

- (1B) Notwithstanding subsection (1), where a person who is a citizen and—
- (a) is employed in the public services or service of a statutory authority; and
  - (b) is not in Malaysia at any day in the basis year for that particular year of assessment by reason of—
    - (i) having and exercising his employment outside Malaysia; or
    - (ii) attending any course of study in any institution or professional body outside Malaysia which is fully-sponsored by the employer,

he is deemed to be a resident for the basis year for that particular year of assessment and for any subsequent basis years when he is not in Malaysia.”

The primary test set by the above definitions is clearly the quantitative test.

In determining the residence status of a taxpayer, the facts concerning him/her which may need to be examined are those of the relevant basis year, the immediately preceding years or even the following year as the case may be.

There are four sets of circumstances in which an individual acquires the status of a resident in Malaysia. Where he/she does not fall within these four categories, he/she is a non-resident.

#### (i) In Malaysia for 182 days in a basis year

Where an individual is in Malaysia for a period or periods which in total are 182 days or more, he/she is a resident for that basis year. Part of a day counts as a full day (s 7(1)(a)).

#### Example 1

An individual who arrived in Malaysia for the first time on 2 January 2014 and left on 30 June 2014 is not a resident since the period of his stay covers 180 days only.

#### Example 2

An individual who arrived in Malaysia on 14 May 2014 and left on 26 November 2014 is a resident since the period of his stay covers 197 days.

#### Example 3

An individual who arrived for the first time in Malaysia and was here:

from 1 March 2014 to 31 May 2014	(92 days)
from 4 July 2014 to 15 July 2014	(12 days)
from 1 September 2014 to 31 December 2014	(122 days)
	<u>226 days</u>

would be a resident since he was in Malaysia for periods which in total were 182 days or more.

#### (ii) In Malaysia for less than 182 days in a basis year

Where an individual is in Malaysia during a particular basis year for a period of less than 182 days but such period is linked to a period of 182 or more consecutive days throughout which he/she is in Malaysia (the qualifying period) in the basis year either immediately preceding or immediately succeeding that particular basis year, the individual will qualify as a resident for that particular basis year. Prior to YA 2002, it was important for an individual to be physically present in Malaysia on 31 December and 1 January of the following year in order to link up the two periods. However, with effect from YA 2002, any absence for these two days can be considered as part of the individual's temporary absences from Malaysia.

Temporary absences from Malaysia are to be treated as forming part of the qualifying period. Temporary absences of an individual include absences:

- connected with his/her services in Malaysia or due to service matters
- connected with attending conferences or seminars or studies abroad
- due to ill health involving himself/herself or members of his/her immediate family, and
- social visits not exceeding 14 days in total.

#### Example 1

A taxpayer left Malaysia permanently on 30 April 2014. He would be treated as a resident for 2014 (the particular basis year) if he was physically present in Malaysia throughout the period from 2 July 2013 (ie 183 days in 2013) or earlier to 1 January 2014 or later. Even if he had left Malaysia on 1 January 2014, he would be resident for YA 2014 since his stay in 2014 was linked to the period of 182 days or more in 2013.

#### Example 2

An individual first arrived in Malaysia on 1 July 2013 and left the country permanently on 30 May 2014. However, he was in Singapore from 9 September 2013 to 26 October 2013 to undergo medical treatment.

He would be resident for 2014 since his period of stay was linked to the period of 182 days or more in 2013. His temporary absence from Malaysia for medical treatment would not reduce the number of days that he was deemed to have been in Malaysia.

#### Example 3

A taxpayer arrived in Malaysia for the first time on 1 November 2013 and left on 16 July 2014. He would be deemed a resident for the basis year 2014 because he was in Malaysia for 197 consecutive days in 2014.

For the basis year 2013, the taxpayer was also resident under s 7(1)(b) since his period of stay was linked to a period of 182 days or more in 2014.

#### ¶4-230 Assessment of partners

No assessment is made on a partnership as it is not a person in law.

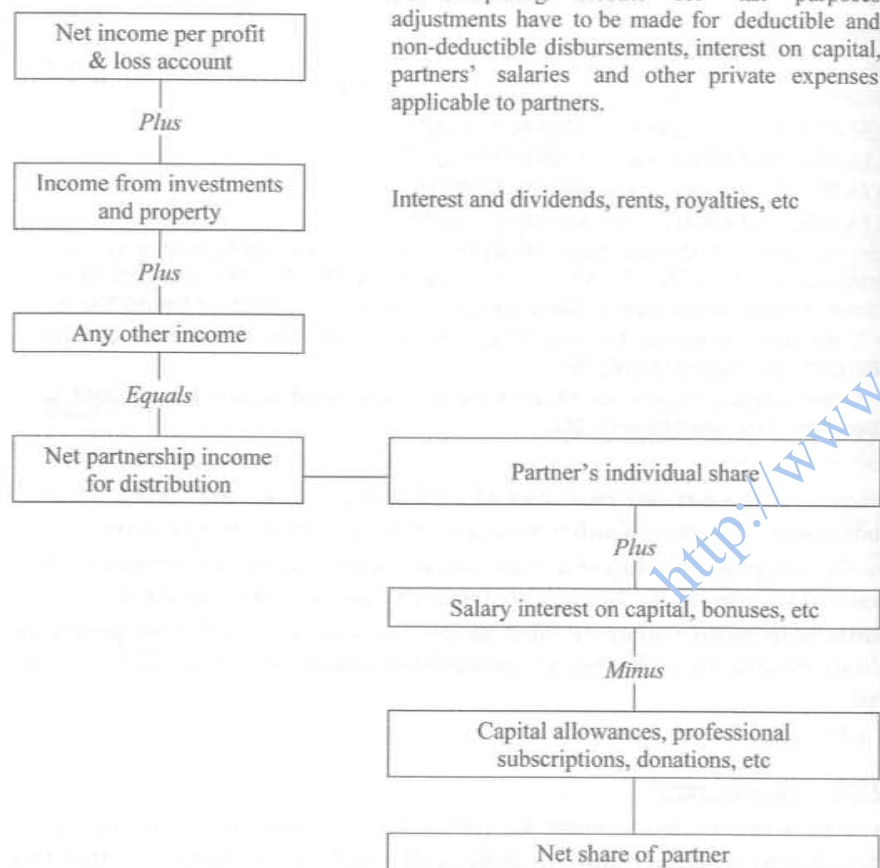
The share of income of a partner for any period is deemed to be his/her entitlement during that period.

The law provides that each partner is to be assessed separately in respect of his/her share of the partnership income. Each partner has to file a separate personal return in which his/her share of the partnership income is included.

Law: s 55(5).

### PARTNERSHIP RETURN FORM P SIMPLIFIED

#### ¶4-300 Partnership form simplified



For computing income for tax purposes adjustments have to be made for deductible and non-deductible disbursements, interest on capital, partners' salaries and other private expenses applicable to partners.

Interest and dividends, rents, royalties, etc

Form P also requires the following additional information:

- nature of business of the partnership
- business registration number
- address of each branch
- changes in constitution of the partnership during the basis year

- full particulars of partners, and
- declaration of disposal of chargeable assets (land, buildings and shares in real property companies) under the *Real Property Gains Tax Act 1976*.

### PARTNERSHIP NET INCOME OR LOSS AND PARTNER'S SHARE

#### ¶4-400 Calculating partnership income

The income of a partnership for any period is computed in the same way and on the same basis as that of a person carrying on a trade or business. This income is usually different from the figure of profit in the partnership accounts.

The profit figure is normally net after certain adjustments are made for partners' salaries, interest on a partner's capital and other personal expenses charged in the partnership accounts. Such appropriations are not allowable for tax purposes.

When the adjusted profit figure is computed, its allocation to each partner is on the basis shown in the partnership accounts.

