of Section 7(6) of the LCA 1990 is to avoid duplicity in notification for the same licensed activity, and simplify the notification requirements.

ARGUMENTS BY PARTIES (2) – cont.

A R
& C

APPELLANT

3. Section 7(6) of the LCA 1990:-

“(6) Notwithstanding subsection (5), a Labuan company is not required to notify the Authority of transactions between the Labuan company and the resident where-

(a) the Labuan company carries on any licensed activity with a resident under the Labuan Financial Services and Securities Act 2010 or the Labuan Islamic Financial Services and Securities Act 2010...”

4. Thus, item 8.2 of the Guidelines (which stipulates that subsequent leasing transactions with Malaysian residents are subject to Labuan FSA’s prior approval) is ultra vires.

LABUAN FSA

4. Further, Section 7 of the LCA 1990 merely contains general provisions on the permitted purpose of a Labuan Company, including the notification of dealings with Malaysian resident under section 7(6) of the LCA 1990.

5. On the other hand, the LFSSA 2010 is a specific legislation that “provide for the licensing and regulation of financial services and securities in Labuan”, including the Labuan leasing business. Hence, it prevails over the general provisions of the LCA 1990.

6. In this regard, the LFSSA 2010 (read together with Labuan Financial Services and Securities Regulation 2010) provides that approval for all Labuan leasing transactions is required, be it with Malaysian resident or non-resident. Thus, item 8.2 of the Guidelines, which was issued to clarify and facilitate compliance with the provisions in the LFSSA 2010, is intra vires Labuan FSA’s powers and functions.

COURT'S FINDING

A R
& C

1

Guidelines issued by Labuan FSA have the force of law

The Federal Court held that Section 4A of the Labuan Financial Services Authority Act 1996 confers Labuan FSA with the power to issue guidelines which carry the force of law.

COURT'S FINDING

A R
& C

2

Labuan FSA's implied power under the Interpretation Acts

The Federal Court, after considering, amongst others, Section 40 of the Interpretation Acts 1948 and 1967, further held that Labuan FSA has the implied power to make subsidiary legislations or to impose conditions when granting a licence or approval.

COURT'S FINDING

A R
& C

3

'Generalibus specialia derogant'

Labuan Financial Services and Securities Act 2010, being a specific legislation governing Labuan licensed activities, prevails over the Labuan Companies Act 1990, which is general in nature.

KEY TAKEAWAYS

A R
& C

Prudent to comply with the relevant guidelines and conditions issued/imposed by Labuan FSA from time to time

Non-compliance may cause the Labuan company's business to fall outside the Labuan Business Activity Tax Act 1990



Non-compliance may expose the Labuan company and/or its officers to the risk of enforcement action by the authority.

A NEW FIRM FOR THE 21ST CENTURY

A R

& C

THANK YOU

www.arc.partners

LEGAL UPDATES AND CASE LAW : Latest Developments in Labuan IBFC

8 APRIL 2021
4:00PM (GMT +8)



Datuk Chin Chee Kee
Chairman
Association of Labuan Trust Companies (ALTC)

Farah Jaafar-Crossby
CEO
Labuan IBFC Inc.



William Lim
Partner
Ariff Rozhan & Co



Anil Kumar Puri
Partner, International Tax and Transaction Services
Ernst & Young Malaysia



PANEL DISCUSSION

LEGAL UPDATES AND CASE LAW :

**Latest Developments
in Labuan IBFC**

8 APRIL 2021
4:00PM (GMT +8)



Labuan Leasing Structures - Tax Implications And Considerations Arising From Nabors Case

Anil Kumar Puri

Partner, International Tax and Transaction Services
Ernst & Young Malaysia

An aerial night photograph of a city, likely London, showing a dense urban landscape with illuminated buildings and streets. A large yellow rectangular box is overlaid on the left side of the image, containing text. The city lights create a warm, golden glow against the dark night sky.

Labuan leasing structures - tax implications and considerations arising from Nabors case

8 April 2021

The EY logo, consisting of the letters 'EY' in a bold, white, sans-serif font. A yellow triangle is positioned above the 'Y'.

