

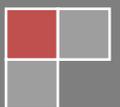
2013

TAX AUDIT FRAMEWORK INLAND REVENUE BOARD OF MALAYSIA

SECTION I:
TAX AUDIT FRAMEWORK

SECTION II:
PETROLEUM TAX AUDIT FRAMEWORK

SECTION III:
TRANSFER PRICING AUDIT FRAMEWORK





INLAND REVENUE BOARD OF MALAYSIA

TAX AUDIT FRAMEWORK

EFFECTIVE DATE: 01 APRIL 2013

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1. INTRODUCTION

- 1.1 A fair, transparent and equitable tax administration system will enhance public confidence in the tax system. Compliance with tax laws must be strictly enforced and tax offences such as non-compliance and tax evasion should be penalized in accordance with the provisions of the Income Tax Act 1967 (ITA).
- 1.2 Under the Self-Assessment System, tax audit is a primary activity of the Inland Revenue Board of Malaysia (IRBM). It is aimed at enhancing voluntary compliance with the tax laws and regulations. A taxpayer can be selected for an audit at any time. However, it does not necessarily mean that a taxpayer who is selected for an audit has committed an offence.
- 1.3 This framework is issued by IRBM to ensure that tax audit is carried out in a fair, transparent and impartial manner. This framework outlines the rights and responsibilities of audit officers, taxpayers and tax agents in respect of a tax audit. Generally, this framework aims to:
 - 1.3.1 Assist audit officers to carry out their tasks efficiently and effectively; and
 - 1.3.2 Assist taxpayers in fulfilling their obligations.

2. STATUTORY PROVISIONS

- 2.1 The provisions of the ITA which are applicable to tax audits are as follows:
 - 2.1.1 Section 78: Power to call for specific returns and production of books.
 - 2.1.2 Section 79: Power to call for statement of bank accounts, etc.
 - 2.1.3 Section 80: Power of access to buildings and documents, etc.
 - 2.1.4 Section 81: Power to call for information.

- 2.1.5 Section 82: Duty to keep records and give receipts.
 - 2.1.6 Section 99: Right of appeal.
 - 2.1.7 Section 100: Extension of time for appeal.
 - 2.1.8 Section 101: Review by Director General
 - 2.1.9 Section 102: Disposal of appeals.
 - 2.1.10 Section 113: Incorrect returns.
 - 2.1.11 Section 116: Obstruction of officers
 - 2.1.12 Section 119A: Failure to keep records.
 - 2.1.13 Section 120: Other offences.
 - 2.1.14 Section 138: Certain material to be treated as confidential.
 - 2.1.15 Section 138A: Public rulings.
 - 2.1.16 Section 140: Power to disregard certain transactions.
 - 2.1.17 Section 141: Powers regarding certain transactions by non-residents.
- 2.2 Statutory provisions relating to tax audit are not limited to the provisions cited above. Statutory provisions also include the ITA as a whole, Real Property Gains Tax Act 1976, Petroleum (Income Tax) Act 1967, Promotion of Investments Act 1986, Stamp Act 1949, Labuan Offshore Business Activity Tax Act 1990 and other acts administered by IRBM.

3. WHAT IS A TAX AUDIT?

- 3.1 A tax audit is an examination of a taxpayer's business records and financial affairs to ascertain that the right amount of income should be declared and the right amount of tax should be calculated and paid are in accordance with tax laws and regulations. IRBM carries out two (2) types of audit, namely desk audit and field audit.

3.1.1 Desk Audit

3.1.1.1 A desk audit is held at the IRBM's office. Desk audits are normally concerned with straightforward issues or tax adjustments which are easily dealt with via correspondence. A taxpayer may be called for an interview at IRBM's office if further information is required.

3.1.1.2 Generally, a desk audit involves checking all information on income and expenses as well as various types of claims made by a taxpayer in his income tax return.

3.1.1.3 Specific desk audit cases can be referred for field audit action. Under such circumstances, the taxpayer will be informed through a field audit notification letter as part of the normal process of commencing the field audit.

3.1.2 Field Audit

3.1.2.1 A field audit is one that takes place at a taxpayer's premise. It involves the examination of the taxpayer's business records. In the case of a sole-proprietorship or partnership, if the taxpayer's business records are incomplete it may involve the examination of non-business records such as personal bank statements, etc. A taxpayer will be given notice prior to a field audit.

3.2 In general, this tax audit framework is applicable to both types of audit, namely desk audit and field audit with the exception of visit to premises and examination of records which are only applicable to field audit.

4. OBJECTIVE OF TAX AUDIT

4.1 The main objective of tax audit is to encourage voluntary compliance with the tax laws and regulations and to ensure that a higher tax compliance rate is achieved under the Self Assessment System. In this regard, the audit officer is required to ensure that the correct amount of income has been reported and the right amount of tax has been paid in accordance with the tax laws and regulations.

4.2 For the purpose of achieving voluntary compliance, the tax audit activity is one of the measures undertaken by IRBM to educate and create

awareness of taxpayers towards their rights and responsibilities under the provisions of the ITA.

5. YEARS OF ASSESSMENT COVERED

- 5.1 Generally, a tax audit covers a period of one (1) year of assessment, determined in accordance with the audit focus criteria of the department.
- 5.2 However, the tax audit may be extended to cover a period up to five (5) years of assessment, pursuant to the issues uncovered during an audit. Further, this 5 year time limit is not applicable to cases involving fraud and tax evasion whether intentional or unintentional.

6. SELECTION OF CASES

- 6.1 Cases for audit are selected through the computerized system based on risk analysis criteria. However, the selection of audit cases is not confined to the selection by the computerized system only, as cases can also be selected based on information received from various sources.
- 6.2 Audit cases are selected in the following manner:
 - 6.2.1 Selection based on risk analysis;
 - 6.2.2 Information received from third party;
 - 6.2.3 Selection based on specific industries;
 - 6.2.4 Selection based on specific issues for a certain group of taxpayers;
and
 - 6.2.5 Selection based on location, etc.

7. HOW A TAX AUDIT IS CARRIED OUT

7.1 Audit Venue

- 7.1.1 A desk audit is carried out at the IRBM's office whereas a field audit is carried out at a taxpayer's business premise.
- 7.1.2 Where the business premises are not suitable, the taxpayer may suggest a suitable alternative for IRBM's agreement.

7.2 Commencement of an Audit

- 7.2.1 A taxpayer who is selected for an audit will be notified by IRBM through a letter of notification of audit. The period between the date of notification of audit and the audit visit is 14 days. However, with the agreement of the taxpayer, a shorter period of notification may be fixed by IRBM. A letter confirming the visit is usually preceded by a phone call.
- 7.2.2 A taxpayer may request for the audit visit to be deferred due to unavoidable circumstances and reasonable grounds.
- 7.2.3 Other than the intended date of the visit, the letter will indicate the records that should be made available for audit, the years of assessment to be audited and the names of audit officers who will conduct the audit as well as the expected time frame required for the audit visit.
- 7.2.4 A taxpayer may contact the Branch Audit Manager or Branch Director of IRBM for the purpose of confirming the audit visit.

7.3 The Visit

- 7.3.1 An audit visit is only applicable to the field audit activity. The audit normally starts off with an interview.
- 7.3.2 The purpose of an interview is to enable the audit officers to meet the taxpayer, obtain an overview of the taxpayer's business activity and to discuss the audit.
- 7.3.3 The taxpayer will be asked to explain his business activities, accounting and record keeping system. During the audit process, the person responsible for the handling of taxpayer's business records will also be interviewed.

7.4 Examination of Records

- 7.4.1 During the course of an audit, the audit officer should be allowed to examine all business records and to inspect stock and equipments physically for verification of the claims made. Records pertaining to the years of assessment which are already time barred will not be examined.