#### Example

Lim and Ali are partners in a firm and the net profit for the year to 31 December 2013 was RM25,000. The only disallowable items, for income tax purposes, charged in the accounts were depreciation (RM1,700) and donations (RM1,300). The partnership agreement provides that Lim and Ali are to be paid an annual salary of RM3,600 and interest on capital (amounting to RM2,000 for Lim and RM400 for Ali). The capital allowances computed in accordance with prescribed rates (see ¶11-050ff) were RM2,400 and donations made to approved institutions were RM1,000. Profits were shared equally.

	RM
Net profit per accounts	25,000
Add:	
Partners' salaries	7,200
Partners' interest on capital	2,400
Depreciation	1,700
Donations	<u>1,300</u>
Provisional adjusted income	37,600
Deduct:	
Partners' salaries and interest on capital	<u>(9,600)</u>
Divisible income	<u>28,000</u>

The partners' respective share of profit from the partnership was:

	Lim	Ali	Total
	RM	RM	RM
Salary	3,600	3,600	7,200
Interest on capital	2,000	400	2,400

### Capital or revenue receipt?

Two identical transactions can yield a capital receipt in one case and an income receipt in another. An accountant who sells his/her car sells it on a capital account, whereas a car dealer who sells a car does it on a revenue account. The latter's receipts are of an income nature. It follows that the status of the recipient in such cases becomes important.

Generally, the accounting treatment gives support to its nature but cannot be considered conclusive for tax purposes.

Since Malaysia does not cater for tax on capital gains or profits (except on certain properties), once a receipt is evaluated as one of a capital nature, it should be ignored for tax purposes (see ¶17-050ff).

In the case of a trade or business, all receipts which are normally related to the circulating capital or stock in trade of the business are considered of an income nature. Those related to fixed capital are of a capital nature. There are certain tests that can be usefully applied in varying degrees to a transaction in question:

- Does the receipt arise from the carrying on of the trade or business? Thus, if a receipt has little relevance with the business or falls outside the scope of its operations, it cannot give rise to a gain or profit from the trade. This does not, however, mean that the receipt will fall outside the scope of taxation. It may well be taxable under some other heading in s 4 of the ITA 1967.
- Is it a capital or a revenue receipt?
- Are there any provisions in the ITA which require that the receipt in question is to be given special treatment? For example, is it specifically exempted or is it subject to tax at a reduced rate?

Insofar as personal services are concerned, the criteria are different. Briefly, all the flows from an employment will rank as income receipts unless specifically exempted.

Income referred to in tax legislation is taxable income, ie that income which is chargeable to tax under the tax laws of the relevant country.

Income is taxable only when it is received or, as in the case of businesses, when it becomes receivable. Further, tax can only be charged on and paid by the person receiving or entitled to the income. Hence, traders may pay tax on the balance of profits or gains and bring money owed to them into account but ordinary individuals are not assessable and do not pay tax until they get the money because until then it is not part of their income (*IR Commrs v Whitworth Park Coal Co Ltd*).

The concept of income is not *in vacuo*. The income bears its quality as income only if it is received by the taxpayer or it has accrued or has arisen to the taxpayer. It can also be income if it is fictionally deemed to be received by, or is deemed to have accrued or arisen to, a taxpayer.

### ¶7-055 Income "deemed" to derive from Malaysia

"Deemed to derive" means "deemed by the statutes" to derive. In other words, income in reality is not derived but the ITA requires it to be treated as income derived from Malaysia. Artificial derivements are provided in the Malaysian ITA and broadly fall under five concepts:

- *Artificial derivation*

Such artificial derivation is provided in s 31 of the ITA. This section deems the "annual value" of property occupied by the taxpayer who owns it to be income derived although no income may actually be received or derived from such property. [CCH Note: s 31 was deleted by s 9 of the *Finance (No 2) Act 2002*.]

- *Artificial place of derivation*

In such a case the income is not in reality derived in Malaysia but the ITA requires it to be treated as if it was derived here.

The fiction in s 15, eg fixes the place of derivation in Malaysia of certain types of interest and royalties.

- *Artificial chargeability of a person*

Here the income of someone else may be deemed to be the income of the person sought to be taxed.

- *Artificial year of taxability*

Here, the income may be deemed to be the income of the previous year, ie the accounting year or year of remittance of offshore income, when actually it may be the income of a different year.

- *Artificial amount of derivation*

This situation arises where the amount actually derived is artificially reduced. For instance, s 54 states that the profits of a non-resident shipping operation will be 5% of the gross earnings from outward shipments from Malaysia.

### ¶7-060 Charging section

Section 4 of the ITA is the charging section and sets out six main headings of income that are chargeable to tax:

- profits or gains from a trade, business, profession or vocation (s 4(a))
- profits or gains from personal services — employment (s 4(b))
- dividends, interest and discounts (s 4(c))
- rents, royalties or premiums (s 4(d))
- pension, charge or annuity or other periodical payments (s 4(e))
- gains or profits from other sources (s 4(f)).

For each year of assessment, tax is levied on the total of the income derived under the above headings.

Law: s 4.

	Scheme A (no EPF) RM	Scheme B with EPF at 10% RM
Cash salary	100,000	90,000
10% EPF		10,000
Salary assessable to tax	100,000	100,000
		90,000

Harry's exposure to tax under Scheme B is reduced by RM10,000.

Law: s 33(1), 39(1).

### ¶7-275 Dual employment contracts

There is nothing in the tax laws of Malaysia which prohibits an employee from exercising two employments, one in Malaysia and one outside Malaysia, or for that matter both in Malaysia. As one may be resident of two countries for the same year, so too one can have employment in two countries in the same tax year.

Where an employee of a multinational group is based in Malaysia and where he/she is required to perform part of the duties of his/her employment outside Malaysia for a branch, an associate company or a subsidiary of the multinational outside Malaysia, he/she need not pay any Malaysian tax on that part of his/her remuneration which is paid to him/her by his/her offshore employer. One important condition must, however, be fulfilled to attain complete tax insulation here, i.e. no part of the services relating to the offshore employment contract must be performed in Malaysia.

#### Example

Moses is employed by CCH Sdn Bhd, a subsidiary of an American multinational company. In respect of his Malaysian and Singapore duties, he is paid RM100,000 and RM50,000 respectively. If Moses has only one contract, where part of his Singapore contract is performed in Malaysia, his income from employment assessable to Malaysian tax would be RM150,000.

If Moses has two contracts, and performs his contracts only in the respective countries, his employment income assessable to Malaysian tax would be RM100,000. His Singapore income of RM50,000 as an employee (not a director) would be subject to the 15% non-resident tax in Singapore.

### ¶7-280 Payments for commencing or continuing an employment

It is considered that a payment for inducing a person to commence an employment is not of an income nature as it does not relate to either "having" or "exercising" an employment under s 13(1)(a).

The Court of Appeal has held that lump sum payments made to rugby union footballers are not taxable. These "signing fees" were held to be inducements to the footballers to put themselves in a position in which they could be employed by the clubs and to relinquish their amateur status (*Jarrold v Boustead*).

A payment for continuing an employment may also, arguably, be treated as non-taxable.

## INCOME FROM A TRADE, BUSINESS, PROFESSION OR VOCATION

### ¶7-300 General

Under the Malaysian ITA, "business" includes "profession, vocation and trade and every manufacture, adventure or concern in the nature of trade, but excludes employment". The ITA does not define income and gains from these sources, but various definitions and clarifications have, however, been provided by the courts and by commercial practice and principles.

A person may be carrying on one particular business which embraces a number of activities or he/she may carry on two or more distinct businesses. A business person may pursue activities which fall outside the scope of his/her business but they may not themselves constitute the carrying on of a business.

The courts have been reluctant to define what a "trade", "profession" or "vocation" is (*Griffiths v JP Harrison (Watford) Ltd*; *IR Commrs v Maxse*; *Partridge v Mallandaine*). Despite this, an abundance of case law can be cited as precedent when the question of whether or not a taxpayer is carrying on a business, profession or vocation is considered.

