Malaysia

Malaysia Transfer Pricing Guidelines on Intra-Group Loans: The IRB Looks Beyond the Interest Rate



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Executive Summary

On 30 July 2026, the Inland Revenue Board of Malaysia ("IRB") issued the Malaysia Transfer Pricing Guidelines – Controlled Financial Transactions: Intra-Group Loans ("Guidelines"). The Guidelines supplement Chapter 9 of the Malaysia Transfer Pricing Guidelines 2024 and explain the IRB's approach to the characterisation, pricing and documentation of intra-group loans.

Although much of the guidance draws upon established transfer pricing principles, its significance should not be understated. The IRB is no longer concerned only with whether the interest rate is comparable with market rates. It may first examine whether the financing should be recognised as a loan at all.

A Loan Agreement Is Only The Starting Point

An arrangement described and recorded as a loan will not necessarily be accepted as debt for transfer pricing purposes. The IRB will consider its economic substance, the conduct of the parties and whether independent parties would have entered the arrangement under comparable circumstances.

Relevant considerations include:

- whether there is a genuine and enforceable obligation to repay;
- whether the loan has a fixed maturity date and repayment schedule;
- whether interest is payable regardless of the borrower's profitability;
- the lender's rights upon default or liquidation;
- whether the lender participates in the borrower's management;
- the accounting and tax treatment adopted; and
- the actual intention and conduct of the parties.

No single factor is decisive. A formal agreement stated interest rate and repayment date will not, by themselves, establish that the funding is genuinely debt.

This is particularly relevant to long-outstanding balances, repeatedly renewed loans, interest-free advances and funding provided to entities that have no realistic means of repayment.



Photo by Liz Yang

The Borrower's Capacity To Borrow Matters

Even where an arrangement has the legal characteristics of a loan, the IRB may ask whether an independent lender would have advanced the amount concerned.

The assessment must therefore consider the borrowers:

- purpose for obtaining the financing;
- projected cash flows and source of repayment;
- existing indebtedness and capital structure;
- financial performance and creditworthiness;
- availability of security;
- currency and interest-rate exposures; and
- other financing options realistically available.

The commercial position of both parties must be considered. An independent lender would evaluate the risk and expected return, while an independent borrower would generally seek the least costly financing that satisfies its commercial requirements.

A group should therefore be able to explain not only how the interest rate was determined, but also why the amount, tenure, security and other conditions of the loan make commercial sense.

Risk of Recharacterisation As Equity

The Guidelines state that the IRB may invoke subsection 140A(3A) of the Income Tax Act 1967 to disregard or recharacterise a purported loan where its substance differs from its form, or where the arrangement differs from one that commercially rational independent parties would have adopted.

If a loan is recharacterised as equity, the borrower may lose the corresponding interest deduction. Transfer pricing adjustments may also attract a surcharge.

This is arguably the most important aspect of the Guidelines. Applying a benchmarked interest rate will not, by itself, make a commercially unrealistic loan acceptable for transfer pricing purposes.

The Guidelines, however, provide only a limited illustration of recharacterisation. They do not explain clearly whether the IRB would recharacterise an entire loan or only the portion exceeding the borrower's arm's length borrowing capacity. In practice, this distinction could be material and should depend on the particular facts and the proper application of subsection 140A(3A).



Credit Rating and Implicit Group Support

Creditworthiness is central to determining an arm's length interest rate. The analysis may involve an independent credit rating, a rating derived from financial and qualitative data, or an assessment based on recognised rating methodologies.

The Guidelines appropriately recognise that a subsidiary's creditworthiness may be enhanced by its membership of a multinational group. This "implicit support" may justify a rating above the subsidiary's stand-alone rating, particularly where the subsidiary is strategically important, operationally integrated or closely associated with the group's reputation.

No separate payment is required for implicit support because the benefit arises from group membership rather than a specific service or legally enforceable guarantee.

Businesses should nevertheless avoid automatically applying either the parent's rating or the subsidiary's stand-alone rating. The degree of expected group support should be evaluated and documented.



Determining The Interest Rate

The Guidelines favour the Comparable Uncontrolled Price ("CUP") method where sufficiently comparable market information is available. Relevant comparisons may include:

- the taxpayer's or group's specific third-party borrowings;
- loans involving borrowers with comparable credit ratings;
- bond issuances;
- commercial paper;
- deposits; and
- other comparable financial instruments.

The group's average borrowing cost will generally not constitute a reliable internal comparable because it may combine borrowings with different currencies, maturities, security and credit characteristics.