- 7.4.2 In certain circumstances, there may be a need to examine records other than business records where it involves the audit of sole-proprietorships and partnerships.
- 7.4.3 The audit officer will not search for or take possession of any record. Examination of records will only be carried out at the taxpayer's business premises. If it is deemed necessary, the audit officer should be allowed to make copies of relevant documents.
- 7.4.4 However, under circumstances where the work place provided by the taxpayer is not suitable or conducive to carry out the audit or where copier facility is not available, the audit officers, with the consent of the taxpayer, may obtain records for examination at the IRBM's office. In such a case, the documents will be returned to the taxpayer once the examination is done.
- 7.4.5 The documents and records to be taken back will be listed and the taxpayer may check the documents and records and make a copy of the list, if necessary.
- 7.4.6 Where records and books of accounts are kept in electronic form, hard copies of such records should be made available for examination. If at the time of the audit visit, the taxpayer is unable to provide the hard copies for examination, the taxpayer should facilitate and assist the audit officers to access the computer system and copy the electronic records onto tapes, disks or diskettes.
- 7.4.7 The audit officers will examine all documents and records necessary to ascertain that the correct amount of income has been reported. Basically, records consists of:

7.4.7.1 Business Records

Taxpayer can obtain guidance in relation to record keeping from the guidebook and public rulings issued by IRBM.

Pursuant to section 138A of the ITA, the Director General of Inland Revenue (DGIR) is given the power to issue public rulings on the interpretation of any provision of the ITA.

The following public rulings and a guide book in relation to record keeping have been issued;

- i. IRBM Public Ruling No. 4/2000: Keeping Sufficient Records (Companies & Co-operatives);
- ii. IRBM Public Ruling No. 5/2000: Keeping Sufficient Records (Individuals & Partnerships);
- iii. IRBM Public Ruling No. 6/2000: Keeping Sufficient Records (Persons Other Than Companies, Co-operatives or Individuals); and
- iv. STS-BK4: Self-Assessment – A Guide to Record Keeping For Business.

7.4.7.2 Records Other Than Business Records

In the audit of cases other than companies such as sole-proprietorships and partnerships, the audit officer may need to examine records other than business records as follows:

- i. Personal bank account statements;
- ii. Credit card statements;
- iii. Records relating to the ownership of assets;
- iv. Records relating to the taxpayer's personal / family expenses; and
- v. Other statements as may be required under section 79 of the ITA.

7.4.8 Section 82 and 82A of the ITA requires every person to keep and retain sufficient records when carrying on a business in order to enable the income or loss from the business to be readily ascertained. As stipulated in the Public Ruling Nos. 4/2000, 5/2000 and 6/2000, the meaning of "records and documents" includes the following:

7.4.8.1 Books of accounts for recording receipts and payments or income and expenditure;

7.4.8.2 Financial statements;

7.4.8.3 Invoices, vouchers, receipts and other documents that are required to verify entries recorded in the books of accounts; and

7.4.8.4 Documents, objects, materials, articles and things which are maintained and kept in the form of electronic medium.

7.4.8.5 Any other record as may be specified by the DGIR.

7.4.9 Failure to keep sufficient records is an offence under section 119A of the ITA. In relation to this, the audit officer may apply alternative approaches or indirect methods for the purpose of ascertaining whether the appropriate amount of income has been reported.

7.5 Audit Time frame

7.5.1 The time required to complete an on-site examination of records is between one (1) to three (3) days. However, the audit time frame may be extended depending on the following factors:

7.5.1.1 The size of the business and the complexity of business transactions;

7.5.1.2 The form in which records are kept; or

7.5.1.3 The extent of co-operation from the taxpayer.

7.5.2 The audit time frame is applicable only to field audits.

7.6 Settlement of Audit

7.6.1 After concluding the audit work, the audit officer will prepare an audit findings report for approval by the Branch Audit Manager.

7.6.2 Under certain circumstances, the taxpayer is required to be present at the IRBM's office for discussion on the proposed tax adjustments. The audit officer, together with at least one senior audit officer, shall discuss the proposed adjustments with the taxpayer.

7.6.3 The taxpayer, without being called by the IRBM, may be present at IRBM's office to seek clarification regarding the progress of the

audit process or to give further information to expedite the settlement of the audit.

7.6.4 The taxpayer will be informed of the audit findings which will cover the following areas:

7.6.4.1 Audit issues raised;

7.6.4.2 Reasons and rationale for raising the audit issues;

7.6.4.3 The amount of proposed tax adjustments (if any) and the years of assessment involved.

7.6.5 If there are tax adjustments to be made, a notification with details of proposed tax adjustments and rationale for making such adjustments will be issued. The taxpayer will be given the opportunity to state his views and give explanations on the audit findings and the proposed tax adjustments forwarded.

7.6.6 A taxpayer is allowed 21 days from the date of notification of proposed tax adjustments to file an official objection if he disagrees with the proposed tax adjustments. Additional information and copies of evidence should be provided to support his objection.

7.6.7 If no objection is made within 21 days from the date of notification of proposed tax adjustments, the taxpayer shall be deemed to have agreed to the proposed tax adjustments or where an objection is found to have no basis in accordance with the provisions of the ITA, the taxpayer will be informed accordingly.

7.6.8 Subsequently, a notice of additional assessment with appropriate penalty imposed under subsection 113 (2) or paragraph 44B (7) (b) or subsection 112(3) of the ITA or a notification of non-chargeability to tax will be issued. However, if there is no adjustment, a letter will be issued to inform that the audit has been finalized without any adjustment.

7.6.9 The time frame for settlement of a tax audit should be 3 months from the commencement of the audit. IRBM will inform the taxpayer on the progress of the audit in the event that the case needs more than 3 months to settle.

- 7.6.10 Once the audit case is settled, the audit should not be repeated on the same issues for the same year of assessment. However, if there are new issues to be pursued or new information is received, an audit can be repeated for the same year of assessment.

8. RIGHTS AND RESPONSIBILITIES

8.1 IRBM

- 8.1.1 An audit officer must adhere to rules and codes of ethics drawn up by IRBM and is required to carry out his duties in the following manner:
- 8.1.1.1 Professional, well mannered, trustworthy, honest and with integrity;
 - 8.1.1.2 Always ready to give explanations on the objectives of the tax audit and the rights and responsibilities of the taxpayer;
 - 8.1.1.3 Knowledgeable and fair in administering tax laws;
 - 8.1.1.4 Co-operative and always ready to give advice and guidance to the taxpayer;
 - 8.1.1.5 Ensure that the audit is carried out smoothly with minimal disruption to the taxpayer;
 - 8.1.1.6 Request for documents, books of accounts and information that are relevant to the audit only;
 - 8.1.1.7 Explain the proposed tax adjustments and provide reasonable time for taxpayer to give responses on issues raised;
 - 8.1.1.8 Ensure the rights and interest of taxpayers and tax agents as well as documents of taxpayers are safeguarded;
- 8.1.2 Identification of an audit officer
- 8.1.2.1 Each audit officer is issued with an authority card bearing his name and photograph. The card also carries

a statement that the officer is authorized to examine books of accounts, documents and records at the taxpayer's premises;

8.1.2.2 Taxpayers are advised to view the authority cards in order to verify the authenticity of audit officers; and

8.1.2.3 Taxpayers are advised to check with the Branch Director of IRBM if they have doubts on the authenticity of audit officers.

