

Intra-Group Management Fees: Making Fees Tax-Efficient and Audit-Ready



Key Takeaway

- ❖ For a management fee to qualify for deduction, businesses should be able to demonstrate the actual services provided, the business purpose of the expenditure, the benefit obtained and the basis for the amount charged.

Management fees are a common feature of businesses operating within a group structure. Centralised functions such as finance, human resources, information technology, administration and strategic management are often provided by a related company in return for a management fee.

While such arrangements may be commercially reasonable, the tax deductibility of management fees depends on whether the expenditure satisfies the requirements of Section 33(1) of the Income Tax Act 1967. A recent Malaysian tax case involving management fees highlights the importance of having sufficient evidence to support both the nature of the services provided and the commercial purpose of the expenditure.

THE TAX ISSUE

Section 33(1) generally allows a deduction for expenses wholly and exclusively incurred in the production of gross income.

For management fees, the key question is therefore not simply whether a company has incurred a payment. The taxpayer should be able to demonstrate that:

- the services were actually provided;
- the services were relevant to the taxpayer's business;
- the expenditure was incurred for the purpose of generating business income; and
- the amount charged can be properly substantiated.



SUBSTANCE OVER DOCUMENTATION

For related-party arrangements, taxpayers should maintain evidence demonstrating the actual activities undertaken. Depending on the nature of the services, this could include:

- service agreements and statements of work;
- invoices containing meaningful descriptions of services;
- management reports;
- emails and correspondence;
- meeting minutes;
- employee or personnel records;
- work schedules and deliverables;
- IT support records;
- accounting or financial reports; and
- other documentation demonstrating the benefit received.
- other income of an income nature.

The stronger the connection between the supporting documentation and the services actually received, the easier it is to demonstrate the commercial substance of the arrangement.

INCREASING MANAGEMENT FEES

Particular attention should also be given where management fees increase significantly from one year to another. An increase in charges should be supported by a reasonable commercial explanation, such as:

- an expansion of business operations;
- additional services;
- increased personnel costs;
- greater use of shared resources;
- changes in the allocation methodology; or
- other identifiable changes in the underlying services.

Where management fees increase significantly, taxpayers should retain contemporaneous documentation to substantiate the increase, including evidence of any corresponding changes in the scope or value of services and the basis for the fees charged.

RELATED-PARTY ARRANGEMENTS REQUIRE GREATER CARE

Management fees paid to related companies can attract greater scrutiny because the parties are not independent from each other. Businesses should therefore consider whether the arrangement would be commercially supportable if reviewed by an independent party.

PRACTICAL CONSIDERATIONS FOR BUSINESSES

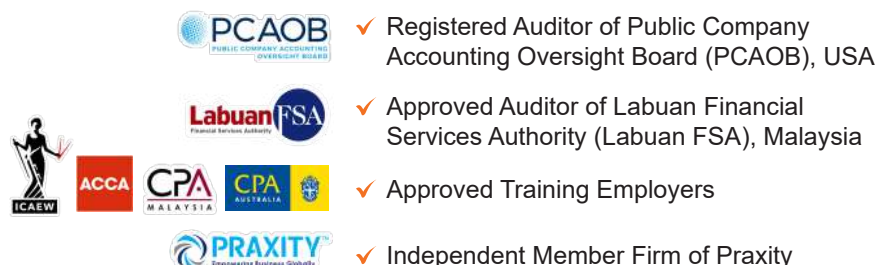
Businesses with intra-group management fee arrangements should consider reviewing their existing documentation and processes. In particular, taxpayers should ensure that the contractual terms accurately reflect the services actually provided

For more details, please refer to :

Inland Revenue Board of Malaysia ("IRBM"), Tax Cases, MSSB v Ketua Pengarah Hasil Dalam Negeri, High Court of Malaya, Civil Appeal No. WA-14-11-04/2021, judgment dated 24 November 2022.



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