

FOREIGN INVESTORS' GUIDE TO SEMICONDUCTOR INVESTMENT IN MALAYSIA

Introduction

Malaysia has long been recognized as a strategic hub for semiconductor manufacturing, with a well-developed ecosystem, strong government support, and an investor-friendly business climate. For foreign investors interested in penetrating the global semiconductor market, Malaysia offers significant opportunities. Malaysia is ever ready with favorable economic and regulatory policies supported by its skilled workforce and legal protection to the incumbent businesses and its prospective investors. The Malaysia's Prime Minister, Datuk Seri Anwar Ibrahim has announced early this year that Malaysia has attracted potential foreign investments amounting to RM76.1 billion as of March 2024.[1] Datuk Seri Anwar credited this success to the across collaboration between ministries and government agencies.

According to the official website of the United States Government, Malaysia's business environment is bolstered by its strategic location with access to Southeast Asian markets, vast land and natural resources, advanced information and communications technology (ICT) infrastructure, skilled English-speaking workforce, and a strong ecosystem of manufacturers and suppliers in key industries such as medical devices, semiconductors, and solar panels.[2] S&P Global Ratings further emphasized that Malaysia is poised to be a major beneficiary of the global semiconductor industry's boom period.[3] This article aims to provide a comprehensive guide to understanding Malaysia's semiconductor sector situations and potential, and how Azmi & Associates can assist foreign investors in navigating the legal landscape.

The Rising Hub for Semiconductor Investments:

(a) Strategic Location and Ecosystem

Malaysia serves as a strategic entry point for businesses looking to tap into Southeast Asia's burgeoning markets, particularly in high-tech industries like semiconductors. It's positioned geographically at the heart of Southeast Asia providing access to the larger

ASEAN region, a market of over 660 million people. Its proximity to major economies like China and India adds to its appeal as a regional hub for manufacturing and trade. The country also benefits from a network of bilateral and multilateral free trade agreements (FTAs), both within ASEAN and globally. Up until March 2023, Malaysia has signed and implemented a total of 16 FTAs and 62 bilateral investment guarantee agreements (IGAs). Some of its notable agreements include the ASEAN Free Trade Area (AFTA), Regional Comprehensive Economic Partnership (RCEP), and bilateral deals with countries like Japan, South Korea, India, New Zealand and Australia.[4] These FTAs and IGAs aim to reduce tariffs and ease market access, making it easier for companies to set up and operate in Malaysia whereby foreign investors are provided with specific protection and guarantees regarding their investments.

Internally, Malaysia is enhancing its infrastructure, particularly in industrial zones such as Bayan Lepas and Batu Kawan in Penang, Kulim Hi-Tech Park in Kedah, and Senai Airport City in Johor. These zones provide advanced manufacturing environments tailored to the needs of high-tech industries including semiconductors, with dedicated logistics support and access to international markets.

(b) Comprehensive Supply Chain

Malaysia is empowered with an integrated and mature semiconductor ecosystem, making it a key player in the global semiconductor supply chain. Malaysia's participation across different stages of semiconductor production solidifies its position, as its semiconductor sector covers involvement in every stage of the production process. This means that companies within the country are capable of handling everything from sourcing the fundamental raw materials[5] i.e. silicon wafers, to the final stages of production, including assembly, testing, and packaging of the semiconductor chips. Additionally, Malaysia adds significant value to the products through testing and innovation platform. Companies located in Malaysia often engage in higher-value activities such as chip design, research and development, and quality control.

This comprehensive presence across the value chain minimizes reliance on external suppliers and streamlines the manufacturing process, reducing potential disruptions. Its vertical integration helps also to prevent bottlenecks that might arise in a less connected supply chain, where delays in one step can ripple through the entire process. It also enables quicker innovations, cost savings, and better scalability in production. Accordingly, the country's contribution is not just in terms of volume but also in terms of quality, as it serves as a strategic hub for many global semiconductor giants.

(c) Government Incentive

Malaysia has been a hub for the electrical and electronics (E&E) industry since the late 1960s or early 1970s[6], with its success in the sector attributed in part to the consistent support from its government. One of the significant steps taken by Malaysian government is its initiative for National Investment Aspirations (NIA) seeks to position Malaysia as a global investment destination for high-value and high-tech sectors,

including semiconductors industry. NIA aims as a forward-looking growth framework to reach its 5 core goals i.e. to increase economic complexity, create high-value jobs, extend domestic linkages, develop new and existing clusters and improve inclusivity. Specifically for semiconductor industry, Malaysia's Ministry of Investment, Trade, and Industry (MITI) has announced the launch of National Semiconductor Strategy (NSS) consists of 3 phases. Phase 1 focuses on enhancing Malaysia's current semiconductor capabilities, expanding outsourced semiconductor assembly and test (OSAT) services, and attracting foreign investment for power chip production. Phase 2 aims to advance the design, fabrication, and testing of logic and memory chips, while integrating local design champions into the global semiconductor ecosystem. In Phase 3, Malaysia seeks to foster world-class semiconductor design and manufacturing equipment firms, while attracting cutting-edge companies for advanced chip manufacturing in the country. The Malaysia government aims to attract at least RM500 billion in investments for Phase 1 alone which is spearheaded by MITI.[7]