8.1.3 An audit officer is prohibited from:

8.1.3.1 Having any personal or financial interest in the business of a taxpayer being audited;

8.1.3.2 Recommending to taxpayer that a certain tax agent be appointed as the tax agent for the audit case; and

8.1.3.3 Abusing his position or power in carrying out his duties as provided under section 118 of the ITA.

8.2 Taxpayer

8.2.1 Responsibilities of a taxpayer

8.2.1.1 Be co-operative, well mannered, fair, honest and with integrity;

8.2.1.2 Provide reasonable facilities and assistance to enable the audit officer to carry out his duties as outlined in Public Ruling No. 7/2000 which includes the following:

i. Giving access to the audit officer to his business premises, providing information and making available documents and records required for examination;

ii. Giving explanation regarding the business, the accounting and information systems;

iii. Giving permission to examine and make copies of records, documents and books of accounts whether in the physical and / or electronic medium;

- iv. Assisting in the provision of or providing access to records, documents and books of accounts in the physical and / or electronic medium; and
 - v. Allowing the use of copiers, telephone or other communication equipment, lighting and power, office space, furniture and providing facilities for copying of electronic records onto tapes, disks or diskettes.
- 8.2.1.3 Co-operate in providing complete responses to all queries:
- i. If questions posed are ambiguous, he may seek clarification from the audit officer;
 - ii. Questions posed normally relate to the business carried out. However, in the case of a sole proprietorship or a partnership, the taxpayer may also be queried on personal matters such as personal expenses, savings, bank account, assets, etc; and
 - iii. If a taxpayer fails to co-operate and provide the required information, he shall be deemed to have committed an offence under the provisions of the ITA.
- 8.2.2 The taxpayer is prohibited from:
- 8.2.2.1 Giving any form of gifts to the audit officer and transacting any business with the audit officer during the audit process;
 - 8.2.2.2 Making any form of payments to the audit officer; and
 - 8.2.2.3 Obstructing or hindering the audit officer in the exercise of his functions. Such obstruction is an offence under section 116 of the ITA. Obstruction includes the following:
 - i. Obstructing or refusing an audit officer from entering lands, buildings, places and premises to perform his duties in accordance with section 80 of the ITA;
 - ii. Obstructing an audit officer from performing his functions and duties under the provisions of the ITA;

- iii. Refusing to provide books of accounts, or other documents in the custody of or under his control when required by the audit officer;
- iv. Failing to provide reasonable assistance to the audit officer in carrying out his duties; and
- v. Refusing to answer or give responses to questions raised during the course of an audit.

8.3 Tax Agent / Representative

- 8.3.1 The taxpayer can request for his tax agent to be present during an interview. The taxpayer is allowed to bring an interpreter to an interview or discussion session if the taxpayer is not conversant in Bahasa Malaysia or English.
- 8.3.2 If a taxpayer appoints a new tax agent to handle his audit case, he should submit a copy of the letter of appointment.
- 8.3.3 The conduct of a tax agent is governed by the code of ethics formulated by IRBM based on the principles of integrity, accountability, transparency and social responsibility.
- 8.3.4 The tax agent is required to carry out his duties in the following manner:
 - 8.3.4.1 Professional, be fully conversant with tax laws and practices and with integrity;
 - 8.3.4.2 Be honest, trustworthy, transparent and give fullest co-operation when dealing with the taxpayer and IRBM such as informing IRBM on ceasing to be the tax agent of a taxpayer and adhere to rules and guidelines laid down by IRBM;
 - 8.3.4.3 Refrain from misusing information acquired or abusing his position as a tax agent for his own personal advantage;
 - 8.3.4.4 Always give complete and accurate feedback relating to the progress of an audit and advise the taxpayer accurately based on the true facts of the audit case; and

8.3.4.5 Safeguard the confidentiality of all information and ensure that the information is not disclosed to any unauthorized party (subsection 138 (5) of the ITA).

8.3.5 The tax agent is prohibited from:

8.3.5.1 Giving wrong advice to taxpayers and collaborating with taxpayers to avoid paying the correct amount of taxes;

8.3.5.2 Delaying the work of a tax audit or acting irresponsibly towards his entrusted duties; and

8.3.5.3 Offering any form of gifts to the audit officers.

9. CONFIDENTIALITY OF INFORMATION

IRBM will ensure confidentiality of all information obtained from the taxpayer during an interview, discussion, through correspondence or examination of records and that it is utilized for tax purposes only.

10. OFFENCES AND PENALTIES

10.1 If it is discovered after the commencement an audit that there has been an understatement or omission of income, a penalty will be imposed under subsection 113(2) or paragraph 44B(7)(b)* of the ITA in which the penalty rate equal to the amount of tax undercharged (100%) accordingly. However, the DGIR in exercising his discretionary powers may consider a lower penalty of 45% to be imposed.

10.2 The concessionary penalty rates may be imposed in cases where the taxpayer makes a voluntary disclosure. As such the taxpayer is encouraged to make a voluntary disclosure regarding the omitted income before the commencement of an audit. This disclosure must be made in writing to the relevant Branch Director of IRBM.

10.3 Where taxpayer who furnishes a return form on or before the due date and the Director General has made an assessment for that year of assessment under subsection 91, ITA 1967 subsequently makes a voluntary disclosure after the due date but not later than 6 months from the due date, the penalty rates are as follows:

Table I

Period of making voluntary disclosure	Rate
Within 60 days from the due date for furnishing the return form	10%
More than 60 days but not later than 6 months from the due date for furnishing the return form	15.5%

* Paragraph 44B (7) (b) is deemed to have effect for the years of assessment 2008, 2009 and 2010.

- 10.4 The concessionary penalty rates for voluntary disclosure other than cases mentioned in paragraph 10.3 are as follows:

Table II

	Period from the due date of submitting return form	Rate
Voluntary disclosure before case is selected for audit.	Up to 6 months	Table I applies
	> 6 months to 1 year	20%
	> 1 year to 3 years	25%
	> 3 years and above	30%
<u>Field Audit</u> Voluntary disclosure after taxpayer has been informed but before commencement of examination of documents during audit visit.	Not applicable	35%
<u>Desk Audit</u> Voluntary disclosure after letter of request for documents is issued to taxpayer but before the commencement of examination of documents submitted.		

11. COMPLAINTS

- 11.1 If the taxpayer is dissatisfied with the manner in which an audit is being carried out, including the behaviour of an audit officer, he may make an official complaint to the IRBM Branch Director / State Director / Director of Compliance Department / Deputy Director General of Inland Revenue / Director General of Inland Revenue.
- 11.2 IRBM will act fairly, objectively and impartially on all complaints received.
- 11.3 IRBM will not entertain any complaint which is found to have no basis and not made in good faith.
- 11.4 IRBM will take action and file a complaint with the relevant authority such as Ministry of Finance / Malaysian Institute of Taxation / Malaysian Institute of Accountants / Malaysian Institute of Certified Public Accountants / Malaysian Association of Tax Agents / Bar Council, if tax agents or their representatives do not co-operate or behave unprofessionally which is inconsistent with their code of ethics.

12. PAYMENT PROCEDURES

- 12.1 Any taxes and penalties to be paid arising out of an audit must be made to the DGIR through any appointed bank or any Collection Branch of IRBM.
- 12.2 The taxpayer is required to make full payment of taxes and penalties arising out of an audit.
- 12.3 If the taxpayer is unable to make full payment of tax, IRBM may consider the taxpayer's application for settling the total tax liability by installments, for a predetermined period.
- 12.4 Application for installment payment scheme should be submitted to the relevant Branch Director of IRBM for approval.
- 12.5 Where a taxpayer fails to adhere to the installment payment scheme agreed upon, late payment penalty on the balance of tax outstanding will be imposed.

13. APPEALS

Section 99 to 102 of the ITA lay the ground rules for appeals relating to assessment raised by IRBM.

13.1 A taxpayer can appeal against an assessment as a result of a tax audit.

13.2 The appeal must be made to the Special Commissioners of Income Tax within 30 days after the service of the notice of additional assessment.

13.3 Should either party be dissatisfied with the decision of the Special Commissioners of Income Tax, the aggrieved party may apply to have the case heard in the High Court and further the Court of Appeal.

14. EFFECTIVE DATE

This framework is effective from 1 April 2013 and not applicable to audit cases involving transfer pricing, thin capitalization and advance pricing arrangement. This tax audit framework shall replace the tax audit framework issued in January 2009.

**Director General of Inland Revenue
Malaysia**

April 2013



INLAND REVENUE BORAD OF MALAYSIA

PETROLEUM TAX AUDIT FRAMEWORK

EFFECTIVE DATE: 01 APRIL 2013

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1. INTRODUCTION

- 1.1 A fair, transparent and equitable tax administration system will enhance public confidence in the tax system. Compliance with tax laws must be strictly enforced and tax offences such as non-compliance and tax evasion should be penalized in accordance with the provisions of the Petroleum (Income Tax) Act 1967 (PITA).
- 1.2 Under the Self-Assessment System, tax audit is a primary activity of the Inland Revenue Board of Malaysia (IRBM). It is aimed at enhancing voluntary compliance with the tax laws and regulations. A taxpayer can be selected for an audit at any time. However, it does not necessarily mean that a taxpayer who is selected for an audit has committed an offence.
- 1.3 This framework is issued by IRBM to ensure that tax audit is carried out in a fair, transparent and impartial manner. This framework outlines the rights and responsibilities of audit officers, taxpayers and tax agents in respect of a tax audit. Generally, this framework aims to:
 - 1.3.1 Assist audit officers to carry out their tasks efficiently and effectively; and
 - 1.3.2 Assist taxpayers in fulfilling their obligations.

