

# BizDO

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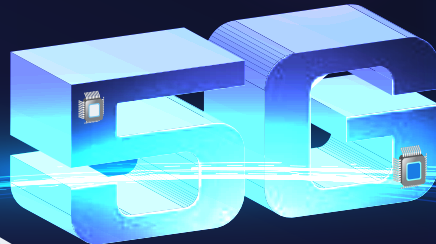
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# AUDIT & ASSURANCE

## BIG DATA AND DATA ANALYTICS: THE FUTURE OF AUDIT

By Rejeesh Balasubramaniam & Sanjay Sidhu

### INTRODUCTION

During the past decade, the tech world has been unceasingly introducing new technologies at a pace faster than any of us has experienced before. It is undeniable that these new and improved technologies have also led to the introduction of more complex systems and processes which are usually described using simple buzzwords for convenience of communication.

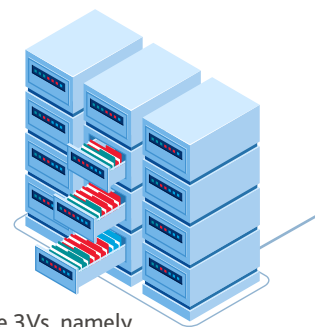


Despite the fact that such complex systems and processes might seem overwhelming to many, a wide range of professions are embracing and striving to tap into such technologies either to improve the efficiency and effectiveness of their services, or in response to pressure to remain relevant in this rapidly changing environment. The COVID-19 pandemic has also triggered an increased demand for these technologies.

Among the plethora of new technological advancements introduced, buzzwords like big data, data analytics and artificial intelligence have captivated the interest of the accounting profession. This interest arises mainly due to the expected opportunity for this technology to open doors to new opportunities never encountered before and the potential for it to revolutionise the way things are done within the accounting profession.

### WHAT IS "BIG DATA"?

Big Data is a term used to refer to extremely large data sets that may be analysed using technology to reveal patterns, trends and associations. It may also be argued that the term Big Data refers to data sets so large and complex that traditional data-processing software applications are not sufficient to deal with them. The key fact to keep in mind is that the concept is still continually evolving as digital transformation and reliance marches onward.



Evolution aside, a constant definition of Big Data comes in the form of the 3Vs, namely Volume, Velocity and Variety. These may be briefly defined as laid out below.



#### Volume

Volume is the V most easily associated with Big Data. When it comes to Big Data, we are talking about quantities of data that reach proportions so immense as to be incomprehensible. A good example of this is Facebook as at the end of 2016, Facebook stored approximately 250 billion images and contained 2.5 trillion posts. Now factor in the Internet of Things ("IoT") — imagine a connected temperature sensor; at a measurement rate of once a minute, that is 525,600 records per year. Now consider how many heat sensors there may be at an oil refinery or a palm oil mill. That's volume.



#### Velocity

Velocity is, quite simply, speed. In the Big Data context, this is a reference to the speed at which data is created, and therefore the speed at which it must be processed and stored in a manner in which it can be easily retrieved and viewed when needed. The developments in connectivity bandwidth, smartphones, cloud computing and the IoT have driven growth at this speed. Go back to our example of temperature sensors at a refinery and imagine now that each sensor is taking a reading every 30 seconds, or every 15 seconds. The speed of receiving, categorising, storing, retrieving and analysing the data must be on par with the speed of creation of the data.



#### Variety

The massive volume and sources of data to which we have referred to above would also mean that such data is likely to be created in a wide variety of types and formats. The data would now be a combination of structured data and unstructured data.

Structured data is information that is stored within defined fields or formats and is organised, processed and accessed in an orderly manner based on a predefined data model. Traditional databases, excel sheets, etc., all fall into this category.

Unstructured data is not necessarily stored in fields or defined formats based on a pre-defined data-model. Photographs, video, Twitter feeds, online chats, voice recordings, etc., are examples of commonly encountered unstructured data.

# AUDIT & ASSURANCE

## BIG DATA AND DATA ANALYTICS: THE FUTURE OF AUDIT

(continued)

### CHALLENGES OF BIG DATA

#### a Cost

Significant investments are required to be committed to acquiring, upgrading and customising the hardware and software capable of handling Big Data. Additional costs would also be required in recruiting and training human resources to bridge the talent gap in Big Data handling and analysis.

#### b Regulation

Organisations will require enhanced policies and controls over the collection, categorisation, storage and usage of data. These processes will not only need to be in compliance with the relevant regulations passed by the regulatory authorities, but may necessarily need to be ahead of the learning curve of the various regulatory bodies' own knowledge. Non-compliance such regulations could have serious reputational and punitive consequences to an organisation.

#### c Data security

The immense amount of data stored within an organisation could represent a digital treasure chest of confidential, personal and proprietary knowledge. This will attract potential security breaches driven by a range of motivations. In addition to the potential loss of business that could come from the loss or exposure of this data, civil legal action and regulatory sanctions may also be suffered as the result of data breach.