Building a better
working world

Panelist



Anil Kumar Puri

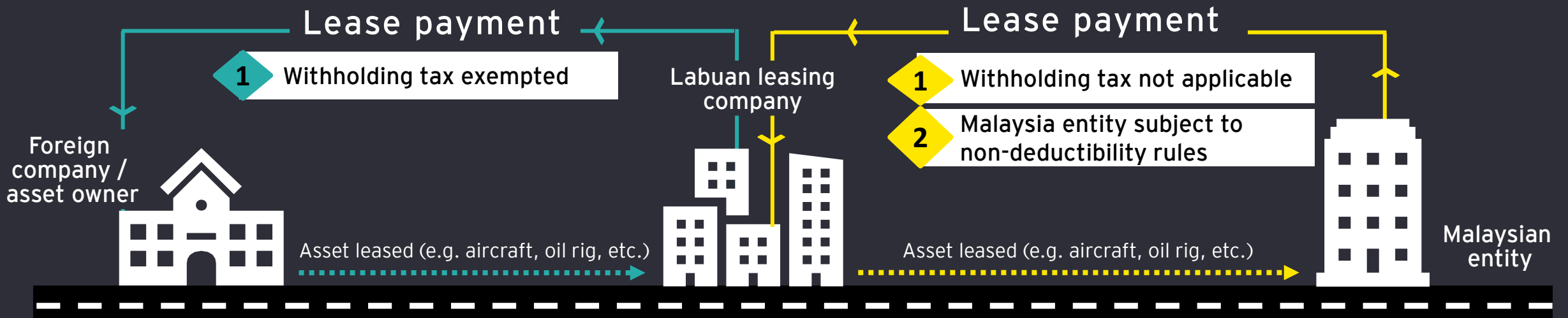
Partner, Ernst & Young Tax Consultants Sdn Bhd

anil-kumar.puri@my.ey.com

This material has been prepared for general informational and educational purposes only and is not intended, and should not be relied upon, as accounting, tax, legal or other professional advice. Please refer to your advisors for specific advice.

Neither the EY organization nor any of its member firm thereof shall bear any responsibility whatsoever for the content, accuracy, or security of any third-party websites that are either linked (by way of hyperlink or otherwise) or referred to in this presentation.

General tax implications of typical Labuan leasing structures under LBATA*



Tax considerations for Labuan leasing company

Must comply with Labuan Economic Substance Requirements

- ▶ Subject to **3%** tax on net audited profits
- ▶ Lease payment to non-residents **exempted from withholding tax**
- ▶ Lease agreements executed are **exempted from stamp duty**.

Where substance not met:

- ▶ Labuan leasing company subject to **24%** tax under LBATA*?
- ▶ Would **withholding tax and stamp duty exemptions** still apply?

Tax considerations for Malaysian entity

Non-deductibility rules

| | | |
|--|------------------|------------|
| | Interest payment | 25% |
| | Rental payment | 25% |
| | Other payments | 97% |

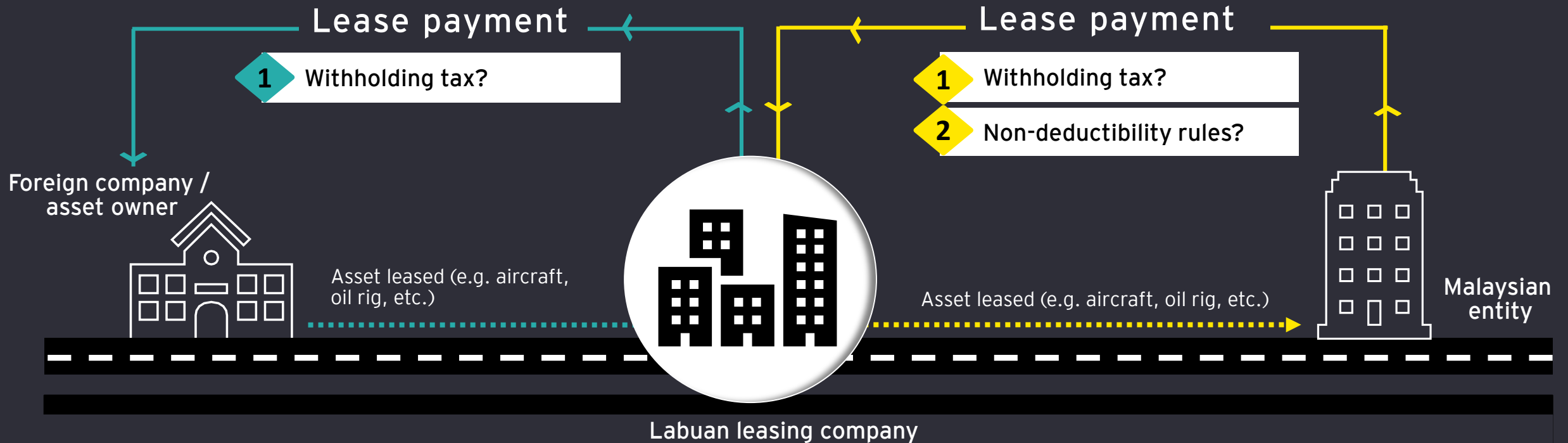
*Note: LBATA = Labuan Business Activity Tax Act 1990. The above implications would apply only where various conditions are met.