2. STATUTORY PROVISIONS

- 2.1 The provisions of the PITA which are applicable to tax audits are as follows:
 - 2.1.1 Section 31: Power to call for specific returns and production of books.
 - 2.1.2 Section 32: Power to call for statement of bank accounts, etc.
 - 2.1.3 Section 33: Power of access to buildings and documents, etc.
 - 2.1.4 Section 34: Power to call for information
 - 2.1.5 Section 34A: Duty to keep records.
 - 2.1.6 Section 43: Right of appeal
 - 2.1.7 Section 44: Extension of time for appeal

- 2.1.8 Section 45: Review by Director General
 - 2.1.9 Section 46: Disposal of appeals
 - 2.1.10 Section 51: Failure to furnish return
 - 2.1.11 Section 52: Incorrect returns
 - 2.1.12 Section 54: Obstruction of officers
 - 2.1.13 Section 58: Other offences
 - 2.1.14 Section 71: Certain materials to be treated as confidential
 - 2.1.15 Section 72: Power to disregard certain transactions
- 2.2 Statutory provisions relating to tax audit are not limited to the provisions cited above. Statutory provisions also include the Petroleum (Income Tax) Act 1967 as a whole.

3. WHAT IS A TAX AUDIT?

- 3.1 A tax audit is an examination of a taxpayer's business records and financial affairs to ascertain that the right amount of income should be declared and the right amount of tax should be calculated and paid are in accordance with tax laws and regulations. IRBM carries out two (2) types of audit, namely desk audit and field audit.

3.1.1 Desk Audit

3.1.1.1 A desk audit is held at the IRBM's office. Desk audits are normally concerned with straightforward issues or tax adjustments which are easily dealt with via correspondence. A taxpayer may be called for an interview at IRBM's office if further information is required.

3.1.1.2 Generally, a desk audit involves checking all information on income and expenses as well as various types of claims made by a taxpayer in his income tax return.

3.1.1.3 Specific desk audit cases can be referred for field audit action. Under such circumstances, the taxpayer will be

informed through a field audit notification letter as part of the normal process of commencing the field audit.

3.1.2 Field Audit

3.1.2.1 A field audit is one that takes place at a taxpayer's premise. It involves the examination of the taxpayer's business records. A taxpayer will be given notice prior to a field audit.

3.2 In general, this tax audit framework is applicable to both types of audit, namely desk audit and field audit with the exception of visit to premises and examination of records which are only applicable to field audit.

4. OBJECTIVE OF TAX AUDIT

4.1 The main objective of tax audit is to encourage voluntary compliance with the tax laws and regulations and to ensure that a higher tax compliance rate is achieved under the Self Assessment System. In this regard, the audit officer is required to ensure that the correct amount of income has been reported and the right amount of tax has been paid in accordance with the tax laws and regulations.

4.2 For the purpose of achieving voluntary compliance, the tax audit activity is one of the measures undertaken by IRBM to educate and create awareness of taxpayers towards their rights and responsibilities under the provisions of the PITA.

5. YEARS OF ASSESSMENT COVERED

5.1 Generally, a tax audit may cover a period of one to three years of assessment determined in accordance with the audit focus.

5.2 However, the years of assessment to be covered in a tax audit may extend beyond the period as stated in paragraph 5.1 depending on the issues identified during an audit.

6. SELECTION OF CASES

6.1 Cases for audit are selected by a committee in the Tax Compliance Department (TCD) based on risk analysis criteria.

6.2 An audit can be carried out simultaneously by the Petroleum Division and the Non Resident Branch (NRB), if the same tax payer is selected for audit

by the TCD. The Petroleum Division will have to exclude the withholding tax issue from the scope and determination of audit, to enable the NRB to fully audit the issue.

7. HOW A TAX AUDIT IS CARRIED OUT

7.1 Audit Venue

7.1.1 A desk audit is carried out at the IRBM's office whereas a field audit is carried out at a taxpayer's business premise.

7.1.2 Where the business premises are not suitable, the taxpayer may suggest a suitable alternative for IRBM's agreement.

7.2 Commencement of an Audit

7.2.1 A taxpayer who is selected for an audit will be notified by IRBM through a letter of notification of audit. The period between the date of notification of audit and the audit visit is 14 days. However, with the agreement of the taxpayer, a shorter period of notification may be fixed by IRBM. A letter confirming the visit is usually preceded by a phone call.

7.2.2 A taxpayer may request for the audit visit to be deferred due to unavoidable circumstances and reasonable grounds.

7.2.3 Other than the intended date of the visit, the letter will indicate the records that should be made available for audit, the years of assessment to be audited and the names of audit officers who will conduct the audit as well as the expected timeframe required for the audit visit.

7.2.4 A taxpayer may contact the Director of Petroleum Division, IRBM for the purpose of confirming the audit visit.

7.3 The Visit

7.3.1 An audit visit is only applicable to the field audit activity. The audit normally starts off with a presentation of the company's background, business activities, accounting and record keeping system.

7.3.2 During the presentation, the audit officers can get a better understanding through the Q&A session.

- 7.3.3 During the audit process, the person responsible for the handling of taxpayer's business records will also be interviewed.

7.4 Examination of Records

- 7.4.1 During the course of an audit, the audit officer should be allowed to examine all business records and to inspect stock and equipments physically for verification of the claims made. Records pertaining to the years of assessment which are already time barred will not be examined.
- 7.4.2 The audit officer will not search for or take possession of any record. Examination of records will only be carried out at the taxpayer's business premises. If it is deemed necessary, the audit officer should be allowed to make copies of relevant documents.
- 7.4.3 However, under circumstances where the work place provided by the taxpayer is not suitable or conducive to carry out the audit or where copier facility is not available, the audit officers, with the consent of the taxpayer, may obtain records for examination at the IRBM's office. In such a case, the documents will be returned to the taxpayer once the examination is done.
- 7.4.4 The documents and records to be taken back will be listed and the taxpayer may check the documents and records and make a copy of the list, if necessary.
- 7.4.5 Where records and books of accounts are kept in electronic form, hard copies of such records should be made available for examination. If at the time of the audit visit, the taxpayer is unable to provide the hard copies for examination, the taxpayer should facilitate and assist the audit officers to access the computer system and copy the electronic records onto tapes, disks or diskettes.
- 7.4.6 The audit officers will examine all documents and records necessary to ascertain that the correct amount of income has been reported.
- 7.4.7 Section 34A of the PITA requires every person to keep and retain sufficient records when carrying on a business in order to enable

the income or loss from the business to be readily ascertained. "Records" includes the following:

- 7.4.7.1 Books of accounts for recording receipts and payments or income and expenditure;
- 7.4.7.2 Invoices, vouchers, receipts and other documents that are required to verify entries recorded in the books of accounts; and
- 7.4.7.3 Documents, objects, materials, articles and things are maintained and kept in the form of electronic medium.
- 7.4.7.4 Any other record as may be specified by the DGIR.

7.5 Audit Timeframe

- 7.5.1 The minimum time required to complete an on-site examination of records is 5 days. However, the audit timeframe may be extended depending on the following factors:
 - 7.5.1.1 The size of the business and the complexity of business transactions;
 - 7.5.1.2 The form in which records are kept; or
 - 7.5.1.3 The extent of co-operation from the taxpayer.
 - 7.5.1.4 The number of partners with different locations.

7.6 Settlement of Audit

- 7.6.1 After concluding the audit work, the audit officer will prepare an audit findings report for approval by the Director of Petroleum Division.
- 7.6.2 Under certain circumstances, the taxpayer is required to be present at the IRBM's office for discussion on the proposed tax adjustments. The audit officer, together with at least one senior audit officer, shall discuss the proposed adjustments with the taxpayer.