In addition to these plans, Malaysia also offers various tax incentives to attract foreign investor into the semiconductor sector. The Promotion of Investments Act 1986 (PIA) has introduced Pioneer Status to provide a tax relief on part or all statutory business income to a pioneer company participating in a promoted activity or producing a promoted product in Malaysia. The tax relief period for a pioneer company is 5 years, starting from the production day stated in the pioneer certificate. Malaysia's Minister of Finance (MOF) has determined that semiconductor sector falls under the promoted activities and promoted products for high technology companies.[8] Applications can be submitted to the Malaysian Investment Development Authority (MIDA) by submitting the relevant form (<https://investmalaysia.mida.gov.my/incentives/>).

Aside, back in December 2022, Malaysia has introduced Reinvestment Allowance (RA) designed to encourage companies, including those in the semiconductor sector, to reinvest in productive assets for expansion of production capacity, modernization or upgrading of facilities, or automation of manufacturing processes. For semiconductor factories, this could cover the purchase of equipment for wafer fabrication, assembly, or testing. This special tax incentive is available to a company in Malaysia which has been in operation for not less than 36 months. An eligible company can claim RA of an amount equivalent to 60% of the capital expenditure incurred in the basis period for a year of company's assessment. The allowance can be offset against 70% of the statutory income and any unutilized RA can be carried forward to future years, subject to certain conditions.[9]

(d) Malaysian Investment Development Authority (MIDA)

MIDA was established by the Malaysian Industrial Development Authority (Incorporation) Act 1965 in 1967 as the principal government agency responsible for promoting and facilitating both domestic and foreign investment in Malaysia's manufacturing and services sectors. Its core functions include attracting foreign direct investment, fostering local investment, and developing key industries through various incentives and policies. MIDA offers support in areas such as fast-tracking approvals for investment projects,

facilitating business operations, providing financial incentives and grants, and promoting strategic collaborations between investors and local stakeholders. It also plays a critical role in coordinating with other governmental bodies to streamline regulations, enhance infrastructure, and support workforce development for high-tech industries, including semiconductors.

(e) Skilled Workforce

Malaysia has a strong talent base, particularly in fields such as engineering, electronics, and semiconductor manufacturing. This is largely due to the country's emphasis on education in science, technology, engineering, and mathematics (STEM). Many local universities and technical institutions produce graduates who are equipped with relevant skills for these industries. Despite this, Malaysia still offers cost-effective labor market while still maintaining a high level of technical proficiency. Foreign investors in the semiconductor sector can hire highly trained professionals at a fraction of the cost they might pay in other parts of the world. This cost-efficiency extends across various roles in the supply chain.

In order to empower and sustain its local talent, Malaysian government has introduced various initiatives to support skills development in high-tech industries. Programs like the Human Resources Development Fund (HRDF) and collaborations between educational institutions and industry players are designed to ensure that the workforce remains relevant with the latest technologies and practices in sectors like semiconductors. Incentives such as grants, subsidies, and tax breaks are also offered to companies investing in employee training, further incentivizing foreign investors to tap into the skilled and continuously improving labor force.

Datuk Seri Anwar undertake through NSS's plan to train and upskill 60,000 high-skilled Malaysian engineers and allocate at least RM25 billion in fiscal support to operationalize the NSS with targeted incentives.[10] Moreover, the NSS also aims to leverage and enhance the Residence Pass-Talent to attract skilled foreign professionals to work in the semiconductor industry in Malaysia.

Key Considerations and Our Firm's Role in Assisting Foreign Investor

(a) Incorporation and Licensing

Foreign investors seeking to establish a business presence in Malaysia need to register their company with the Companies Commission of Malaysia (CCM), a fundamental requirement for any business entity. Following this, obtaining the necessary licenses and permits is crucial, particularly from authorities such as MIDA. The specific licenses required will vary based on the nature of the semiconductor activities, whether it be manufacturing, research and development, or other related operations. This process ensures compliance with Malaysian regulations and positions the business for successful operations within the country.

Azmi & Associates plays a pivotal role in streamlining this complex process on behalf of our clients. We offer comprehensive guidance on both the incorporation and licensing stages, leveraging our expertise to navigate the intricate legal landscape. By meticulously handling the regulatory requirements, we help minimize delays and operational obstacles, allowing our clients to focus on their core business activities. Our proactive approach ensures that all necessary prerequisites are addressed promptly and efficiently, facilitating a smoother entry into the Malaysian market.