### DATA ANALYTICS

Data analytics refers to the process of analysing and examining data to identify trends and new insights as well as drawing conclusions that can help organisations make informed business decisions. Analytics as a concept is not at all new — analytic tools have been in regular use in business since the mid-1950s.

The main characteristics that set big data analytics apart from traditional basic analytics are speed, efficiency and integration of multiple data types. Major leaps in technological advancement in the past decade have enabled organisations to process data much more efficiently and faster by leveraging specialised

analytics systems and software to perform the data processing. Organisations can now gather information, run analytics and draw observations and conclusions in a real-time or near real-time manner, and from combinations of data sources, enabling them to make informed decisions and take a competitive edge they never had before.

Data analytics usually involves several types of technology being applied together in order to harness the most value from the data provided, which includes the following examples:

#### a Data management

Process of acquiring, organising, validating, securing, and processing data to ensure that such required data are accessible, reliable (meeting the required standards for data quality), and timely.

#### b Data mining

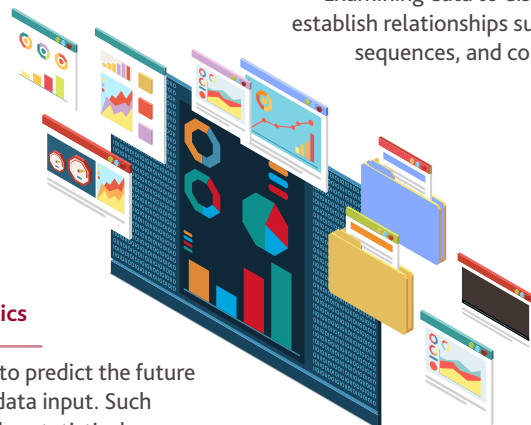
Examining data to discover patterns and establish relationships such as connections, sequences, and correlations between several events.

#### c Predictive analytics

Analytics which aims to predict the future outcomes of a set of data input. Such analytics usually involve statistical algorithms techniques and machine learning technologies that predict the likelihood of future outcomes based on historical trends and outcomes.

#### d Text analytics

Analysing text data by combing through text from websites, emails, books, documents, social media and other text based sources to gain useful insights for the user with the aid of machine learning and natural language processing technology.



# AUDIT & ASSURANCE

## BIG DATA AND DATA ANALYTICS: THE FUTURE OF AUDIT

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### DATA ANALYTICS IN AUDITING

Auditing has often been referred to as a "grey profession", a profession steeped in standards, tradition and methodology. With all the development going on around us, the primary role of the auditor remains unchanged - to act as an independent party where robust audits are to be performed to serve the public interest by enhancing the credibility of the financial information presented to stakeholders.

Auditors have been performing early versions of analytics all along, through the concepts of high level analytical review, detailed analytical review and corroborative review. The advent of new technologies, systems and processes has, in effect, given auditors access to information, analytical power and processing power at a level never before experienced and therefore, quite possibly never before considered or imagined in relation to its impact on the practice of auditing. So, although the primary role of auditors has not changed, the way audits are done will continue to transform to ensure that the highest quality of audit evidence amid the rapidly changing and increasingly demanding business environment.

While the profession has long recognised the impact of data analytics on enhancing the quality and relevance of the audit, widespread use of this technique has been hampered due to a lack of efficient and economically feasible technology solutions as well as talent gaps in data analytics. However, recent technology advancements in data analytics and machine learning are providing a promising opportunity to relook the way in which an audit is executed.

The key aspects of integrating data analytics into an audit is to facilitate auditors to better understand the business, identify key audit risk areas and deliver enhanced quality and coverage while providing more business value.

Data analytics are commonly used in an audit to identify key audit risk areas and even identify potential red flags through analysing patterns and relationships between multiple sets of data in a client's business. The multiple sets of data used for the analysis are not only restricted to data from the financial reporting system (i.e. general ledger, sales ledger, accounts receivables and payables ledger), but can also span data from other sources such as sales statistical data, customer/vendor master data, employee master data, and financial/non-financial budgets. By better understanding the factors and drivers affecting the specific areas of the client's business, auditors are now able to identify key audit risk areas in a more effective and precise manner. Simultaneously, the findings which auditors can provide by interpreting data using data analytics will help improve their dialogue with clients at all stages of the audit.

The use of data analytics expands the audit beyond traditional sample based testing, to include analysis of entire populations of audit-relevant data, hence enhancing the quality and coverage of audit evidence. There are already existing analytic tools like IDEA and ACL that can perform a variety of analyses, based on the parameters designed by the auditors, and then provide lists of exceptions for the auditor to evaluate. Yet, it is machine-learning technology that will bring data analytics to a whole new level. Data analytics augmented with machine learning technology is able to learn based on the auditor's previous conclusions pertaining to the results of the analysis; such as whether the exceptions identified are genuine or false positives. Hence, for this instance, the more conclusions the machine learns from the auditor, the better it is in identifying the exceptions.