- 7.6.3 The taxpayer, without being called by the IRBM, may be present at IRBM's office to seek clarification regarding the progress of the audit process or to give further information to expedite the settlement of the audit.
- 7.6.4 The taxpayer will be informed of the audit findings which will cover the following areas:
- 7.6.4.1 Audit issues raised;
 - 7.6.4.2 Reasons and rationale for raising the audit issues;
 - 7.6.4.3 The amount of proposed tax adjustments (if any) and the years of assessment involved.
- 7.6.5 If there are tax adjustments to be made, a notification with details of proposed tax adjustments and rationale for making such adjustments will be issued. The taxpayer will be given the opportunity to state his views and give explanations on the audit findings and the proposed tax adjustments forwarded.
- 7.6.6 A taxpayer is allowed 21 days from the date of notification of proposed tax adjustments to file an official objection if he disagrees with the proposed tax adjustments. Additional information and copies of evidence should be provided to support his objection.
- 7.6.7 If no objection is made within 21 days from the date of notification of proposed tax adjustments, the taxpayer shall be deemed to have agreed to the proposed tax adjustments or where an objection is found to have no basis in accordance with the provisions of the PITA, the taxpayer will be informed accordingly.
- 7.6.8 Subsequently, a notice of additional assessment with appropriate penalty imposed under subsection 52(2) or subsection 51(3) of the PITA or a notification of non-chargeability to tax will be issued. However, if there is no adjustment, a letter will be issued to inform that the audit has been finalized without any adjustment.
- 7.6.9 The timeframe for settlement of a tax audit should be within 240 days from the last day of the audit. In the event that a case has exceeded the above period without any action being taken, IRBM will then notify the taxpayer by mail or email.

- 7.6.10 Once the audit case is settled, it will not be audited again for the same year of assessment on the same issues. However, if there are new issues to be pursued or new information is received, an audit can be repeated for the same year of assessment.

8. RIGHTS AND RESPONSIBILITIES

8.1 IRBM

- 8.1.1 An audit officer must adhere to rules and codes of ethics drawn up by IRBM and is required to carry out his duties in the following manner:
- 8.1.1.1 Professional, well mannered, trustworthy, honest and with integrity;
 - 8.1.1.2 Always ready to give explanations on the objectives of the tax audit and the rights and responsibilities of the taxpayer;
 - 8.1.1.3 Knowledgeable and fair in administering tax laws;
 - 8.1.1.4 Co-operative and always ready to give advice and guidance to the taxpayer;
 - 8.1.1.5 Ensure that the audit is carried out smoothly with minimal disruption to the taxpayer;
 - 8.1.1.6 Request for documents, books of accounts and information that are relevant to the audit only;
 - 8.1.1.7 Explain the proposed tax adjustments and provide reasonable time for taxpayer to give responses on issues raised.
 - 8.1.1.8 Ensure the rights and interest of taxpayers and tax agents as well as documents of taxpayers are safeguarded;

8.1.2 Identification of an audit officer

- 8.1.2.1 Each audit officer is issued with an authority card bearing his name and photograph. The card also carries a statement that the officer is authorized to examine books of accounts, documents and records at the taxpayer's premises;
- 8.1.2.2 Taxpayers are advised to view the authority cards in order to verify the authenticity of audit officers; and
- 8.1.2.3 Taxpayers may check with the Director of Petroleum Division if they have doubts on the authenticity of audit officers.

8.1.3 An audit officer is prohibited from:

- 8.1.3.1 Having any personal or financial interest in the business of a taxpayer being audited;
- 8.1.3.2 Recommending to taxpayer that a certain tax agent be appointed as the tax agent for the audit case; and
- 8.1.3.3 Abusing his position or power in carrying out his duties as provided under section 56 of the PITA.

8.2 Taxpayer

8.2.1 Responsibilities of a taxpayer

- 8.2.1.1 Be co-operative, well mannered, fair, honest and with integrity;
- 8.2.1.2 Provide reasonable facilities and assistance to enable the audit officer to carry out his duties as outlined in Section 33 PITA which includes the following:
 - i. Giving access to the audit officer to his business premises, providing information and making available documents and records required for examination;
 - ii. Giving explanation regarding the business, the accounting and information systems;

- iii. Giving permission to examine and make copies of records, documents and books of accounts whether in the physical and / or electronic medium;
 - iv. Assisting in the provision of or providing access to records, documents and books of accounts in the physical and / or electronic medium; and
 - v. Allowing the use of copiers, telephone or other communication equipment, lighting and power, office space, furniture and providing facilities for copying of electronic records onto tapes, disks or diskettes.
- 8.2.1.3 Co-operate in providing complete responses to all queries:
- i. If questions posed are ambiguous, he may seek clarification from the audit officer;
 - ii. If a taxpayer fails to co-operate and provide the required information, he shall be deemed to have committed an offence under the provisions of the PITA.
- 8.2.2 The taxpayer is prohibited from:
- 8.2.2.1 Giving any form of gifts to the audit officer and transacting any business with the audit officer during the audit process;
 - 8.2.2.2 Making any form of payments to the audit officer; and
 - 8.2.2.3 Obstructing or hindering the audit officer in the exercise of his functions. Such obstruction is an offence under section 54 of the PITA. Obstruction includes the following:
 - i. Obstructing or refusing an audit officer from entering lands, buildings, places and premises to perform his duties in accordance with section 33 of the PITA;
 - ii. Obstructing an audit officer from performing his functions and duties under the provisions of the PITA ;

- iii. Refusing to provide books of accounts, or other documents in the custody of or under his control when required by the audit officer;
- iv. Failing to provide reasonable assistance to the audit officer in carrying out his duties; and
- v. Refusing to answer or give responses to questions raised during the course of an audit.

8.3 Tax Agent / Representative

- 8.3.1 The taxpayer can request for his tax agent to be present during an interview.
- 8.3.2 The taxpayer is allowed to bring an interpreter to an interview or discussion session if the taxpayer is not conversant in Bahasa Malaysia or English.
- 8.3.3 If a taxpayer appoints a new tax agent to handle his audit case, he should submit a copy of the letter of appointment.
- 8.3.4 The conduct of a tax agent is governed by the code of ethics formulated by IRBM based on the principles of integrity, accountability, transparency and social responsibility.
- 8.3.5 The tax agent is required to carry out his duties in the following manner:
 - 8.3.5.1 Professional, be fully conversant with tax laws and practices and with integrity;
 - 8.3.5.2 Be honest, trustworthy, transparent and give fullest co-operation when dealing with the taxpayer and IRBM such as informing IRBM on ceasing to be the tax agent of a taxpayer and adhere to rules and guidelines laid down by IRBM;
 - 8.3.5.3 Refrain from misusing information acquired or abusing his position as a tax agent for his own personal advantage;

8.3.5.4 Always give complete and accurate feedback relating to the progress of an audit and advise the taxpayer accurately based on the true facts of the audit case; and

8.3.5.5 Safeguard the confidentiality of all information and ensure that the information is not disclosed to any unauthorized party (subsection 71 (5) of the PITA).

8.3.6 The tax agent is prohibited from:

8.3.6.1 Giving wrong advice to taxpayers and collaborating with taxpayers to avoid paying the correct amount of taxes;

8.3.6.2 Delaying the work of a tax audit or acting irresponsibly towards his entrusted duties; and

8.3.6.3 Offering any form of gifts to the audit officers.

9. CONFIDENTIALITY OF INFORMATION

IRBM will ensure confidentiality of all information obtained from the taxpayer during an interview, discussion, through correspondence or examination of records and that it is utilized for tax purposes only.

10. OFFENCES AND PENALTIES

10.1 If it is discovered after the commencement an audit that there has been an understatement or omission of income, a penalty will be imposed under subsection 52(2) of the PITA in which the penalty rate equal to the amount of tax undercharged (100%) accordingly. However, the DGIR in exercising his discretionary powers may consider a lower penalty of 45% to be imposed for the first offence.