Impact of not obtaining LFSA's approval for subsequent leasing transaction

Extract from Nabors High Court decision

[6] However, the applicant entered into a subsequent leasing transaction (the Subsequent Leasing Transaction) with NMSB in respect of Rig 503 without the approval of the respondent and without paying any leasing fees under the LFSSR. The applicant belatedly applied for approval vide letter dated 28 October 2013 some twenty months later. The respondent rejected the application on 6th May 2014 and informed the applicant that the subsequent leasing transaction “should not be deemed as Labuan business activity and any income derived from the transaction should not be taxed under the Labuan Business Activity Tax Act 1990. Under the Labuan Business Activity Tax Act 1990 (LBATA), the applicant can avail tax benefits if a particular leasing transaction is deemed a “Labuan business activity”.

What if a Labuan leasing company is taxed under the ITA*?



- 1** Taxed at **24%** under the ITA
- 1a** Need to assess the deductibility of expenses
- 1b** Need to assess the availability of capital allowances
- 2** Availability of stamp duty and withholding tax exemptions? **?**

*Note: ITA = Income Tax Act 1967

Labuan Economic Substance Requirements

From 1 January 2019 onwards, Labuan leasing companies are required to comply with the Labuan Substance Regulations ¹.

| Labuan entity carrying on a Labuan business activity | Minimum number of full-time employees in Labuan ² | Minimum amount of annual operating expenditure in Labuan (RM) |
|-----------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------|
| (a) Not more than 10 related Labuan leasing companies or Labuan Islamic leasing companies | 2 for each group (as defined) of companies | |
| (b) 11 to 20 related Labuan leasing companies or Labuan Islamic leasing companies | 3 for each group of companies | |
| (c) 21 to 30 related Labuan leasing companies or Labuan Islamic leasing companies, or | 4 for each group of companies | |
| (d) More than 30 related Labuan leasing companies or Labuan Islamic leasing companies | 1 additional employee for each group of companies for each increase of 10 related Labuan leasing companies or Labuan Islamic leasing companies | 100,000 for <u>each</u> Labuan leasing company or Labuan Islamic leasing company |

Notes:

1. The Labuan Substance Regulations are the Labuan Business Activity Tax (Requirements for Labuan Business Activity) Regulations 2018, as amended by the Labuan Business Activity Tax (Requirements for Labuan Business Activity) 2018 (Amendment) Regulations 2020.
2. There needs to be at least one employee employed in a managerial capacity.

An aerial photograph of a dense urban landscape, likely Hong Kong, showing a vast number of high-rise buildings packed closely together. The buildings vary in height and color, with many in shades of beige and brown. There are patches of greenery and some lower-rise structures interspersed among the skyscrapers. The lighting suggests a late afternoon or early morning setting, with long shadows and a warm, golden glow.

Thank you!

EY | Building a better working world

EY exists to build a better working world, helping to create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation are available via ey.com/privacy. EY member firms do not practice law where prohibited by local laws. For more information about our organization, please visit ey.com.