There are circumstances where interest income may qualify as business income as the transactions may be indicative of a business or an adventure or concern in the nature of trade (*PCEO Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* (1997) MSTC 2,891). In *Director General of Inland Revenue v Pan Century Edible Oils Sdn Bhd* (1998) MSTC 3,675, interest income from excess cash placed on short-term and long-term deposits was taxable as business income.

Section 4B (which took effect from YA 2013) provides that interest income shall be treated as business income only if the debenture, mortgage or other source to which the interest relates forms part of the stock-in-trade of a business of a person or the interest is receivable by a person from the business of lending money and that business is one which is licensed under any written law.

Pursuant to the savings and transitional provisions, any unabsorbed loss and capital allowance for YA 2012 in respect of interest from a business source prior to the introduction of s 4B and amendment to s 24(5) will be carried forward and deducted against the aggregate statutory income from any other business source in YA 2013 and subsequent years of assessment until the amount is fully deducted.

Based on the above amendments, all other types of interest income (eg interest charged to trade debtors for late payment) will be subjected to tax as a passive source of income. As such, court decisions such as *Pan Century Edible Oils* and *Isyoda* would

**¶8-805 Income from dealing in non-ringgit sukuk**

From YA 2009 until YA 2011, the statutory income derived from a business of dealing in non-ringgit *sukuk* that originates from Malaysia and issued or guaranteed by the Government of Malaysia or approved by the Securities Commission under the CMSA 2007 by a Malaysian resident who is:

- a holder of a Capital Markets Services Licence granted under s 61 of the CMSA 2007
- a registered person under s 76(1)(a) of the CMSA 2007, or
- a registered person under s 76(2) of the CMSA 2007,

shall be exempted from tax provided that such dealing is carried on through the proprietary account of such person.

Such dealing shall be treated as a separate and distinct source of business and activity, and separate accounts are to be maintained by such person.

The exemption is extended to YA 2014 via the Income Tax (Exemption) (No 10) Order 2011.

Law: Income Tax (Exemption) (No 9) Order 2008; Income Tax (Exemption) (No 10) Order 2011.

**¶8-810 Income from dealing in securities and advising on corporate finance relating to non-ringgit sukuk**

From YA 2009 until YA 2011, statutory income derived from the regulated activity of dealing in securities and advising on corporate finance relating to the preparation, underwriting and distributing of non-ringgit *sukuk* that originates from Malaysia and issued or guaranteed by the Government of Malaysia or approved by the Securities Commission under the CMSA 2007 by a Malaysian resident who is:

- a holder of a Capital Markets Services Licence granted under s 61 of the CMSA 2007
- a registered person under s 76(1)(a) of the CMSA 2007
- a registered person under s 76(2) of the CMSA 2007, or
- a specified person under Sch 3 of the CMSA 2007 who carries on the regulated activity of advising on corporate finance solely incidental to the carrying on of its business or the practice of his profession,

shall be exempted from tax.

Such activity shall be treated as a separate and distinct source of business and activity, and separate accounts are to be maintained by such person.

Under the Income Tax (Exemption) Order 2010, with effect from YA 2010, any person is exempted from income tax in relation to any income derived from *sukuk ijarah* (other than convertible loan stock) issued in any currency by 1Malaysia Sukuk Global Berhad. Withholding tax under s 109 and 109B will not apply to the exempted income.

The exemption is extended to YA 2014 via the Income Tax (Exemption) (No 10) Order 2011.

Law: Income Tax (Exemption) (No 10) Order 2008, Income Tax (Exemption) Order 2010; Income Tax (Exemption) (No 11) Order 2011.

**¶8-820 Fees received by corporate advisors for listing of foreign companies and foreign products in Malaysian stock exchange**

Effective from YA 2009 to YA 2013, an income tax exemption will be given on fees received by corporate advisors for primary listing, dual listing or cross listing of:

- corporations with predominantly foreign-based operations
- exchange-traded funds and real estate investment trusts with foreign-based assets
- foreign-listed securities, and
- foreign financial instruments.

The exemption is subject to listing conditions approved by the Securities Commission.

Law: Income Tax (Exemption) (No 11) Order 2008.

**¶8-825 Insurance and takaful companies**

Tax exemption is given to insurance or *takaful* companies on statutory income for five years from the commencement of operations of branches or subsidiaries on:

- profits of newly established branches overseas, or
- income remitted by new subsidiaries overseas.

This is effective for applications to establish new branches or subsidiaries overseas received by Bank Negara not later than 31 December 2015 (see further details in ¶13-412).

Law: Income Tax (Exemption) (No 5) Order 2009.

**¶8-830 Owners of buildings awarded the Green Building Index (GBI) certificate**

Under the Income Tax (Exemption) (No 8) Order 2009, a resident company which was issued with a GBI certificate from 24 October 2009 until 31 December 2014 by the Board of Architects Malaysia was to be given tax exemption equivalent to 100% of the additional capital expenditure incurred in relation to the construction of a building, alteration, renovation, extension or improvement of an existing building to be set off against 100% of the statutory income for each year of assessment.

The Income Tax (Exemption) (No 5) Order 2011 replaces the Income Tax (Exemption) (No 8) Order 2009 and is effective from YA 2009. The new Order is basically the same as the previous one except that it has been widened to incorporate expenditure incurred on plant and machinery, revised the non-applicability provision and introduced a withdrawal of the exemption if a disposal of the qualifying expenditure occurs within two years.

An amount equal to the *qualifying expenditure* (QE) incurred by a resident person (including a resident company incorporated under the *Companies Act 1965*) for the purpose of obtaining a GBI certificate on a building used for the purpose of a business is exempt from payment of income tax on statutory income from that business. Where the exemption cannot be given in full due to insufficiency of statutory income, the unabsorbed portion shall be carried forward until the whole amount is fully exempted.

The principle to be applied in determining whether or not interest is deductible involves a determination of the purpose for which the principal amount of the loan has been applied. If the moneys borrowed are used for the purchase of revenue or capital assets of a business or in meeting outgoings incurred in carrying on the business or for the purchase of property from which income is derived, the interest thereon is deductible (*Munro v FC of T*). Thus, a taxpayer who borrowed moneys to finance the construction of a hotel was entitled to claim the interest as an expense incurred in the production of assessable income; the interest had been incidental and relevant to the production of that income (*Travelodge Papua New Guinea Ltd v Chief Collector of Taxes*).

In the UK case of *Robinson v Scott Bader Co Ltd*, it was held that where a company's sole object is to benefit itself and to achieve this it affords financial assistance to its subsidiary, the expenses incurred for this purpose are deductible. See ¶9-070.

The general rule is that if money is borrowed for the purchase of revenue or capital assets of a business or for meeting disbursements in carrying on the business or for acquiring property from which income is derived, the interest on moneys so borrowed ranks for deduction (*Munro v FC of T*).

Section 33(1)(a)(i) has no application to cases where interest is paid on money borrowed to settle a debt as it does not amount to it being employed in the production of income. In other words, interest incurred on a loan taken to refinance an existing loan is not deductible.

### Case law

However, the High Court held that such interest is deductible (*RB Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* (1995) 2 MSTC 2,360). Interest payments were held to be taken out of the scope of s 33(1)(a)(i) where there was mixed utilisation of the borrowed money (*SS Construction Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri* (1995) 2 MSTC 2,369).

Section 33(2) specifically provides that where a taxpayer has borrowed money for the purpose of producing income, and has also lent or invested money otherwise than for the purpose of producing income, the deductibility of interest paid on borrowed moneys will be restricted.

In order to arrive at the proportion of inadmissible interest, a taxpayer must first assemble the following information:

- the amount of monthly interest deemed payable over the accounting year. The subsection provides that "interest . . . shall be deemed to accrue evenly over that period . . .". Consequently, the total amount of interest is divided into the number of months in the accounting year
- the amount of moneys borrowed and unpaid at the end of each month
- the amount of invested money at the end of each month. This is to be done by reference to its original cost value, and
- the income, if any, derived from the invested money during the relevant period.