10.2 The concessionary penalty rates may be imposed in cases where the taxpayer makes a voluntary disclosure. As such the taxpayer is encouraged to make a voluntary disclosure regarding the omitted income before the commencement of an audit. This disclosure must be made in writing to Director of Petroleum Division.

10.3 Where taxpayer who furnishes a return form on or before the due date and the Director General has made an assessment for that year of assessment under subsection 39 PITA 1967, subsequently makes a

voluntary disclosure after the due date but not later than 6 months from the due date, the penalty rates are as follows:

Table I

Period of making voluntary disclosure	Rate
Within 60 days from the due date for furnishing the return form	10%
More than 60 days but not later than 6 months from the due date for furnishing the return form	15%

- 10.4 The concessionary penalty rates for voluntary disclosure other than cases mentioned in paragraph 10.3 are as follows:

Table II

	Period from the due date of submitting return form	Rate
Voluntary disclosure before case is selected for audit.	Up to 6 months	Table I applies
	> 6 months to 1 year	20%
	> 1 year to 3 years	25%
	> 3 years and above	30%
<u>Field Audit</u> Voluntary disclosure after taxpayer has been informed but before the commencement of the audit visit.	Not applicable	35%
<u>Desk Audit</u> Voluntary disclosure within 30 days from date of letter requesting for documents is issued		

11. COMPLAINTS

- 11.1 If the taxpayer is dissatisfied with the manner in which an audit is being carried out, including the behaviour of an audit officer, he may make an official complaint to the Director of Petroleum Division / Director of

Compliance Department / Deputy Director General of Inland Revenue (Compliance) / Director General of Inland Revenue.

- 11.2 IRBM will act fairly, objectively and impartially on all complaints received.
- 11.3 IRBM will not entertain any complaint which is found to have no basis and not made in good faith.
- 11.4 IRBM will take action and file a complaint with the relevant authority such as Ministry of Finance / Malaysian Institute of Taxation / Malaysian Institute of Accountants / Malaysian Institute of Certified Public Accountants / Malaysian Association of Tax Agents / Bar Council, if tax agents or their representatives do not co-operate or behave unprofessionally which is inconsistent with their code of ethics.

12. PAYMENT PROCEDURES

- 12.1 Any taxes and penalties to be paid arising out of an audit must be made to the DGIR through any appointed bank or any Collection Branch of IRBM.
- 12.2 The taxpayer is required to make full payment of taxes and penalties arising out of an audit.
- 12.3 If the taxpayer is unable to make full payment of tax, IRBM may consider the taxpayer's application for settling the total tax liability by installments, for a predetermined period.
- 12.4 Application for installment payment scheme should be submitted to the Director of Petroleum Division, Corporate Tax Department for approval.
- 12.5 Where a taxpayer fails to adhere to the installment payment scheme agreed upon, late payment penalty on the balance of tax outstanding will be imposed.

13. APPEALS

Section 43 to 46 of the PITA lay the ground rules for appeals relating to assessment raised by IRBM.

- 13.1 A taxpayer can appeal against an assessment as a result of a tax audit.
- 13.2 The appeal must be made to the Special Commissioners of Income Tax within 30 days after the service of the notice of additional assessment.

13.3 Should either party be dissatisfied with the decision of the Special Commissioners of Income Tax, the aggrieved party may apply to have the case heard in the High Court and further the Court of Appeal.

14. EFFECTIVE DATE

This framework is effective from **1 April 2013**.

**Director General of Inland Revenue
Malaysia**

April 2013



INLAND REVENUE BOARD OF MALAYSIA

TRANSFER PRICING AUDIT FRAMEWORK

EFFECTIVE DATE: 1 APRIL 2013

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1. PURPOSE

1.1. The transfer pricing audit framework issued by the IRBM aims to ensure that cross-border and local transfer pricing audits are carried out in a fair and transparent manner, in accordance with the provisions of the Income Tax Act 1967 (ITA). This framework outlines the rights and responsibilities of audit officers, taxpayers and tax agents in respect of a tax audit. Generally, this framework aims to:

1.1.1. Assist audit officers to carry out their tasks efficiently and effectively; and

1.1.2. Assist taxpayers in fulfilling their obligations.

2. OBJECTIVE OF TRANSFER PRICING AUDIT

2.1. The main objective of a transfer pricing audit is to ensure that controlled transactions comply with the arm's length principle, the Malaysian tax laws as well as administrative requirements of the IRBM. In addition, transfer pricing audits also fulfill the normal audit objectives that serve to encourage voluntary compliance and ensure that a higher tax compliance rate is achieved under the Self-Assessment System. In this regard, the audit officer is required to make certain that a taxpayer pays his fair share of tax in accordance with the tax laws and regulations.

3. STATUTORY PROVISIONS AND REFERENCES

3.1. Apart from provisions stated in paragraph 2.1 of the Tax Audit Framework, other provisions relevant in a transfer pricing audit include:

3.1.1. Section 132: Double taxation arrangements

3.1.2. Section 139: Controlled companies

3.1.3. Section 140A: Power to substitute the price and disallowance of interest on certain transactions

3.2. Income Tax (Transfer Pricing) Rules 2012; and

3.3. Transfer Pricing Guidelines 2012.

4. WHAT IS A TRANSFER PRICING AUDIT?

4.1. A transfer pricing audit is an examination of a taxpayer's business records and financial affairs to ascertain the application of the rules on controlled transactions. The examination is to ensure that transfer pricing rules are being applied in accordance with the methods and manners provided for in the Income Tax (Transfer Pricing) Rules 2012 and Transfer Pricing Guidelines 2012, as well as comply with administrative requirements of the IRBM on the types of records and documentations to be maintained. Transfer pricing audit also serves to ensure that the arm's length principle is being adopted, and the fair share of tax is being reported, calculated and paid in accordance with the tax law and regulations. IRBM carries out two (2) types of transfer pricing audit, namely transfer pricing desk audit and transfer pricing field audit.

4.1.1. Transfer Pricing Desk Audit

4.1.1.1. A desk audit is held at the IRBM's office. Desk audits are normally concerned with enforcement of compliance on transfer pricing issues via correspondence. A taxpayer may be called for an interview at IRBM's office if further information is required.

4.1.1.2 Desk audit cases can be referred for field audit action. Under such circumstances, the taxpayer will be informed through a field audit notification letter as part of the normal process of commencing the field audit.

4.1.2 Field Audit

4.1.2.2 A field audit is one that takes place at the taxpayer's premise. It applies the normal audit procedure involving the examination of the taxpayer's business records with additional processes to determine the arm's length nature of the controlled transactions. A taxpayer will be given a notice prior to a field audit.

4.2 Generally, this audit framework is applicable to both types of audit, with the exception of visit to premises and examination of the taxpayer's business records which are only applicable to field audit.

5. YEARS OF ASSESSMENT COVERED

Transfer pricing audits generally cover a period of three to six years of assessment depending on the transfer pricing issues. However, with effect from 1 January 2014, the years of assessment to be covered will be restricted up to five years of assessment. This is in line with the amendment to Section 91(1) of the ITA 1967.

6. SELECTION OF CASES

- 6.1. A transfer pricing audit case selection is first determined by the significance in amount of controlled transactions between related companies, before a detailed risk analysis is carried out.
- 6.2. Cases must be approved by a Selection Committee before proceeding with an audit.

7. HOW A TRANSFER PRICING AUDIT IS CARRIED OUT

7.1 Transfer Pricing Field Audit

7.1.1 Commencement of an Audit

7.1.1.1 Prior to an audit visit, a taxpayer will be asked by IRBM to submit documents which also include Transfer Pricing Documentation, as described in paragraph 25 and Appendix A of the Transfer Pricing Guidelines 2012, whichever is applicable.

7.1.1.2 A taxpayer who is selected for an audit will be notified by IRBM through a letter of notification of audit. The period between the date of notification of audit and the audit visit is at least 14 days. However, if the notification could not be issued within 14 days, the taxpayer will be informed in advance via phone or e-mail to confirm the date of the visit.

7.1.1.3 Other than the intended date of the visit, the letter will indicate the records that should be made available for audit, the years of assessment to be audited, the names of audit officers who will conduct the audit, as well as the expected timeframe required for the audit visit.