Nevertheless, the risk in this manner of application, often referred to as data bias risk, is that the machine learns from the previous conclusions made by the auditor, irrespective of whether the conclusions made by the auditor are correct or incorrect. In this case, the machine would start to clear certain items that should be exceptions or vice versa. Therefore, it is imperative to put in place a robust review process to ensure that conclusions being fed into the machine learning are correct and accurate.

In more advanced applications, a set of transactions are input into a data analytic tool with machine learning technology to identify the patterns in the transactions and be able to identify a specific norm of the transactions. Subsequently, the tool can then be used on other sets of transactions with similar nature to identify transactions that don't match the specific norm as exceptions. This application of machine learning is also subject to data bias since the specific norm is determined based on the set of data provided. For instance, if the data set that was used to determine the specific norm consists of a high quantity of incorrect transactions, then such incorrect transactions would be deemed as within the specific norm and hence would not be identified as exceptions.

Currently, many audit firms are already delivering audit analytics by extracting large amounts of client data and subsequently analysing the data on separate machines with dedicated audit analytics software. While these analytics are often performed in the audit firm's environment, the next major leap for data analytics in future audits, with the help of artificial intelligence and machine learning technology, is for audit firms to be able to install intelligent audit analytic software that resides within their clients' data centres and stream the analytical results to the audit teams real-time, facilitating continuous auditing.

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(continued)

Businesses are already beginning to expect auditors to deliver more insights and value to the business as part of the audit, through the use of technology and innovation. The use of data analytics and machine learning will definitely be the key solution for the audit profession to provide more value to clients. As mentioned above, through the use of data analytics and machine learning, auditors are able to highlight not only financial reporting matters but also other value-adding findings as part of the overall audit findings, which clients were not previously aware of; such as the relationship between certain factors and the business performance, significant drivers affecting the business performance, key business risks and red flags to fraudulent activities.

The auditor's role will switch from performance of administrative procedures to the design of procedures, interpretation of the results generated through analytics, and exercising professional judgement on conclusions based on these interpretations.

The transition to this future would not be achieved overnight, as after all, it would be a massive leap for the profession to transform from traditional audit approaches to one that fully integrates data analytics and artificial intelligence in a seamless manner.

### WHAT ARE THE CHALLENGES?

The transition to an integrated audit with data analytics and artificial intelligence will not be without challenges. There are a number of barriers that must be addressed beforehand.

#### **a** Data extraction

In order for auditors to perform analytics in an audit, auditors must first be able to extract their clients' data efficiently and cost-effectively.

However, it has been increasingly essential for organisations to invest significantly in data security amid the various data breach scandals occurring lately. Organisations are required to protect their data, usually with multi-layered approval processes and technology safeguards. As a result, the process of obtaining client approval for the provision of data to the auditors can be difficult and time-consuming. In the 3V world, auditors (and their clients) are also going to need to transition from extracting and taking away data to simply being given extensive access to data warehouses on-site.

#### **b** Wide array of accounting systems

The wide array of accounting systems often encountered by auditors within their portfolio of clients and, in many cases, multiple accounting systems within the same company can be overwhelming in terms of extraction of data.

Extracting data from unfamiliar accounting systems could prove to be a painstaking process. This results in multiple attempts and a lot of back and forth between the company and the auditor on data capture.

Currently, the extraction of data is often limited to accounting ledger data. However, exploiting Big Data to support the audit will mean obtaining both structured and unstructured data, financial and non-financial. This increases the complexity of data extraction and data mapping.

#### **c** Skills gap

Integrating data analytics and artificial intelligence into an audit will only be meaningful when it influences the nature, scope, and extent of the audit. This will require auditors to develop new skills focused on knowing what questions to ask of the data, and the ability to use the outputs from analytics to produce audit evidence, draw audit conclusions and derive meaningful business insights.

A ground-up initiative to better understand and influence the education programs in universities and colleges, enhancing learning and development programs within the audit firm, and establishing the appropriate implementation programs to support audit teams will be required to effectively integrate data analytics and artificial intelligence into the audit.

#### **d** Aligning with auditing standards and regulations

The auditing profession is currently governed by standards and regulations that were formulated well before the advent of Big Data. Although there are continuous efforts made to maintain the relevance of the standards and regulations through amendments and introduction of new standards, standard setters, like all of us, are effectively playing catch-up in understanding and considering the relevant factors and feedback from various stakeholders before the auditing standards and regulations can be truly be aligned with the use of data analytics and artificial intelligence. Major areas that need to be addressed are as follows:

#### **i** Validation of data

As part of the audit procedures in an audit, auditors are required to determine the clerical accuracy and completeness of information or system-generated reports provided by the client and whether it is appropriate to be relied on, before performing further audit procedures on such information and reports.