The following rules are then applied to the above information:

- if at the end of a month, the amount of invested money is greater than the amount of borrowed money, no claim of interest, deemed to be paid for that month, will be admitted
- if at the end of a month, the amount of invested money is less than the amount of borrowed money, the monthly interest is reduced by the proportion of the interest that the amount of the invested money bears to the amount of the outstanding borrowed money at the end of that month
- if at the end of a month, there is no money lent or invested the whole of the interest for that month will rank for deduction, and
- if income is derived from invested money, ie dividends or interest, and if it can be proved to the satisfaction of the Director General that the invested money was provided from the borrowed money, then the disallowable interest, if any, will be reduced by the income from the invested money.

The following is a simple illustration of how the provisions of s 33(2) operate:

	Interest payable RM	Money borrowed RM	Money loaned or invested RM
Jan	1,000	300,000	150,000
Feb	1,000	400,000	300,000
Mar	1,000	250,000	300,000
Apr	1,000	150,000	300,000
May	1,000	700,000	500,000
Jun	1,000	400,000	500,000
Jul	1,000	600,000	200,000
Aug	1,000	Nil	200,000
Sep	1,000	350,000	200,000
Oct	1,000	100,000	Nil
Nov	1,000	700,000	300,000
Dec	1,000	400,000	300,000

The proportion of interest that will be disallowed for income tax purposes will be:

	RM		Interest disallowable for tax purposes RM
Jan	$\frac{1,000 \times 150,000}{300,000}$	=	500
Feb	$\frac{1,000 \times 300,000}{400,000}$	=	750
Mar	The whole interest is disallowable as the invested money exceeds the money borrowed	=	1,000
Apr	As for March	=	1,000
May	$\frac{1,000 \times 500,000}{700,000}$	=	715
Jun	As for March	=	1,000

## Research

Section 34A provides for the deduction of research expenditure incurred by a taxpayer and related to the trade or business carried on by him/her. The deduction is extended to such expenditure, if incurred on the taxpayer's behalf and related to his/her trade or business. Research expenditure whether incurred in Malaysia or outside Malaysia will rank for deduction provided the research is approved by the Minister. "Research" is not defined in the ITA but the meaning of the term has been provided in Public Ruling No 5/2004.

"Research" means any systematic study or intensive study carried out in the field of science or technology with the object of using the results of the study for the production or improvement of materials, devices, products, produce or processes. However, the definition in the PIA 1986 goes further and excludes the following:

- quality control of products, or routine testing of materials, devices, products or produce
- research in the social sciences or the humanities
- routine data collection
- efficiency surveys or management studies, and
- market research or sales promotion.

It would appear that s 34A expenses would include pre-commencement expenses which in normal circumstances are considered of a capital nature. This recognises the time-lag between the initial expenses incurred, other than those on the acquisition of fixed assets, and the final result.

The following expenditure is specifically prohibited:

- (i) capital expenditure incurred on plant and machinery, fixtures, land, premises, buildings, structures or works of a permanent nature
- (ii) expenditure in respect of alterations, additions or extensions of items in (i) above, and
- (iii) expenditure in the acquisition of any rights in or over any property.

To encourage a pioneer company to undertake research and development (R & D) during the pioneer period, s 34A(4A) provides that with effect from YA 2003, a pioneer company will be allowed to elect to claim a tax deduction for R & D expenses incurred during the pioneer period in the post-pioneer period. The Addendum to Public Ruling No 5/2004 provides that the election has to be made on a yearly basis for each relevant year of assessment. The amount of qualifying research expenditure for each year of assessment will be accumulated and carried forward to be deducted on the first basis period of the post-pioneer business instead of being given a double deduction for each relevant year of assessment.

## Business Deductions

### Research and development

Companies undertaking R & D activities may qualify for pioneer status, investment tax allowance or for double deductions on revenue expenditure for R & D (under the ITA), depending on the nature of their activities. The definition of "R & D" under the PIA 1986 is as follows:

"... any systematic or intensive study carried out in the field of science or technology with the object of using the results of the study for the production or improvement of materials, devices, products, produce or processes ..."

The definition goes on to specifically exclude quality control or routine testing, routine data collection, etc. Based on the above definition, a company undertaking only designing, prototyping or testing would not qualify for the incentives.

To encourage R & D activities, with effect from YA 1998, the incentives were extended to companies undertaking designing and prototyping as an independent activity. The incentives are pioneer status or investment tax allowance, or a double deduction on expenditure for in-house R & D, and expenditure on R & D undertaken in an approved R & D institution. Companies undertaking testing alone will not qualify for the incentives.

Under the Malaysian ITA, in order to encourage more taxpayers to undertake research, it is provided that a deduction of twice the expenditure will be allowed.

Where a building is used for the purpose of research approved by the Minister such a building will qualify as an industrial building and wear and tear allowances will be granted accordingly. Where a building is rented and used for research, any expenditure incurred on alteration and renovation will also qualify for industrial building allowances.

### Restrictive covenant payments

Sums paid specifically for a restrictive covenant were held to be not deductible from the assessable income of the employer (*Associated Portland Cement Manufacturers Ltd v Kerr*). See also ¶7-260.

### Fines

In *Mayne Nickless Ltd v FC of T*, it was held that fines and penalties are not deductible. The Court held that public policy considerations operated to deny any deduction and the admission of deduction of outgoings of this nature would frustrate the policy of the legislation imposing the penalty. The offences for which the fines were imposed were mainly parking infringements and overloading.

### Reimbursement of revenue expenses

These are of a capital nature (*Comms of IR v William Sharp & Son*).

### Buying off competition

Where a taxpayer pays a sum of money to buy off competition, the payment is considered one of a capital nature. Expenditure incurred by a taxpayer to prevent publication of a competing newspaper was held to be of a capital nature as it benefited the business entity, structure or organisation set up or established for the earning of profits (*Sun Newspapers Ltd v FC of T*).

is open to any member of the public (with effect from YA 2014, the abovementioned fund can also be used to purchase buildings to be used as places of worship)

- an organisation which maintains or assists in maintaining a zoo, museum, art gallery or similar undertaking
- an organisation which engages in or is connected with the promotion of culture or the arts
- an organisation engaged in or in connection with the conservation or protection of animals
- a government-assisted organisation engaged solely in addressing problems relating to industrial and commercial development and promoting and enhancing the relationship between the public sector and the private sector
- a government-assisted organisation established and maintained exclusively to administer and augment a fund established or held solely for promoting national unity
- an organisation, established exclusively for the conservation or protection of the environment
- an "international organisation" as defined under the *International Organisation (Privileges and Immunities) Act 1992* carrying out such charitable activities as determined by the Minister
- an organisation established and maintained exclusively to administer, augment a fund established or held for the purpose of carrying out projects towards the acculturation of the community in information and communication technology, approved by the Minister
- a benevolent fund or trust account established or held for the sole purpose of providing relief or aid to an individual who has no, or insufficient means, or in the case of a dependent individual whose parents or guardian has no, or insufficient means, to pay for the cost of the medical treatment required by such individual to treat a serious disease.

The above types of institutions must be located in Malaysia to rank for approval.

Such approved charitable institutions or organisations under s 44(6) are themselves exempted from income tax in respect of income, other than dividend income received by them. However, in order for them to retain the s 44(6) status, they must comply with the condition that at least 70% of its income is disbursed annually for charitable purposes. However, with effect from YA 2005, the minimum income to be disbursed annually for charitable purposes has been reduced from 70% to 50% of the income received in the basis year.