(b) Buying and/or Leasing of Factory

When investing in Malaysia's semiconductor industry, foreign investor must carefully consider the purchase or lease of suitable property or location to establish a local presence. Key factors include identifying the right location, whether within the designated industrial zone or free trade zones. It is also important to note the regulations around property acquisition by foreigners. Hence, depending on the investor's objectives, purchasing industrial land or leasing properties, both for operational flexibility, may be a strategic decisions.

Project Practice Group in Azmi & Associates is well-versed in assisting foreign investors navigate these complexities. Our team shall provide comprehensive guidance on property and land laws, acquisition processes and leasing options that may aligned investor's interest with Malaysia's regulations.

(c) Compliance with Environmental and Sustainability Standards

In Malaysia, adherence to environmental regulations is not just encouraged but required for all companies. This compliance encompasses a range of standards, including waste management, carbon emissions, and broader sustainability practices. Investors must ensure their operations align with these regulations to maintain their business integrity and contribute to the country's environmental goals.

At Azmi & Associates, we are dedicated to guiding clients through these regulatory landscapes. Our advisory services are designed to help businesses understand and meet the stringent environmental requirements.

(d) Intellectual Property Protection

In the highly competitive semiconductor industry, safeguarding intellectual property (IP) is of paramount importance. Investors must diligently protect their innovations by leveraging Malaysia's intellectual property laws, which are designed to align with international standards. This ensures that their technological advancements are shielded from potential threats and competitors.

Azmi & Associates will be able to play a crucial role in this process with the support of our dedicated IP department. We offer a comprehensive range of services, including patents and know-how protection and registration, brand protection, trademark management, domain name registration and protection and design protection.

Additionally, we handle IP infringements and enforcement actions to ensure that our clients' innovations remain protected (<https://www.azmilaw.com/intellectual-property/>).

(e) Cross-Border Transactions and Joint Ventures

When considering partnerships or joint ventures with local entity or government-link company, investor must ensure that these arrangements are structured in strict compliance with Malaysian laws while also safeguarding your interests. This involves careful planning and adherence to regulatory requirements to avoid potential legal pitfalls. Proper structuring not only aligns with local legislation but also protects the company's objectives and investments.

Aside from agreement with local suppliers to facilitate a seamless supply chain, Azmi & Associates can play a critical role in this process by offering expert legal guidance on structuring cross-border transactions and joint ventures. We ensure that all agreements are legally sound and adhere to both local and international regulations. Our services include negotiating terms, managing legal risks, and providing essential support throughout the collaboration to facilitate smooth and compliant business operations. Recently, Azmi & Associates served as the main counsel and advisor in a landmark strategic investment collaboration involving three prominent national fund and retirement institutions i.e. Permodalan Nasional Berhad (PNB), Employees' Provident Fund (EPF), and Kumpulan Wang Perasaraan (Diperbadankan) (KWAP) with OSRAM Opto Semiconductors (Malaysia) Sdn. Bhd.

(f) Employment Laws

Investors must adhere to local human resources (HR) and employment laws to ensure smooth operations and legal compliance. In Malaysia, this includes understanding regulations related to employment contracts, worker rights, and workplace safety. Companies investing in Malaysia are required to align their HR practices with these legal standards to avoid potential disputes and ensure a harmonious working environment. Compliance not only mitigates legal risks but also enhances the investment's sustainability by fostering a positive workplace culture.

Azmi & Associates is well-equipped to assist with these matters, thanks to our extensive expertise and experience in the area of employment law. We offer comprehensive services to guide you through the complexities of local HR regulations, ensuring your entity adheres to all legal requirements. From drafting compliant employment contracts to advising on worker rights and workplace policies, our team is dedicated to providing tailored solutions that align with both local laws and your strategic objectives.

Conclusion

To conclude, embracing cultural sensitivity and understanding Malaysia's vast culture and diversity are crucial for foreign investors looking to succeed in the semiconductor industry. The presence of major semiconductor companies like Intel, Infineon, and Texas

Instruments highlights Malaysia's strong capabilities and reliability as a manufacturing hub. This established track record of global leaders reaffirms Malaysia's significant role in the international semiconductor market. By integrating effectively into this thriving ecosystem and respecting local norms, investors can not only unlock substantial opportunities but also contribute to the sector's continued growth and success. As a full-pledged legal firm, we will be able to play a pivotal role in guiding foreign investors through the complexities of legal frameworks, ensuring compliance with local regulations, and safeguarding their business interests in a foreign market. We will be available to assist at every stage, from initial planning to the successful completion of your investment journey.

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