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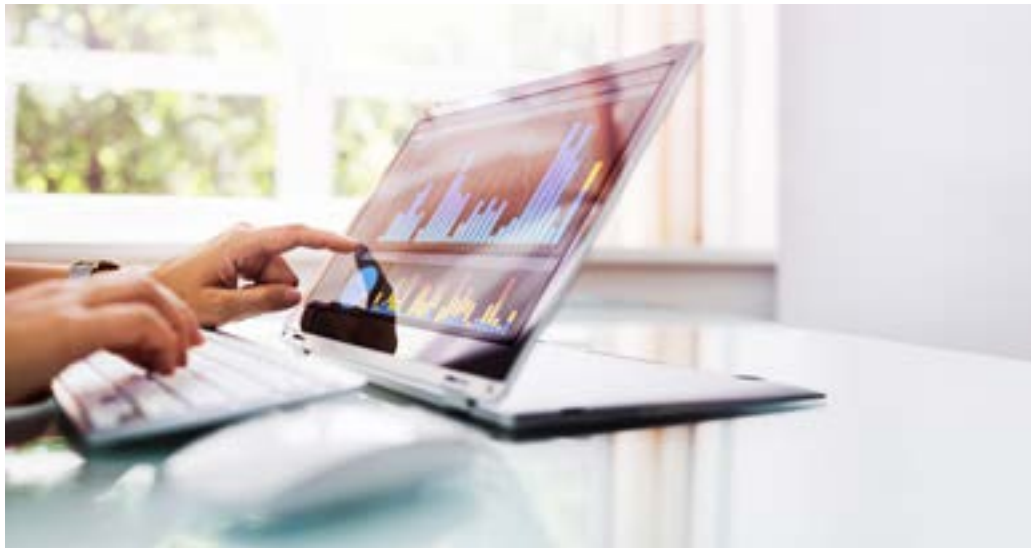
But Big Data related audit analytics rely on the raw transaction data being extracted directly from the underlying databases, as well as unstructured data from other sources. Procedures are then required to be performed to validate the accuracy and completeness of the data, and then reconciled to the system generated reports given to auditors to ensure that the audit analysis is based on the same data the company uses to produce its financial information. Having said that, there are limitations in the extent to which auditors can perform these procedures on such data due to the complexity and volume of data involved, especially in a Big Data environment.

### ii Hierarchy of audit evidence

The standards provide a hierarchy of evidence, with third-party evidence at the top and management inquiries at the bottom. However, the standards do not indicate what type of evidence analytics provides. It is possible to relate some of these types of tests to the current framework in the standards, but not all. Without a proper description of the type of evidence that analytics provides, auditors are reluctant to claim it as evidence, thus potentially negating the benefits.

### iii Audit Regulators

The use of data analytics in audits could raise concerns among standard setters on the approach for audit regulators to assess the integrity of the data analytic tools used by auditors and whether they are functioning as intended. Auditors often use data analytic tools endorsed by their audit firm to ensure the tools' reliability and effectiveness. However, the programming scripts driving the functioning of the more advanced and complex data analytic tools are usually not maintained in the audit file and hence are not available for regulators to review. Although details of the underlying programming scripts and the parameters



can be documented in the audit file to a certain extent, such data analytic tools are often operated globally and might be maintained outside the geographic jurisdiction of the local audit regulators. In short, auditors will need to adopt a standard approach to ensuring and demonstrating the integrity of the data analytic tools used.

### CONCLUSION

We delved earlier into the 3Vs of Big Data, but there is arguably a 4th and 5th "V" that needs to be considered.

The first of these is Value, which is increasingly referred to as the most important aspect of Big Data. The ability to turn the investment in technology to collect and process Big Data into valuable knowledge and insight in return is key to businesses. It follows from this that the application of traditional audit skills to the new technologies should and would generate the types of insights that achieve just this objective.

The final V is Veracity — the correctness and reliability of the data. Again, the knowledge of and skills of the auditor can and must be brought to bear in this area not only for the auditor to be able to rely on the data, but

also to provide the assurance to their clients that they have a level of filtering, checking and accuracy in the data introduced into their systems.

Ultimately, although the primary role of auditors will not change, the way audit is performed in the future will be significantly different from the audit of today, and the subject matter on which those audits are performed will evolve. Auditors will be able to use larger data sets and analytics to better understand the business, identify key risk areas and deliver enhanced quality and coverage while providing more business value. But to achieve this transformation, the profession will need to work closely with key stakeholders, from the businesses they are auditing to the regulators and standard-setters.

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# ADVISORY

## AN ACCOUNTANT'S GUIDE TO CRYPTOCURRENCY

Compiled by Pam Lee Wen Ai

### WHAT IS "CRYPTOCURRENCY"?

Cryptocurrency is a type of digital asset that is an intangible, digital currency that uses a highly sophisticated type of encryption called cryptography to secure and verify transactions as well as to control the creation of new units of currency. It is designed to work as a decentralized medium of exchange, independent of a financial institution or any other central authority. While Bitcoin is the most well-known cryptocurrency, it is not the only one. Other major types of cryptocurrencies include Ethereum, Ripple, Bitcoin Cash and LiteCoin. There are also other digital assets (or "cryptoassets").