If there is evidence that the public or a large section of the community will benefit, the institution or organisation will pass the qualifying tests. Hence, a public school in England which derived a portion of its income from charity, was managed by a public body, did not have profit making intentions, and had as its object the benefit of a large class of persons, was held to be a public institution (*Blake v London Corporation*). Gifts in kind to public institutions do not qualify for deduction.

### Example

If a trader presents a motor car to the home for the aged, which is an approved institution, he will not be entitled to deduct the cost of the car against his assessable income. If, on the other hand, he paid the cost of the car to the home, and the home in turn bought the car from him, a deduction would arise.

As gifts are non-business deductions, unless there is a balance of aggregate income, no relief will be allowed.

### Example

If a company had an aggregate income of RM1,000 for YA 2014 and had made a cash donation of RM1,500 to the Association for the Blind, only RM70 (ie 7% of the aggregate income) would be allowed, and the disallowable balance of RM1,430 would not be available to be carried forward for set-off against subsequent years' profits. If the company made a loss, then no part of the donation would qualify. If the above referred to YA 2015, the company would obtain a deduction for RM100 (ie 10% of the aggregate income) of the cash donation.

Law: s 44(6), (7), (11B), (11C).

## 10-810 Gifts to Government

The basis for claiming deductions of gifts to the Malaysian Government is the same as that applicable to approved institutions. That is to say, the gifts must be in cash, they must be made in the relevant year, they can only be set off if there is statutory income and any balance disallowable cannot be carried forward. Where the gifts are in the form of artifacts, manuscripts or painting, the amount equal to the value, as determined by the Department of Museums and Antiquities or the National Archives, will be deductible. The Malaysian Government gives support to educational and welfare organisations and where it exercises some form of control and supervision, such an organisation is often considered to be a government institution.

Law: s 44(6A).

## ¶10-820 Carry forward of unallowed donations

The ITA does not provide for unallowed balances of donations and religious dues to be carried forward for set-off against future income.

## ¶10-830 Cash contributions to libraries

From YA 1995, gifts of money of up to RM20,000 made by individuals to public libraries and libraries of schools and institutions of higher learning are deductible.

Law: s 44(8).

## ¶10-870 Contributions towards providing facilities for disabled persons

From YA 1998, gifts of money or contribution in kind made by individuals for the provision of facilities in public places for the benefit of disabled persons are deductible.

Law: s 44(9).

resident, on a CIF ("cost, insurance and freight") contract the goods are considered as having been delivered in Malaysia. On the other hand, where goods are on an FOB ("free on board") basis, they are considered as having been delivered outside Malaysia, ie delivered at the port of loading.

### ¶12-240 Director General's tests and queries

The following are some of the many factors and questions on which the Director General determines whether or not a non-resident does business within Malaysia:

- Does the agent accept orders in Malaysia on behalf of the non-resident person or does he/she merely transmit the solicited orders to the non-resident for the latter's acceptance abroad?
- Are the goods sent direct to the buyer — ie invoiced to him/her — or are they sent to the agent for delivery to the buyer? In the latter case, it would appear that in the first instance the principal will invoice the agent. This is followed by the agent invoicing the buyer.
- Where are the payments for the goods made, ie direct from the buyer to the overseas seller or from the buyer to the agent and ultimately to the overseas seller?
- Are the goods sent to Malaysia on CIF or FOB terms?
- Does the agent maintain a stock of merchandise in Malaysia belonging to the non-resident, from which he/she makes deliveries in respect of contracted sales?
- What are the terms of the agency agreement? Here the agency contract can provide useful information about the relationship between the principal and his/her Malaysian agent.
- What is the degree of control by the non-resident of the agent in Malaysia, ie pricing, sales, etc?
- Does the non-resident trade in Malaysia through a consignee?

### ¶12-250 Regular agency

Whether or not a regular agency exists is a question of fact and some of the more important factors that go to determine this are:

- Does the agent act for only one principal or several principals?
- Does the agent act as a sole agent for the non-resident person?
- Is the agent's appointment confined to a specific area in Malaysia or does it cover the whole of Malaysia?
- Has the non-resident principal, by notification in the press or *Government Gazette*, made it known that he/she is appointing an agent in Malaysia? Or does the agent, by notification, hold himself/herself out as the agent for the non-resident person?
- Is the agent merely indenting for supplies or does he/she also place orders for his/her own retailing and wholesaling activities?
- Does the agent get a commission only on orders placed through him/her or by him/her or does he/she get an overriding commission on all orders placed by whosoever from within the jurisdiction he/she is covering?
- Does the agent have the authority to conclude contracts in Malaysia on behalf of the non-resident principal?

### ¶12-260 Brokers

The position of a broker is somewhat different from that of an agent. Any sales or transactions carried out by a broker in the ordinary course of his/her business do not expose the non-resident buyer or seller to any danger of carrying on a trade within Malaysia.

Normally *bona fide* brokers in Malaysia who transact business on behalf of non-resident persons receive a remuneration in the form of brokerage or commission. Thus, where a non-resident person executes sales or carries out transactions, through a *bona fide* broker in Malaysia, this will not in itself be taken as ground for charging the non-resident to Malaysian tax. In other words, any business between non-residents and *bona fide* agents or brokers will not expose the non-resident to Malaysian tax.

### ¶12-270 Non-residents trading through consignees

Non-residents who carry on activities in Malaysia through consignees are liable to Malaysian income tax on the profits they derive from sales effected by the Malaysian consignees. This extends to trading in any commodity produced outside or inside Malaysia. Specific exemption is, however, given to those non-residents who trade through consignees in rubber, copra, pepper, tin, tin ore, gambier, sago flour or cloves on condition that these commodities are produced outside Malaysia (see ¶18-625).

### ¶12-280 Double taxation agreements

Malaysia's double taxation agreements provide for the concept of a "permanent establishment" (see ¶15-250). Generally, the agreements provide that a person resident in a state which has contracted an agreement with Malaysia will not be deemed to be trading in Malaysia unless he/she has a fixed place of business, ie a permanent establishment, here. From the point of view of the non-resident, whether a company or an individual, it is immaterial if taxes are paid or payable in Malaysia if they can be offset by way of credits in the home country as a consequence of a double taxation agreement. In practice, however, because of the different tax bases existing between countries, each country pursues the objective of collecting all the tax to which it is legally entitled (see further ¶15-050ff).

### ¶12-290 Non-resident sales agents

Often non-resident sales agents provide services outside Malaysia for the Malaysian exporters and manufacturers. The commissions paid to such non-resident agents for their services are not considered to be taxable here on the grounds that the commissions arise abroad at the location where the services are performed, and not in Malaysia.

## FOREIGN BRANCH OR SUBSIDIARY OR JOINT VENTURE

### ¶12-300 Choice of media

A non-resident has the choice of conducting his/her operations in Malaysia in the form of:

- a branch
- a separate Malaysian company, or
- a joint venture with a Malaysian business organisation or investor.

- natural rubber sheet and slabs, standard Malaysian rubber, crepe natural rubber, natural rubber latex and natural gums
- crude palm kernel oil, palm kernel cakes and crude palm oil
- copra, copra cakes and crude coconut oil
- logs, sawn timber (ungraded and non-kiln dry) and wood chips (except briquettes), and
- petroleum oils (crude and other than crude) and petroleum gases and other gaseous hydrocarbons (liquified or in gaseous state), hydrogen, nitrogen and oxygen.

The allowance is given to the following types of companies in the service sector:

- |                             |   |
|-----------------------------|---|
| (1) legal                   | (10) private health   |
| (2) accounting              | (11) private education  |
| (3) architecture            | (12) publishing services                                      |
| (4) marketing               | (13) information and communications technology (ICT) services |
| (5) business consultancy    | (14) engineering services                                     |
| (6) office services         | (15) printing services, and                                   |
| (7) construction management | (16) local franchise services.                                |
| (8) building management     |   |
| (9) plantation management   |   |

The eligibility for items (1) to (11) above is deemed to have come into operation on 1 January 1998 while for items (12) and (13), the effective date is YA 2001 under the Income Tax (Exemption) (No 2) Order 2001. The effective date for items (14) to (16) is YA 2006 under the Income Tax (Exemption) (Amendment) Order 2006.