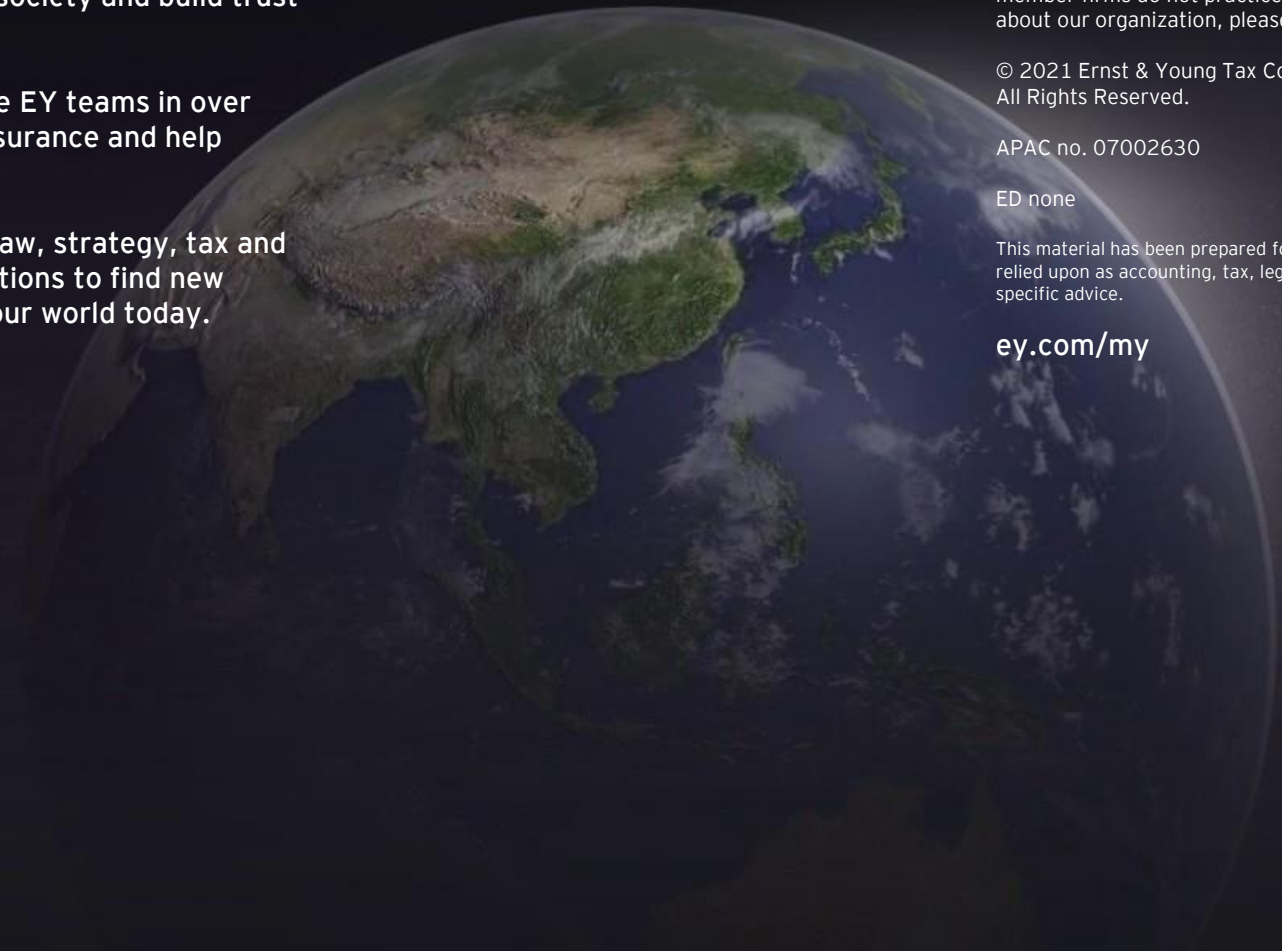
© 2021 Ernst & Young Tax Consultants Sdn Bhd
All Rights Reserved.

APAC no. 07002630

ED none

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, legal or other professional advice. Please refer to your advisors for specific advice.

ey.com/my



LEGAL UPDATES AND CASE LAW :
Latest Developments | **8 APRIL 2021**
in Labuan IBFC | **4:00PM (GMT +8)**