These are commonly referred to as digital tokens. For example, a company can initiate a "token sale" or a "token launch" which is otherwise frequently referred to as an initial coin offering (ICO). In an ICO, a company is creating a new product and wants to build a user base who will benefit from purchasing the product early. The ICO also enables the company to raise proceeds to develop the product. It is attractive to companies because they can bypass the rigorous and regulated capital-raising process required by venture capitalists or banks. While this FAQ does not further explore ICOs or tokens, entities are encouraged to consult with their legal, accounting and tax advisors given the complexities and significant debate by regulators around such digital assets.

(Source: Cryptocurrency: The Tops Things You Need To Know, published by BDO USA, LLP)

#### HOW DOES IT WORK?

Say you want to buy a Lamborghini (fun fact: Lamborghini officially accepts bitcoin as payment!) - you go to the dealership and say you want to make the purchase. They would say that it's going to cost you 10,000 bitcoin (based on whatever the spot rate is on the day; the spot rate is dictated by just normal supply and demand economic principles).



At that point, you would transfer the amount of bitcoin required to settle the transaction. What happens next, is that the transaction gets recorded on an open ledger (open: because anyone can view it and is not editable). Bitcoin therefore allows for a transfer of value from one party to another without having to go through a centralised trusted third party provider and represents the first digital transfer of value from one party to another without going through a centralised third party (e.g. bank).

(Source: Financial Evolution: The new world of Crypto, published by BDO South Africa)

#### HOW ARE CRYPTOCURRENCY CREATED?

The process of creating a new type of cryptocurrency coins requires either building a new blockchain or modifying an existing process to create a new variant, or "fork." The majority of these so-called "altcoins" are forks of the Bitcoin protocol.



The only way more coins of an existing crypto coin can be created is through a process called "mining" in which the miner is awarded a transaction fee (a new coin) in exchange for contributing to the underlying blockchain algorithm by being the first to solve a cryptographic puzzle. Mining is extremely competitive and requires significant computing power.

Some cryptocurrencies, like Bitcoin, are finite in supply, meaning that there is a maximum number of coins that will ever be in circulation. Others do not have a maximum cap, but limit the number of new coins that can be generated each year.

(Source: Cryptocurrency: The Tops Things You Need To Know, published by BDO USA, LLP)

#### WHAT IS CURRENTLY THE ACCOUNTING TREATMENT OF CRYPTOCURRENCY?

From an accounting perspective, intuitively, one would think that a cryptocurrency should be viewed as a financial instrument (i.e. the contractual right to receive cash or another type of asset). This is based on the assumption that if we give away a Bitcoin, the receiver has a contractual right to receive cash at some point in the future.

However, "cash" has a very specific definition as defined by the International Financial Reporting Standards (IFRS): it is a commonly accepted medium of trade. The "commonly accepted" element of this definition is where this gets tricky.

Currently, coins and paper money are commonly accepted as a medium of exchange and they are the medium used by entities to present information in their annual financial statements.

From a cryptocurrency perspective - we are just not quite there - yet. As cryptocurrency becomes more widely adopted, accounting professionals may begin to challenge whether cryptocurrencies are "commonly accepted".

# ADVISORY

## AN ACCOUNTANT'S GUIDE TO CRYPTOCURRENCY

(continued)



Currently, cryptocurrencies are treated as intangible assets (e.g. software), thus falling under IAS38 IFRS standard. An intangible asset is an asset that you control, as a result of a past event and from which you expect to receive economic benefits from in the future.

(Source: Financial Evolution: The new world of Crypto, published by BDO South Africa)

Cryptocurrencies meet the definition of an intangible asset and would be recorded at acquisition cost (i.e. price paid or consideration given). Intangible assets are subject to an impairment test. Any recognised impairment losses cannot be subsequently reversed.

Some believe the intangible model does not properly reflect the economics of cryptocurrencies because they can potentially be written down for impairment but never written up when they appreciate in value. This outcome could be less than helpful for financial statement users when significant volatility exists.

(Source: Cryptocurrency: The Top Things You Need To Know, published by BDO USA, LLP)

In conclusion, accounting for cryptocurrencies is not as simple as it might first appear. There is currently no IFRS standard on cryptocurrencies and one would argue the current accounting treatment of cryptocurrency (as an intangible asset) has not caught up with today's needs.

### WHAT IS THE TAX CONSIDERATION FOR CRYPTOCURRENCY IN MALAYSIA?

According to the Inland Revenue Board of Malaysia (LHDN), cryptocurrency investors who *actively* trade their assets at the digital asset exchange are required to declare their gains for their annual income tax.

LHDN referred to Section 3 of the Income Tax Act 1967 and said that it will treat income earned through digital platforms similarly to income generated through conventional businesses.