Law: PIA 1986; Income Tax (Exemption) (No 2) Order 2001; Income Tax (Exemption) (Amendment) Order 2006.

### ¶13-320 Rate of allowance

This incentive is given at the following rates:

- 10% of the value of increased exports of manufactured products by the company where the products exported attained at least 30% of value added
- 15% of the value of increased exports of manufactured products by the company where the products exported attained at least 50% of value added
- 10% of the value of increased exports of agricultural produce (fresh and dried fruits, fresh and dried flowers, ornamental plants and ornamental fish, frozen raw prawn or shrimp, frozen cooked and peeled prawn, and frozen raw cuttlefish and squid) by the company, and
- 50% of the value of increased exports for companies in the service sector (prior to YA 2002, it was 10% of the value of increased exports).

#### Definition

"Value added" refers to the sale price of goods at ex-factory price less the cost of raw materials. "Increased exports" refers to the increase in the value of direct exports (not including sales to Free Industrial Zones and Licensed Manufacturing Warehouses) or qualifying services exported over the preceding year.

Except for private health-care and education services, "qualifying services" refers to services which are provided to foreign clients from Malaysia. As for private health-care and education services, these are qualifying services when the services are provided to foreign clients either in or from Malaysia. "Foreign client" refers to a company, a partnership, an organisation or a co-operative society which is incorporated or registered outside Malaysia or an individual who is a non-Malaysian citizen and does not hold a Malaysian work permit or an individual who is a non-resident Malaysian citizen living abroad.

#### Increased rate of allowance for health-care services

The Income Tax (Exemption) (No 6) Order 2009 provides that, for YAs 2010 to 2014, the tax exemption on statutory income granted to health-care service providers who provide services in Malaysia to foreign clients will be increased from 50% to 70% of the value of the increased exports but limited to 70% of the statutory rate for each year of assessment. For the purpose of this incentive, foreign clients include:

- a non-Malaysian citizen who participates in "Malaysia My Second Home" Programme and his/her dependants
- a non-Malaysian citizen holding a Malaysian student pass and his/her dependants
- a non-Malaysian citizen holding a Malaysian work permit and his/her dependants, or
- a non-resident Malaysian citizen living abroad and his/her dependants.

However, health-care services offered to such excluded foreign clients will continue to enjoy the existing incentives.

The abovementioned Order does not apply to the following persons who:

- have been granted any incentives (except for deductions for promotion of exports) under the PIA 1986
- have been granted investment allowance in respect of an approved service project under Sch 7B of the ITA
- have been granted an exemption under s 127(3)(b) or 127(3A) of the ITA, or
- have been granted an exemption under the Income Tax (Exemption) (No 9) Order 2002.

Law: Income Tax (Exemption) (No 2) Order 2001; Income Tax (Exemption) (No 9) Order 2002; Income Tax (Allowance for Increased Exports) (Amendment) Rules 2003; Income Tax (Exemption) (No 6) Order 2009.

unitholder which is not a resident company, the REIT or PTF has to deduct and remit to the IRB at the following applicable withholding tax rates:

**Income distributed to:**

	Withholding tax rate
Non-corporate investors (resident and non-resident individuals)	— 15% for 5 years
Foreign institutional investors (particularly the pension funds and collective investment funds)	— 20% for 5 years
Non-resident companies	— 26% (YA 2008) — 25% (YA 2009)

A resident company which receives income distributed from an REIT or PTF is subject to tax at the corporate rate of 26% and 25% for YA 2008 and YA 2009 respectively.

The unitholders are allowed a tax credit under s 110, where the undistributed income of an REIT or PTF that has been subject to tax in a year of assessment is subsequently distributed in the following years of assessment.

From 1 January 2009 until 31 December 2011:

- the final withholding tax rate imposed on foreign institutional investors is reduced from 20% to 10%
- the withholding tax rate on non-corporate investors including resident and non-resident individuals is reduced from 15% to 10%.

**Public Ruling No 7/2012 — Taxation of Unit Holders of Real Estate Investment Trusts [REITs]/Property Trust Funds [PTFs]**

The Ruling explains the tax treatment of the income distributed by REITs/PTFs to their unitholders. Essentially:

- unitholders are taxed in the year of assessment the distribution is received.
- there are three types of income distributed by REITs/PTFs, and the tax treatment varies accordingly:
  - Income that is exempted at the REIT/PTF level. A REIT/PTF which distributes at least 90% of its total income in a basis year is exempted from tax for that year. However, this income would still be taxable in the hands of the unitholders, and there is no credit (as per s 110(9A) of the Income Tax Act) available to be offset against the tax imposed.
  - Income that has been taxed at the REIT/PTF level. Such income would also be taxable in the hands of the unitholders, but a credit (as per s 110(9A)) is available to be offset against the tax imposed.
  - Tax-exempt income received by REITs/PTFs and which is subsequently distributed to unitholders continues to be exempt in the hands of these unitholders.
- Unitholders are taxed based on their residence status

**Public Ruling 8/2012 — Real Estate Investment Trusts/Property Trust Funds — an overview**

This Ruling provides a general description of REITs, PTFs and Islamic REITs in Malaysia, as well as their regulatory framework. Noteworthy is the guidance provided on the special tax treatment accorded to the rental income received by REITs/PTFs, the exemption of REIT/PTF income and the treatment of rental income of a unit trust.

It explains that Islamic REITs are similar to conventional REITs/PTFs except that the Islamic REITs invest through *Syariah*-compliant capital market instruments. For the establishment of Islamic REITs, a person must observe and comply with both the requirements under the guidelines for Islamic REITs and the guidelines on REITs.

Paragraph 7 of the Ruling sets out the key features and structure of conventional REITs/PTFs and Islamic REITs. It illustrates the types of authorised investment activities as follows:

Types of authorised investment activities	
Conventional REITs/PTFs	Islamic REITs
• Real estate	• Acquiring real estate with existing clients
• Multi-purpose companies	• Investment, deposits and financing for Islamic REITs
• Real estate-related assets	• Insurance
• Non-real estate-related assets	• Forward sales or purchases of currency for risk management
• Cash, deposits, and money market instruments	
• Investments in foreign real estate and markets	

It also sets out non-permissible activities of conventional and Islamic REITs.

The Ruling also explains the difference between the tax treatment of rental income for a REIT/PTF and rental income from a unit trust. Rental income received by the REIT/PTF would be treated as business income, subject to certain restrictions. Details on the restrictions are further discussed in Public Ruling No 9/2012 on Taxation of Real Estate Investment Trusts/Property Trust Funds. Rental income of other property trusts is treated as s 4(d) income, with special deductions available under s 63A and 63.

**Public Ruling No 9/2012 — Taxation of Real Estate Investment Trusts/Property Trust Funds**

The IRB issued Public Ruling No 9/2012 on the taxation of real estate investment trusts/property trust funds on 26 November 2012. The Ruling provides guidance on the tax treatment of approved REITs and PTFs. REITs and PTFs are accorded special treatment on the rental income received. Pursuant to s 63C of the ITA, the rental income received by REITs and PTFs from their real property investments is treated as business income. However, the deductible expenses are restricted to the gross rental income, ie any excess expenditure is lost and may not be carried forward. Likewise, REITs and PTFs may claim capital allowances, but the claims are restricted to the adjusted rental income available. Any excess capital allowance may not be carried forward.

later than 2 July 2015) verified by the Small and Medium Enterprises Corporation Malaysia. The exemption is applicable for a period of five consecutive years of assessment commencing from the date the acquisition is completed. A qualifying company may nevertheless be disqualified from the exemption in certain specified circumstances (ie circumstances similar to those stated in the exemption order above).

