

## **PRACTICE NOTE NO. 3/2023**

### **TAX TREATMENT ON COPYRIGHT AND SOFTWARE PAYMENTS BY A DISTRIBUTOR AND A RESELLER TO A NON-RESIDENT**

1. This Practice Note is issued to provide clarification relating to the tax treatment on copyright and software payments by a distributor and a reseller to a non-resident.
2. The tax treatment in relation to copyright and software payments by a distributor and a reseller to a non-resident depends on the facts of each case.
3. The definition of royalty refers to the provisions of subsection 2(1) of the Income Tax Act 1967 (ITA), while the tax deduction for royalty payments refers to section 109 of the ITA.
4. Copyright and software payments are considered as royalties because they are payments for the use or right to use of copyright and software in which the intellectual property of the software is still owned by the original owner of that copyright and software.
5. The purchase of software or the use of applications (Apps) and content by distributor and reseller from the original owner regardless of whether the software can be modified, exploited or distributed is considered as royalty.

#### Example 1:

Company A operates a business of buying computer software and reselling it to customers. Company A buys the computer software from Company B, which is not resident in Malaysia and is the owner of the copyright and software. Company A is granted the right to make copies, distribute, modify, reproduce copies, or license the software. Company A is also allowed to manage the master file of the software owned by Company B.

Company A then sells the software to customers in Malaysia. Company A will receive an activation key from Company B and provide it to the customer, allowing them to access the software that has been downloaded from Company B's server. The payment for the software purchases made by Company A to Company B is considered as royalty and is subject to withholding tax payment under section 109 of the ITA.

Example 2:

The facts are the same as in Example 1 where Company A is granted the right to distribute the software but does not have the right to make copies, modify, reproduce copies or license the software. In this situation, the payment made by Company A to Company B is also considered as royalty and is subject to withholding tax payment under section 109 of the ITA as the intellectual property of the software still belongs to Company B.

6. Payments for software made to a non-resident who does not have a permanent establishment or place of business in Malaysia, are considered as royalty and will be subject to withholding tax under section 109 of the ITA.
  
7. In the context of a Double Taxation Avoidance Agreement (DTA), the definition of royalty and permanent establishment may differ. Therefore, reference should be made to the DTA of the respective contracting countries.

**Director General of Inland Revenue  
Inland Revenue Board of Malaysia**

**DATE OF PUBLICATION: 5 DECEMBER 2023**