This tax treatment is similar for active traders of shares and other assets. The profits made by individuals who occasionally trade cryptocurrencies or shares may be viewed as capital gains, which is not taxable in

Malaysia. But the profits earned by individuals who trade actively may be viewed as revenue and thus, deemed as taxable income.

### IMPACT OF CRYPTOCURRENCY

As cryptocurrencies become investment grade instruments which corporates begin to trade, hold and transact with, there will need to be robust discussions around accounting treatments and accounting policies.

This will have an impact on liquidity, capital adequacy and credit risk as new business models are being investigated as to the use of cryptocurrencies as collateral.

It is only a matter of time for the first client attempt to disclose their annual financial statements with "Bitcoin" as their functional currency which could require the International Accounting Standards Board (IASB) to relook all accounting standards with regards to its applicability to crypto currencies and the new business models which are being attempted by entrepreneurs.

(Source: Financial Evolution: The new world of Crypto, published by BDO South Africa)

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# ADVISORY

## ACCELERATE YOUR BUSINESS INTO DIGITAL SPACE

Compiled by Pam Lee Wen Ai



### KEY HIGHLIGHTS OF THE MALAYSIA DIGITAL ECONOMY BLURPRINT

#### 1 VISION

To be a regional leader in the digital economy and achieve inclusive, responsible and sustainable socioeconomic development.

#### 3 OBJECTIVES

Encourage industry players to become creators, users and adopters of innovative business models under the digital economy.

Harness human capital that can thrive in the digital economy.

Nurture an integrated ecosystem that allows society to adopt the digital economy.

#### 6 THRUST

Drive digital transformation in the public sector.

Boost economic competitiveness through digitalisation.

Build enabling digital infrastructure.

Build agile and competent digital talent.

Create an inclusive digital society.

Build a trusted, secure and ethical digital environment.

22 STRATEGIES

48 NATIONAL INITIATIVES

28 SECTORAL INITIATIVES

# ADVISORY

## ACCELERATE YOUR BUSINESS INTO DIGITAL SPACE

(continued)

### KEY HIGHLIGHTS OF THE MALAYSIA DIGITAL ECONOMY BLUEPRINT (CON'T)

According to the blueprint, the government has set the following targets:



- ① Cashless payment for all ministries and agencies;
- ② 80% of the public sector to use cloud storage;
- ③ the chief information officer (CIO) to take on the role of the chief digital officer in every ministry;
- ④ OSC 3.0 Plus online to be used by all local authorities (a system to present online applications for development plans, making payments online, and to enable the technical agency review these applications virtually and subsequently acquire outcomes through the system);
- ⑤ 400 electronic payment transactions made per capita;
- ⑥ a greater mandate for MAMPU (the Malaysian Administrative Modernisation and Management Planning Unit) to act as an adviser, project member or subject matter expert on nationwide digital-related projects.

Malaysia to become a regional market producer of digital products and a digital solution provider.

By  
2022

By  
2025

By  
2030

- ① 100% of Malaysian households will have Internet access;
- ② online learning (My Device, My Digital Teacher Programme);
- ③ the digital economy will account for 22.6% of Malaysia's gross domestic product (GDP);
- ④ to attract two to five unicorns with headquarters in Malaysia (a unicorn is a start-up with US\$1 billion [or about RM4.04 billion] in valuation);
- ⑤ RM70 billion in digital investment;
- ⑥ 80% end-to-end government services to be available online;
- ⑦ legislations relating to broadband as a basic utility at the federal and state levels to be streamlined by 2025 (among the laws to be reviewed are the Local Government Act 1976 and the Street, Drainage and Building Act 1974 [Act 133]);
- ⑧ all ministries and agencies to use MyGDX (the Malaysian Government Central Data Exchange, a data sharing platform that provides data brokerage services for common data referred by government agencies; data sourced from original sources);
- ⑨ all schools to have access to the Internet (identifying financing models with contributions from the private sector and civil society organisations (CSOs) to support the implementation of this initiative);
- ⑩ the local data centre industry to churn out a revenue of RM3.6 billion;
- ⑪ for Malaysia to have the highest number of submarine cables landing in Southeast Asia.

# ADVISORY

## ACCELERATE YOUR BUSINESS INTO DIGITAL SPACE

(continued)

### KEY FOCUS AREAS TO BE DIGITALLY READY



#### DIGITAL TRANSFORMATION

The COVID-19 crisis has accelerated the need for digital transformation and adoption for businesses. An effective digital strategy can help alleviate the effects of these challenges, while also identifying new opportunities.

Digital transformation is not about technology and not just a job for the IT department. Increasingly more non-tech C-suite executives (e.g. CEO, CMO, CFO and COO) are responsible for leading digital transformation in their organisations.

For digital transformation to work, focus on the fundamentals which are changing mindsets and organisational culture before deciding on what technologies to use to solve business problems, boost efficiency and add value.