- **Stamp Duty (Exemption) (No 11) Order 2013**

Please see ¶18-400.

### ¶13-880 Tax incentives in respect of Tun Razak Exchange

The following rules and orders were gazetted on 31 January 2013 in respect of the Tun Razak Exchange (TRX):

- The Income Tax (Industrial Building Allowance) (Tun Razak Exchange Marquee Status Company) Rules 2013, under which companies using qualifying buildings will be able to claim an industrial building allowance of 10% per year. The Rules provide guidance as to the determination of an industrial building. The above Rules take effect from YA 2014.
- Income Tax (Exemption) (No 4) Order 2013, under which approved developers would be entitled to an income tax exemption on 70% of the statutory income derived from:
  - (i) the disposal of any building, or rights over any building or part of a building for up to five years of assessment, and
  - (ii) the rental of a building or part of a building for up to five years of assessment.

The above Order is effective from YA 2013 until YA 2022 for (i) above and until YA 2027 for (ii).

- The Income Tax (Accelerated Capital Allowance) (Tun Razak Exchange Marquee Status Company) Rules 2013, under which a TRX Marquee status company is entitled to claim an accelerated capital allowance on the renovation costs incurred at an initial rate of 20% and an annual rate of 40%. The above Rules take effect from 1 January 2014 until 31 December 2020.
- The Income Tax (Deduction for Relocation Costs for Tun Razak Exchange Marquee Status Company) Rules 2013, under which a TRX Marquee status company is entitled to deduct the relocation costs incurred, provided that the relocation takes place before 31 December 2020.

The above Rules take effect from YA 2014.

- The Income Tax (Deduction for Rental Payments) (Tun Razak Exchange Marquee Status Company) Rules 2013, under which a TRX Marquee status company is allowed an additional deduction of 50% of the rental payments incurred in respect of a rented building used for the purposes of its business in

the TRX. The deduction may only be claimed for up to 10 years of assessment, and it expires on 31 December 2020. The above Rules take effect from YA 2014.

- The Stamp Duty (Exemption) Order 2013, under which the stamp duty that is chargeable on a service agreement executed between 1 January 2014 and 31 December 2022, and between a service provider and a TRX Marquee status company, is exempted. The above Order is effective from 1 January 2014.
- The Stamp Duty (Exemption) (No 2) Order 2013, under which the stamp duty chargeable on the following is exempted:

- (i) Any instrument of transfer for the purchase of commercial property by a TRX Marquee status company.
- (ii) Any loan agreement executed between a TRX Marquee status company named in the sale and purchase agreement (S & P) and a bank or financial institution to finance the purchase of a commercial property, provided that the S & P and the loan agreement are both executed between 31 January 2013 and 31 December 2020. The exemption from the stamp duty shall be given to the first owner of that commercial property, and
- (iii) Any lease or agreement for lease of any commercial property entered into by a TRX Marquee status company, provided that the lease agreement for the commercial property is executed between 31 January 2013 and December 2022, and the exemption shall be granted to the first lessee of the property. The above Order is effective from 31 January 2013.

#### TRX Marquee status company

A TRX Marquee status company means:

- an institution licensed under the *Banking and Financial Institutions Act 1989* carrying on a banking business or a merchant banking business, or a related company within the same group
- a company licensed under the *Insurance Act 1996* carrying on an insurance business, or a related company within the same group
- a company licensed under the *Islamic Banking Act 1983* carrying on an Islamic banking business, or a related company within the same group
- a company registered under the *Takaful Act 1984* carrying on a *takaful* business, or a related company within the same group
- a company holding a capital markets service licence
- a person, other than an individual, that is a registered person under the *Capital Markets and Services Act 2007*, which is approved by the Minister of Finance.

for income tax purposes. However, the fact that the return is not at a fair market rate interest is also relevant. It is learnt, however, that the authorities are of the view that the compensation would not be taxable. This is expected to be confirmed in a dialogue with the professional bodies.

Law: s 111, 111D.

## ¶14-420 Instalment payments

Individuals (other than employed individuals who already have tax deducted from their salaries) and companies are required from 1 January 1989 to pay tax under an instalment payment scheme. (See further ¶1-900, ¶2-800 and ¶14-120.)

### Taxpayers affected

Section 107B introduced a scheme for compulsory payment of tax by instalments covering all taxpayers other than individual taxpayers who are already paying tax under the deduction scheme for employees. In the case of individual taxpayers, only those with estimated tax liability of RM1,000 or more will be included in this scheme. Where separate assessments are issued to husband and wife, the RM1,000 threshold will apply to each individual.

The estimated tax payable by instalments in 2014 (for YA 2014) is based on the tax payable in YA 2013.

All taxpayers included in this scheme are issued the Notices of Instalment Payment.

### Method of instalment payments

The Notice of Instalment Payment will show the scheme for each taxpayer requiring him/her to make six bimonthly payments beginning from the month of March to the month of January in the following year. The due date for each payment will be the 1<sup>st</sup> of the relevant month.

### Request for variation of instalment payments

Any request for variation of instalment payments must be made not later than 30 June each year. Requests for changes will only be granted in respect of the amount of each instalment; changes in due date(s) will not be granted.

### Penalties

If an instalment payment is not made within 30 days from the due date, a penalty of 10% on that instalment will be imposed automatically by the computer. The notice of late payment penalty will only be issued after the date of the final instalment.

Where an approval is given to change the amount of the instalment and the tax payable for a year of assessment exceeds the total of the instalments payable, then the difference which exceeds 30% of the tax payable is liable to a penalty of 10%.

## Example 1

Puan Amelia received the Notice of Instalment Payment (CP 500) in February 2014 and the instalment payments for the year 2013/2014 in respect of the tax liability for YA 2013 were as follows:

Instalment*	Due date	RM
1	1 March 2013	40,000
2	1 May 2013	40,000
3	1 July 2013	40,000
4	1 September 2013	40,000
5	1 November 2013	40,000
6	1 January 2014	40,000
		<u>240,000</u>

Puan Amelia paid the third instalment on 16 August 2013 although the due date was 1 July 2013. If the instalment was settled within 30 days of the due date, ie on or before 30 July 2013, no penalty would be imposed. However, since the instalment was paid on 16 August 2013, the penalty would be computed as follows:

$$10\% \text{ penalty on RM40,000} = \text{RM4,000}$$

## Example 2

The IRB issued a Notice of Instalment Payment to Encik Ahmad in February 2013 with an estimated tax liability for YA 2013 of RM300,000. However, according to his company's estimate, the estimated tax liability for YA 2013 was only RM100,000. As such, in June 2013, the company requested the IRB to revise the instalment payments. Later, upon submission of the tax return, it was found that the actual tax liability was RM180,000. The penalty for the excessive difference in the tax payable would be computed as follows:

	RM
Actual tax payable for YA 2013	180,000
Total instalment payments requested by the company	<u>(100,000)</u>
Difference	80,000
30% of actual tax payable (30% of RM180,000)	<u>(54,000)</u>
	26,000
Penalty (RM26,000 @ 10%)	<u>2,600</u>

### Remission of penalties imposed

On 2 September 2008, the IRB issued Guideline 3/2008 on "Remission of Increase in Tax" to provide clarification on the circumstances in which a remission of penalties imposed may be considered. An appeal may be allowed in writing to the Collection Branch/Collection Unit of the IRB branch whereby it will be considered on a case by case basis depending on the merit of each case. Either a full or partial remission may be granted.

A full remission may be given under the following circumstances:

- it is proven that payment was made within the stipulated period
- extension of time for payment had been granted

### ¶15-520 Exchange of information

The article on exchange of information is one of great importance although it remains largely unused. Exchange of information may be of two types:

- Information which should flow between treaty countries automatically and periodically. It should cover any domestic changes in tax laws relating to dividends, interest, rentals, royalties, salaries, etc, in the treaty countries.
- Information on the basis of specific requests on issues expressly stated in such requests. The treaty country requesting the information has to prove that it has a valid tax interest in making the request and data must concern a specific and identified taxpayer.