Where reliable comparables are unavailable, the cost of funds method may be used. However, the lender's cost cannot be considered in isolation. The resulting rate must be tested against market conditions and the borrower's alternative sources of finance.

Where a group financing entity merely passes externally borrowed funds to another group company and performs only an intermediary function, it should not automatically earn a full financing return. Its remuneration should reflect the functions performed and risks genuinely controlled.

Similarly, arrangement and commitment fees should not be imposed merely because banks commonly charge them. A related lender should be compensated only for activities performed, costs incurred and risks assumed.

The Simplified Method

The Guidelines introduce two designated rates based on rates published by Bank Negara Malaysia:

- the deposit rate; and
- the average lending rate ("ALR").

The deposit rate may generally be elected for qualifying domestic intra-group loans funded from the taxpayer's internal funds, provided, among other conditions, that the loans are denominated in Ringgit Malaysia and the aggregate amount does not exceed RM50 million.

The ALR may generally be used for qualifying cross-border intra-group loans denominated in Ringgit Malaysia where the aggregate amount does not exceed RM50 million.

The simplified method is unavailable where funds are borrowed by one group entity and passed to the ultimate borrower. Taxpayers must also retain evidence that all eligibility conditions are satisfied.

The simplification is welcome, especially for smaller taxpayers. Nevertheless, several practical questions remain:

- whether the RM50 million threshold refers to the closing balance, highest balance or total advances during the year;
- which month's published rate should apply;
- how the rate should be applied to loans drawn or repaid during the year;
- whether the election must be applied consistently to all qualifying loans; and
- the precise operation of the ALR for different types of cross-border arrangements.

The eligibility conditions are also framed principally from the lender's perspective because the interest income must be taxable under paragraph 4(c). Accordingly, the simplified method should not be assumed to cover every inbound or outbound intra-group loan.


Photo by Sanjai Sudheesh

Documentation Remains Necessary

An exemption from preparing full contemporaneous transfer pricing documentation does not exempt a taxpayer from the arm's length principle.

Taxpayers should retain:

- executed loan agreements;
- the commercial purpose for the financing;
- evidence of the borrower's borrowing requirement;
- cash-flow forecasts and repayment capacity;
- credit-rating or creditworthiness analysis;
- details of security, guarantees and covenants;
- the pricing methodology and comparable transactions;
- evidence supporting eligibility for the simplified method; and
- records showing that the parties acted consistently with the agreement.

Where contemporaneous transfer pricing documentation is required, it must be submitted within 14 days of a written request from the IRB. Relevant records must generally be retained for seven years.

The Guidelines also indicate that existing intra-group loan arrangements should be reviewed regularly. This is important because many group balances originate from informal advances, settlement of expenses or cash movements and were never supported by a proper financing analysis.

Our Observations

The Guidelines bring useful discipline to intra-group financing, particularly by emphasising repayment capacity, creditworthiness and commercial rationality. They also provide a practical simplified method for certain smaller Ringgit-denominated loans.

However, the Guidelines leave several areas requiring clarifications.

First, they do not state a specific effective date or provide transitional treatment for existing loans, although taxpayers are expected to review existing arrangements. It would be helpful for the IRB to clarify how the Guidelines apply to loans entered before 30 July 2026.

Secondly, the debt-versus-equity analysis is necessarily judgmental. The Guidelines provide no financial ratio or objective threshold for determining an acceptable level of debt. This may give rise to different interpretations during an audit.

Thirdly, the simplified method reduces benchmarking work but does not dispense with the need to establish that the arrangement is genuinely a loan. A designated rate cannot protect funding that lacks commercial substance or a realistic prospect of repayment.

Finally, an arm's length interest rate does not, by itself, secure an interest deduction. Deductibility remains subject to the general provisions governing interest expenses and the interest restriction rules under section 140C.



What Businesses Should Do Now

Businesses should identify all intra-group loans, advances and long-outstanding related-party balances and review them before the next tax filing or transfer pricing documentation cycle.

The review should proceed in the following order:

1. determine whether the balance is genuinely debt or is, in substance, capital;
2. assess the borrower's ability to obtain and repay the financing;
3. confirm that the contractual terms reflect the parties' actual conduct;
4. evaluate the borrower's creditworthiness and the effect of implicit group support;
5. determine whether the simplified method is available; and
6. where it is not, prepare an appropriate benchmarking or cost-of-funds analysis.

The practical message is straightforward: documenting an interest rate is no longer sufficient. Businesses must be prepared to defend the commercial basis of the financing itself.

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