Companies that begin their journey today are much more equipped to staying in business and continue evolving tomorrow. The challenges will be great—but the rewards, greater.

Digital transformation is not the end goal. It is a step in the right direction.



#### BUILD AGILITY AT WORK

No business wants uncertainty, but, in the current climate, uncertainty abounds. The businesses that foster agility and prepare accordingly will be best positioned to respond to changes in the market.

To support organisational agility, it is best practice to review, update and test the business continuity plan and incident response plan. It is useful to have visibility into the business continuity plans of important suppliers and third party vendors as well. Additional steps to increase agility on a continual basis include upskilling employees and improving business processes.

Change starts at the top, so top executives and management need to champion the changes and collaborate.

(Source: Agility at Work: Workplace Strategy for the Digital Age, published by BDO USA, LLP)



# ADVISORY

## ACCELERATE YOUR BUSINESS INTO DIGITAL SPACE

(continued)

### KEY FOCUS AREAS TO BE DIGITALLY READY (CON'T)



#### CYBERSECURITY

The Covid-19 pandemic, which has fuelled unprecedented demands for internet services, cloud-based services and information technology (IT) support services, has coincided with a sharp rise in the number of cyber-attacks that have impacted organisations.

With employees required or encouraged to work remotely from home to curb the spread of the virus, many businesses find themselves unprepared and vulnerable to additional cyber risks, which can impact the confidentiality, integrity, and availability of key data and information systems.

While we often hear high profile examples of cyber-attacks, the fact is that no organisation is too big or too small to be targeted by cyber attackers.

**Research shows that most businesses take 6 months or more to detect a breach.**

Protecting your business starts with understanding some of the biggest risks such as lack of defined remote work policy, insecure devices and networks, inadequate virtual private networks (VPNs) controls as well as cyber-attacks and fraud attempt detection.



#### DATA PRIVACY

There has been a huge shift in the importance placed on data privacy.

Working from home is the "new normal" given the Covid-19 pandemic. This brings internal and external challenges. Internal considerations include the rapid shift to remote working with increased use of personal devices and dependence on key individuals. External challenges include the emergence of increased opportunities for fraudsters to illegally obtain personal data as well as the potential impact of an impaired service from external providers which may result in increased data breaches.

(Source: Privacy Insights 2020, published by BDO)

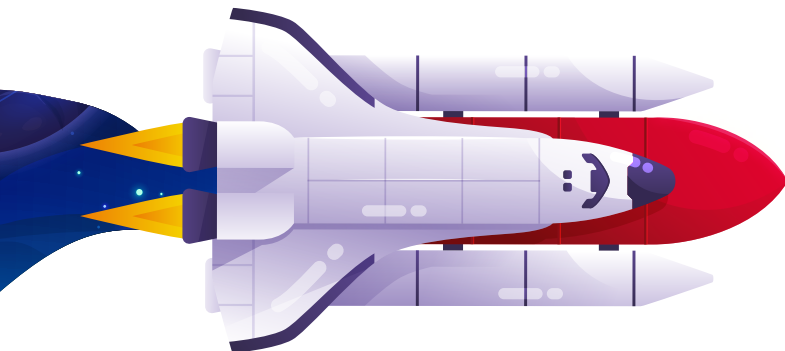
Compliance with data privacy regulations will require good data hygiene in the form of purposeful collection, protection of sensitive information and adherence to retention programmes that remove expired information. In assuring each of these, companies can expect to achieve more than mere compliance and penalty avoidance, but also to lower the cost of infrastructure and operations and to help employees gain quick access to good information to support business decisions.

(Source: The Intrinsic Value of Ensuring Data Privacy, published by BDO)

Data protection is only as strong as your weakest link – people. Organisations need to be constantly vigilant in maintaining high levels of awareness and engagement with all employees and other stakeholders to ensure that best practices and policies are adopted and followed consistently.

**As you embark on your digital journey, our team in BDO are ready to support you and our relevant services include:**

- Cybersecurity assessments
- IT risk management and data protection
- IT project management
- Business continuity management
- Third party attestations e.g. WebTrust for Certification Authorities/Public Key Infrastructure, Risk Management in Technology (RMiT), Systems and Organisations Controls 2 (SOC 2) compliance, etc



# TAX

## TRANSFER PRICING UPDATE:

### MALAYSIA TIGHTENS TRANSFER PRICING COMPLIANCE REQUIREMENTS

By Bernice Tan

The Income Tax (Transfer Pricing) Rules 2012 ("Malaysian TP Rules") require taxpayers in Malaysia to prepare Contemporaneous Transfer Pricing Documentation ("TPD"). This legislation has been effective in Malaysia since 1 January 2009. Previously, taxpayers were given 30 days to submit TPD upon request by the Inland Revenue Board of Malaysia ("MIRB").