This article only concerns the tax authorities of the treaty countries. Taxpayers in themselves are not concerned with the provisions of this article. In all Malaysian treaties, there is an article which embodies the rules under which information may be exchanged between the competent authorities of the contracting countries. There are good reasons for the inclusion of an article such as this. Some of these reasons are:

- it lays a proper basis for implementing the domestic laws of the Contracting State
- it can prevent transfer pricing, tax evasion and tax avoidance, and
- it provides an effective means of applying the specific provisions of the tax treaty.

The situations in which information can be obtained under an exchange of information article are:

- when applying the article to royalties (or interest or rents), Country A (where the beneficiary of the royalty is resident) asks Country B (where the payer is resident) for information concerning the royalty transmitted
- where an allocation of profits and expenditure has to be made when taxing business profits, an exchange of information between the Contracting States would be of great use, and
- when information on matters relating to assessments, collection of taxes, etc, is required.

This article also provides that the competent authorities must treat the information obtained as secret in the receiving State. The information exchanged remains secret and is not to be disclosed to any person other than those, including a court, concerned with the enforcement, assessment, collection of taxes or determination of tax appeals. A treaty country is not obliged to disclose any business, industrial or professional secrets.

### ¶15-530 Miscellaneous

Other articles in Malaysia agreements pertain to:

- the preservation of consular and diplomatic fiscal privileges
- territorial extension — this would cater for the extension of the agreement to a territory whose international relations are the responsibility of one of the Contracting States; eg the agreement with Denmark does not extend to the Faroe Islands and Greenland

- the date on which the agreement becomes effective, and
- the procedures for the termination of the agreement.

### ¶15-540 Limitation where remittance basis applies

In all the Malaysian treaties limit relief available where income assessable on a remittance basis is not remitted. A situation can arise where a country normally levies a withholding tax of 30% but reduces this to 10% under the terms of its treaty with Malaysia. However, that country will feel cheated if it knows that the individual is able to avoid paying any Malaysian tax simply by not remitting it to Malaysia. The treaty would, therefore, provide that, only if the royalty is remitted to Malaysia and consequently taxable there, would the reduced withholding tax be available.

## RELIEF PROVISIONS

### ¶15-600 Different tax reliefs

All double taxation agreements contain a variety of relief provisions geared to achieving the maximum tax neutrality between the Contracting States. Unilateral and treaty provisions usually provide the following main types of relief.

#### Tax credits

This is simply a credit given to a taxpayer's domestic tax bill in respect of foreign tax suffered by him/her on the same income. But there is a limit. A taxpayer is not allowed, as a credit, all the foreign tax, if it has been charged at a higher rate than the one charged by his/her home country. The underlying logic here is that one is left to pay world tax at whichever is the higher of the two rates — at home or abroad.

The following general rules apply where the credit method is used:

- To avail oneself of the credit for tax paid in a foreign country, the foreign income must be declared locally. This can lead to additional tax payable locally, should the local rate of tax exceed that suffered in the foreign country.
- Credit is only given in respect of tax paid on income in the foreign country or in respect of taxes paid which are of a similar character to taxes levied in the home country.
- Foreign tax credit is restricted to the lesser of tax paid locally on foreign income or the actual amount of foreign tax suffered.
- The allocation of home country expenses between home source income and foreign source income by the authorities of the home country can increase domestic tax and affect the foreign tax credit available.
- Credit for indirect foreign tax is given where it is so provided in the treaty. That is to say, not only is credit available on taxes withheld from dividends paid, but also for the underlying corporate income tax suffered by the overseas company in relation to the profits out of which the dividend is paid. This credit is extended to corporate entities which receive dividends from foreign subsidiaries in which they own a minimum shareholding, often 10% to 25%.

### ¶17-320 Treatment of gifts

Paragraph 12 of Sch 2 deals with gifts of assets which are subject to RPGT. It is provided that, where a gift is made and the donor and the donee are related, ie husband and wife, parent and child or grandparent and grandchild, the donor is deemed, without having to make an election, to have received no gain and suffered no loss and is therefore exempted from RPGT. In so far as the donee is concerned, since he/she will have acquired the asset, his/her acquisition price will be equal to the sum total of the donor's acquisition price plus all the permitted expenses (see ¶17-250).

Where the asset is acquired as a gift on death, the recipient is deemed to acquire the asset at its market value as at the date of transfer of ownership of the asset to the recipient.

#### Example

Hassan gave his daughter, Aidah, on 11 November 2014 one of his properties which he purchased on 1 August 2007 for RM180,000. The permitted expenses amounted to RM3,000. Since it was a gift from the parent to his child, there would be no chargeable gain or allowable loss from the transfer of the above property.

Disposal price deemed to be (RM180,000 + RM3,000)		RM183,000
Less: Acquisition price	RM180,000	
Add: Permitted expenses	RM3,000	(RM183,000)
Chargeable gain/allowable loss		Nil

The acquisition price to Aidah would therefore be RM183,000 which is the disposal price to Hassan.

Had Aidah obtained the property as a gift on the death of Hassan, the acquisition price to Aidah would have been the market value as at the date of transfer of ownership of the property to Aidah.

Law: Sch 2 para 12, 19(1).

### ¶17-340 Disposal price deemed to be acquisition price

In the following cases, the disposal price shall be deemed to be equal to the acquisition price:

- the devolution of the assets of a deceased person on his/her executor or legatee under a will or intestacy or on the trustees of a trust created under his/her will
- the transfer of assets between spouses
- the transfer of assets owned by an individual or his wife, or by an individual jointly with his wife or a connected person, to a company controlled by the individual and/or his wife or a connected person for a consideration consisting wholly or substantially of shares in the company; an individual can be in control of a company where the subscribers of the company's shares hold the shares in trust for him (*HJBK v DGIR* (1989) 1 MSTC 376)

- acquisition from or disposal to a nominee or trustee resident in Malaysia by an individual or his wife or by both
- conveyance or transfer by way of security
- gifts made to the Government, a State Government, a local authority or a charity exempt from Malaysian income tax
- the disposal of an asset as a result of a compulsory acquisition under any law, and
- the disposal of an asset by a person to an Islamic bank under a scheme where that person is financed by such a bank in accordance with the *Syariah* principle.

The above-stated situations will result in a "no gain, no loss" transfer.

Law: Sch 2.

### ¶17-360 Disposer and acquirer

Section 13(1) requires the disposer and the acquirer to make a return to the Director General within 60 days (one month prior to 1 January 2010) of disposal:

- specifying the acquisition price, the disposal price and the gain or loss on disposal of the asset
- furnishing all relevant information necessary for the determination of the acquisition price and the disposal price of the asset, and
- submitting a written valuation of the asset by a valuer, where the disposal is related to the market value.

Where there is disposal of an asset subject to RPGT, the acquirer is required to retain the whole of the money consideration or a sum not exceeding 5% (2% with effect from 1 January 2010) of the total value of the consideration, whichever is the lesser, until he/she receives the Director General's certificate of clearance. With effect from 1 January 2010, the acquirer shall now retain a sum not exceeding 2% of the total consideration and remit the same to the Director General within 60 days after the date of disposal except the following situations:

- (1) disposal of a real property or shares in a real property company which have been held for more than five years, or
- (2) disposal of a private residence by an individual who is a citizen or a permanent resident where an election for the exemption under s 8 of the RPGT Act 1976 has been made (for the purpose of this exemption, any private residence owned and occupied by an individual's wife is deemed to be owned and occupied by the individual), or
- (3) disposal of a real property or shares in a real property company at a loss, or
- (4) disposal of a real property or shares in a real property company to a Real Estate Investment Trust or a Property Trust Fund approved by the Securities Commission under Real Property Gains Tax (Exemption) (No 4) Order 2003.