7.1.1.4 If necessary, the taxpayer may contact the Division Director / Branch Audit Manager / Branch Director of IRBM for the purpose of confirming the audit visit.

7.1.2 Audit Visit

7.1.2.1 A transfer pricing audit visit starts off with a briefing by an audit officer explaining the purpose of the audit.

7.1.2.2 The taxpayer will be asked to prepare presentation slides explaining in detail the background of the company, the business and global operations, the complete management structure and functions, accounting and record keeping system focusing on controlled transactions between related companies.

7.1.2.3 During the audit process, selected key personnel from relevant departments will also be interviewed.

7.1.2.4 In addition to the location where records are kept, the audit officer may also visit other selected locations, for example the manufacturing plant of the taxpayer.

7.1.2.5 In certain circumstances, visits may be made to related companies in Malaysia who are involved in the controlled transaction. In such events, the related company concerned will be duly notified.

7.1.3 Examination of Records

7.1.3.1 For the purpose of examination of records, items defined in paragraphs 7.4.1 to 7.4.6, 7.4.8 and 7.4.9 of the Tax Audit Framework are applicable.

7.1.3.2 The audit officers will examine all documents and records necessary to ascertain that the arm's length principle is adopted. Basically, records consist of:

- i. Business Records

Taxpayer needs to obtain guidance in relation to record keeping from the guidebook and public rulings issued by IRBM.

Pursuant to section 138A of the ITA, the Director General of Inland Revenue (DGIR) is given the power to issue Public Rulings on the interpretation of any provision of the ITA. The following Public Rulings and guide book in relation to record keeping that have been issued are:

- a) IRBM Public Ruling No. 4/2000: Keeping Sufficient Records (Companies & Co-operatives);
- b) IRBM Public Ruling No. 6/2000: Keeping Sufficient Records (Persons Other Than Companies, Co-operatives or Individuals); and
- c) STS-BK4: Self-Assessment – A Guide to Record Keeping For Business.

ii. Other Records

In transfer pricing audit cases, the audit officer may need to examine records other than business records such as:

- a) All agreements, contracts and other binding documents concerning business activities with related companies or third parties as required under paragraph 25.4 of the Transfer Pricing Guidelines 2012;
- b) Documentation on specific transactions as required under Appendix A of the Transfer Pricing Guidelines 2012;
- c) Records relating to the ownership of properties;
- d) Other statements as required under section 79 of the ITA.

- iii. Section 82 of the ITA requires every person to keep and retain sufficient records when carrying on a business in order to enable the business to be readily ascertained of its profit or loss. As stipulated in the Public Ruling Nos. 4/2000, 5/2000 and 6/2000, the meaning of “records and documents” includes the following:
- a) Books of accounts for recording receipts and payments or income and expenditure;
 - b) Financial Statement;
 - c) Invoices, vouchers, receipts and other documents that are required to verify entries recorded in the books of accounts;
 - d) Documents, objects, materials, articles and items handled and stored in an electronic medium; and
 - e) Any other record that may be specified by the DGIR.

7.1.3.3 If the document required in relation to the transaction of business in Malaysia is being kept outside of Malaysia by a related company, the taxpayer is required to submit the document within the specified period.

7.1.3.4 Failure to keep sufficient records is an offence under section 119A of the ITA. In relation to this, the audit officer may apply alternative approaches or indirect methods for the purpose of ascertaining whether the appropriate amount of income has been reported.

7.1.4 Audit Timeframe

The time required to complete an on-site examination of records is between 4 to 5 days. However, the audit timeframe may be extended depending on the following factors:

7.1.4.1 The size and complexity of the business transactions;

7.1.4.2 The form in which records are kept; or

7.1.4.3 The extent of co-operation from the taxpayer.

7.1.5 Settlement of Audit

7.1.5.1 After concluding the audit work, the audit officer will prepare an audit report for approval by the Division Director/Branch Audit Manager.

7.1.5.2 The taxpayer may be required to be present at the IRBM's office for discussion on the proposed tax adjustments.

7.1.5.3 The taxpayer is encouraged to set an appointment with IRBM, at IRBM office to seek clarification regarding the progress of an audit or to give further information to expedite the settlement of the audit.

7.1.5.4 The taxpayer will be informed of the audit findings together with an explanation on the audit findings, if any.

7.1.5.5 If there are tax adjustments to be made, a notification with details of proposed tax adjustments and rationale for making such adjustments will be issued. A taxpayer is allowed 21 days from the date of notification of proposed tax adjustments to file an official objection if he disagrees with the proposed tax adjustments by providing additional information and copies of evidence to support his objection.

7.1.5.6 If no objection is made within 21 days from the date of notification of proposed tax adjustments, the taxpayer shall be deemed to have agreed to the proposed tax adjustments or, where an objection is found to have no basis in accordance with the provisions of the ITA, the taxpayer will be informed accordingly.

7.1.5.7 A notice of additional assessment together with details of tax adjustment and appropriate penalty imposed under subsection 113 (2) or paragraph 44B(7)(b) or subsection 112(3) of the ITA or a notification of non-chargeable to tax will be issued. However, if there is no adjustment, a letter

will be issued to inform that the audit has been finalized without any adjustment.

7.1.5.8 Audit cases that have been settled will be monitored through compliance reviews to ensure continued compliance with the arm's length principle. If there are new issues to be pursued or failure to comply with the arm's length principle, the case will again be selected for audit.

7.2 Transfer Pricing Desk Audit

7.2.1 Commencement of an Audit

A desk audit commences when a letter requesting for documents is issued to the taxpayer. Documents include Transfer Pricing Documentation as explained in the Transfer Pricing Guidelines 2012.

7.2.2 Generally, a desk audit involves checking information on controlled transactions, comprising of:

7.2.2.1 Reviewing the accounts and financial statement;

7.2.2.2 Analysing and reviewing the Transfer Pricing Documentation;

7.2.2.3 Analysing and reviewing non-transfer pricing issues; and

7.2.2.4 Reviewing settled audit cases to ensure compliance with audit findings, for subsequent years.

7.2.3 In certain circumstances, audit visits may be performed for verification purposes.

8 RIGHTS AND RESPONSIBILITIES

8.1 IRBM

The rights and responsibilities of a transfer pricing audit officer are as listed in paragraph 8.1 of the Tax Audit Framework.

8.2 Taxpayer

8.2.1 Responsibilities of a taxpayer:

8.2.1.1 Be co-operative, polite, fair, honest and with integrity, and is encouraged to be actively involved in all stages of the audit process up to settlement;

8.2.1.2 Provide reasonable facilities and assistance to enable the audit officer to carry out his duties as outlined in Public Ruling No. 7/2000 which includes the following:

- i. Giving access to the audit officer to the business premises, providing information and making accessible any documents and records required for examination;
- ii. Allowing the audit officer to interview key personnel;
- iii. Giving explanations regarding the business, accounting and information systems;
- iv. Giving permission to examine and make copies of records, documents and books of accounts whether in the physical and/or electronic medium;
- v. Assisting in providing access to records, documents and books of accounts in the physical and/or electronic medium; and
- vi. Allowing the use of copiers, telephone, internet or other communication equipment, lighting and power, office space, furniture and providing facilities for copying of electronic records into thumb drive and external hard drive.

8.2.1.3 To co-operate in providing complete responses to all queries:

- i. If questions posed are ambiguous, taxpayer may seek clarification from the audit officer;
- ii. Taxpayer is requested to bring an interpreter during an interview or discussion if the taxpayer is not fluent

in Bahasa Malaysia or English.

8.2.1.4 If additional information is requested during/after the audit visit, the taxpayer must submit the documents within the given time frame.

8.2.2 The taxpayer is prohibited from:

8.2.2.1 Giving any form of gifts or transacting any business with the audit officer during the audit process;

8.2.2.2 Making any form of payments to the audit officer;

8.2.2.3 Obstructing or hindering the audit officer in exercising his functions. Such obstruction is an offence under section 116 of the ITA. Obstruction includes the following:

- i. Obstructing or refusing an audit officer from entering lands, buildings, places and premises to perform his duties in accordance with section 80 of the ITA;
- ii. Obstructing an audit officer from performing his functions and duties under the provisions of the ITA;
- iii. Refusing or purposely delaying the provision of books of accounts, or other documents in the custody of or under his control when required by the audit officer;
- iv. Failing to provide reasonable assistance to the audit officer in carrying out his duties; and
- v. Refusing to answer or give responses to questions raised during the course of an audit.