Under Section 113(2) of the Income Tax Act 1967, penalties would be imposed on TP adjustments arising from preparing an incorrect return and the TP Audit Framework 2019 ("TP Audit Framework") provides that a penalty of 50% of the tax undercharged is applicable if no Contemporaneous TPD is prepared. If TPD is prepared but is not submitted by the due date upon request by the MIRB or in instances when the TPD has been prepared but the TPD is not in accordance with the requirements in the TP Guidelines 2012, the penalty would be 30% of the tax undercharged.

The MIRB has however noted that the level of non-compliance amongst taxpayers is still very high. With the view to increasing the rate of compliance, the Finance Act 2020 introduces several key transfer pricing amendments which are effective from 1 January 2021.

#### KEY TRANSFER PRICING AMENDMENTS EFFECTIVE FROM 1 JANUARY 2021:

##### • Failure to Furnish Contemporaneous TPD

A new Section 113B(1) of the Income Tax Act 1967 provides that where a company fails to furnish Contemporaneous TPD upon request by the IRB, the taxpayer may be prosecuted and, upon conviction be subject to a fine of between RM20,000 and RM100,000 and/or imprisonment of up to 6 months. This applies regardless of whether the company is taxable or not and the Court may still order the taxpayer to furnish the TPD within 14 days or such other period as the Court deems fit. Where prosecution is not instituted, the taxpayer may nevertheless be subject to a penalty of between RM20,000 and RM100,000 for failure to submit the TPD. Note that this penalty applies in respect of each year of assessment (with the time bar period in Malaysia being seven years).

##### • Submission of Transfer Pricing Documentation within 14 Days of a Request by the MIRB

On 29 January 2021, MIRB has updated the Malaysian Transfer Pricing Guidelines 2012 to provide that TPD should be made available within 14 days (as opposed to the previous 30 days) of a request by the MIRB.

This requirement will apply to transfer pricing audit cases which have commenced on or after 1 January 2021.

##### • Surcharge on the Transfer Pricing Adjustment

Previously, taxpayers would not be subject to penalties if the TP adjustment does not result in additional tax liability. The new Section 140A(3C) provides that a surcharge of up to 5% will be imposed on all TP



# TAX

## TRANSFER PRICING UPDATE:

### MALAYSIA TIGHTENS TRANSFER PRICING COMPLIANCE REQUIREMENTS

(continued)

adjustments and this will apply irrespective of whether there is tax payable on the adjustment.

This new provision essentially closes the net on taxpayers who previously were not subject to TP penalties notwithstanding a TP adjustment as a result of unabsorbed tax losses, unabsorbed capital allowances, tax incentives, etc.

#### • Power to Disregard Structure in a Controlled Transaction

Pursuant to Rule 8 of the Malaysian TP Rules, the Director General ("DG") has the power to disregard and re-characterise the structure in a controlled transaction to reflect arm's length economic and commercial reality. The DG's power has now been inserted into the principal legislation via Section 140A(3A) and 140A(3B) of the Income Tax Act, 1967.

Section 140A(3A) further fortifies the DG's power to disregard a related party transaction if the DG is of the opinion that:

- i The economic substance of the transaction defers from its form; or
- ii The form and substance are the same but the transaction, viewed in totality, differs from those which would have been adopted by independent parties behaving in a commercially rational manner and the structure impedes the DG from determining the appropriate transfer price.

Under Section 140A(3B) the DG has the power to re-characterise the transaction to reflect the structure that would have been adopted by an independent person dealing at arm's length having regard to the economic and commercial reality.

#### BDO'S COMMENT

With increased enforcement expected on MNCs worldwide through the BEPS initiative, these changes reflect the MIRB's expectation that Malaysian taxpayers comply with the requirement to prepare Contemporaneous TPD.

Given that the statute of limitations for the raising of assessments or additional assessments for transfer pricing adjustments is seven years (in the absence of fraud, wilful default or negligence), it now becomes increasingly crucial for companies that are required to prepare Contemporaneous TPD to ensure that their TPD is up-to-date and that they are able to meet the 14-day deadline imposed by the MIRB or face penalties of up to RM100,000 per year of assessment.

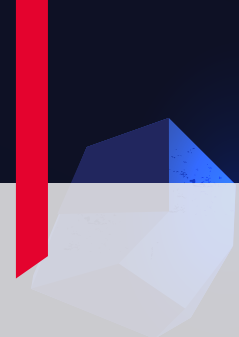
Companies that have previously not prepared TPD due to the availability of unabsorbed losses or tax incentives can no longer avail themselves to this stand given that they will now be subjected to a surcharge of up to 5% on all TP adjustments and penalties will be imposed for failure to submit TPD on time.

The DG's power to disregard and re-characterise an intercompany transaction to reflect arm's length behaviour shows the importance that the MIRB is placing on enforcing the arm's length principle in Malaysia. Taxpayers should therefore look closely at their existing supply chain, TP pricing and policies and ensure that this is supported by robust TPD and corroborative analysis accordingly.

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