8.2.2.4 IRBM strongly discourage taxpayers from changing or appointing a different tax agent/representative in situations where a decision/settlement has been reached between the agents and IRBM.

8.2.2.5 Taking into consideration the length of time required to complete a transfer pricing audit, such changes will result in the loss of valuable time, costs and efforts of all parties

concerned, as in most cases the audit process will have to be repeated, hence hampering the audit process and further delaying the duration for case settlement.

8.2.2.6 IRBM prohibits the appointment of any lawyer to represent the case prior to filing the case to Special Commissioners of Income Tax/court.

8.3 Tax Agent / Representative

8.3.1 If a different tax agent (other than for compliance audit) is appointed for transfer pricing audit purposes, the taxpayer must submit a copy of the letter of appointment as required under Section 153 of the ITA.

8.3.2 A tax agent can be present together with the taxpayer during the interview session.

8.3.3 The conduct of a tax agent is governed by the code of ethics issued by IRBM based on the principles of integrity, accountability and transparency.

8.3.4 A tax agent is required to carry out his duties in the following manner:

8.3.4.1 With integrity, professional and be fully conversant with tax laws and practices, including those related to transfer pricing;

8.3.4.2 Be honest, trustworthy, transparent and cooperative when dealing with the taxpayer and IRBM. This includes informing IRBM whenever the tax agent no longer represents a taxpayer, and adhere to the rules and guidelines laid down by IRBM;

8.3.4.3 Able to handle the technical issues and provides adequate/proper advice based on the ITA 1967 and other relevant rules and regulations, and act as an intermediary between IRBM and the tax payer;

8.3.4.4 Refrain from misusing information acquired, or abusing his position as a tax agent for his own personal

advantage;

8.3.4.5 Always provide complete and accurate feedback relating to the progress of an audit, and advise the taxpayer accurately based on the true facts of the audit case;

8.3.4.6 Ensure the taxpayer pays his fair share of tax in Malaysia instead of reducing tax payable; and

8.3.4.7 Safeguard the confidentiality of all information and ensure that the information is not disclosed to any unauthorized party (subsection 138 (5) of the ITA).

8.3.5 The tax agent is prohibited from:

8.3.5.1 Giving wrong advice and collaborating with taxpayers to avoid paying the correct amount of taxes;

8.3.5.2 Delaying the audit settlement process or acting irresponsibly; and

8.3.5.3 Offering any form of gifts to the audit officers.

9. CONFIDENTIALITY OF INFORMATION

IRBM will ensure confidentiality of all information obtained from the taxpayer during an interview, discussion, through correspondence or examination of records, and that they are utilized for tax purposes only.

10. OFFENCES AND PENALTIES.

10.1. If it is discovered during a transfer pricing audit that there has been an understatement or omission of income, a penalty will be imposed under subsection 113(2) or paragraph 44B(7)(b)* of the ITA in which the penalty rate equals to the amount of tax undercharged (100%) accordingly.

*Paragraph 44B(7)(b) is deemed to have taken effect for the years of assessment 2008, 2009 and 2010.

10.2. A concessionary penalty rate may be imposed in a case where the

taxpayer makes a voluntary disclosure. As such, the taxpayer is encouraged to make a voluntary disclosure regarding the omitted income before the commencement of an audit. For transfer pricing audit cases, disclosure must be made in writing to the Director of Multinational Tax Department/relevant Branch Director of IRBM.

- 10.3. For audit cases that involve voluntary disclosure of an understatement or omission of income on non-transfer pricing issues, the concessionary penalty rates as in the Tax Audit Framework apply. Nonetheless, the concessionary penalty rates for voluntary disclosure for transfer pricing issues are as follows (as stated in paragraph 26 of the Transfer Pricing Guidelines 2012):

Type of Penalty	Condition	Penalty rate		
		Normal Case	Voluntary disclosure after taxpayer has been informed but before commencement of the audit visit	Voluntary disclosure before case is selected for audit
1	Understatement or omission of income	45%	35%	15%
2	Taxpayer did not prepare transfer pricing documentation	35%	30%*	15%*
3	Taxpayer prepared transfer pricing documentation but did not fully comply with the requirements under the Transfer Pricing Guidelines	25%	20%	10%
4	Taxpayer prepared a comprehensive, good quality, contemporaneous transfer pricing documentation in accordance with existing regulations	0%	0%	0%

* Upon voluntary disclosure, the taxpayer is still required to prepare the Transfer Pricing Documentation.

- 10.4. For each repeated offence, the rate of penalty shall be increased by 20% as compared to the last penalty rate imposed for the previous offence, but limited to a sum not exceeding 100% of the total amount of tax undercharged.

11. COMPLAINTS

- 11.1. If the taxpayer is dissatisfied with the manner in which an audit is being carried out, including the behaviour of an audit officer, he may make an official complaint to the Director of Multinational Tax Department /IRBM Branch Director / State Director / Director of Compliance Department / Deputy Director General of Inland Revenue / Director General of Inland Revenue.
- 11.2. IRBM will act fairly, objectively and impartially on all complaints received.
- 11.3. IRBM will not entertain any complaint which is found to have no basis and not made in good faith.
- 11.4. IRBM will take action and file a complaint with the relevant authority such as Ministry of Finance, Chartered Tax Institute of Malaysia, Malaysian Institute of Accountants, Malaysian Institute of Certified Public Accountants, Malaysian Association of Tax Agents or Bar Council, if tax agents or their representatives do not co-operate or behave unprofessionally, which is inconsistent with their code of ethics.

12. PAYMENT PROCEDURES

- 12.1. Any taxes and penalties to be paid arising out of an audit must be made to the DGIR through any appointed bank or any Collection Branch of IRBM.
- 12.2. If the taxpayer is unable to make full payment of tax, IRBM may consider the taxpayer's application for settling the total tax liability by instalments, for a predetermined period.
- 12.3. Application for instalment payment scheme must be submitted to Division Director/Director of Multinational Tax Department/the relevant Branch Director of IRBM for approval.
- 12.4. Where a taxpayer fails to adhere to the instalment payment scheme agreed upon, late payment penalty on the balance of tax outstanding will be imposed.

13. MUTUAL AGREEMENT PROCEDURES

Taxpayers residing in Malaysia can apply for assistance from the competent authorities in Malaysia through the Mutual Agreement Procedure, on issues arising from transfer pricing audit adjustments affecting cross-border transactions with related companies in any treaty partner country (Please refer to the Guidelines on Mutual Agreement Procedure).

14. OFFSETTING ADJUSTMENT

- 14.1 Any additional adjustments in respect of transfer pricing for a particular assessment made on the taxpayer in a controlled transaction, can be presented with an offsetting adjustment on the assessment of the related party in the same transaction.
- 14.2 The related party concerned should apply for the offsetting adjustment in a letter to the branch where the tax file is handled, with a copy to the branch of the taxpayer where the initial transfer pricing adjustment has been made. The letter must be submitted within 21 days from the date of the notice of assessment/amended assessment is issued.
- 14.3 However, the offsetting adjustment is subject to review and approval by the IRBM.

15. APPEALS

Appeals relating to assessments raised by IRBM are laid out under Section 99 to 102 of the ITA.

- 15.1 A taxpayer can appeal against an assessment as a result of a tax audit.
- 15.2 The appeal must be made to the Special Commissioners of Income Tax within 30 days after the service of the notice of additional assessment.
- 15.3 Should either party be dissatisfied with the decision of the Special Commissioners of Income Tax, the aggrieved party may apply to have the case heard in the High Court and further the Court of Appeal.

16 EFFECTIVE DATE

The tax audit framework is effective from 1 April 2013.

**Director General of Inland Revenue
Malaysia**

1 APRIL 2013