

TECHNICAL

Direct Taxation

PUBLIC RULING NO. 11/2014 ON FOREST ALLOWANCES RELATING TO TIMBER EXTRACTION – SUMMARY OF CONTENTS

The above [Public Ruling \(PR\) No.11/2014](#) was issued on 31 December 2014 and alerted in our [e-CTIM TECH-DT 7/2015](#) dated 15 January 2015.

The objective of the PR is to explain the type of capital expenditure that qualifies for forest allowance (FA), the computation of FA and forest charges and the tax treatment of logging expenses.

For the purpose of this PR

Forest in relation to a person, means a forest in respect of which he has concession or a licence to extract timber therefrom, being a forest in use by him for the extraction of timber therefrom for the purposes of a business of his which consist wholly or partly of that extraction.

Concession means the right given by a government to a person for carrying on a specified activity in a designated area.

Disposal of forest means the conveyance, assignment or surrendering of the concession or licence for a valuable consideration or payment.

Main Contents of the PR

| Para No. | Subject and Summary | | | | | | |
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| 4 | <p><i>Qualifying Forest Expenditure And Computation Of Allowances</i></p> <ul style="list-style-type: none"> A claim for FA can be made by a person who has been granted a concession or licence and carries on a business of timber extraction. FA is granted in respect of capital expenditure <i>incurred on the construction in the forest</i> of the following :— <table> <thead> <tr> <th>Asset</th><th>Rate</th></tr> </thead> <tbody> <tr> <td>a. Roads or buildings, including bridges or jetties used for the purposes of the timber extraction business;</td><td>10%</td></tr> <tr> <td>b. Buildings provided for the welfare of or as living accommodation for employees engaged in extraction of timber*.</td><td>20%</td></tr> </tbody> </table> <p>* Provided that the person may elect to treat the building as an industrial building which qualifies for initial allowance of 40% in the Income Tax Return Form. Election is not applicable where the buildings are used by directors or management, administrative or clerical staff of the business.</p> <p>[Note: It appears that the Director General of Inland Revenue (DGIR) has made a direction on the procedure for election. Please refer to Para 42(1), Schedule 3 of the Income Tax Act 1967 (ITA)].</p> <ul style="list-style-type: none"> Such roads or buildings shall be of little or no value to any person if the activity of | Asset | Rate | a. Roads or buildings, including bridges or jetties used for the purposes of the timber extraction business; | 10% | b. Buildings provided for the welfare of or as living accommodation for employees engaged in extraction of timber*. | 20% |
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| | <p>timber extraction ceases, except if they are used in connection with the business of timber from another forest or the working of a farm after timber have been extracted.</p> <p><u>[Note: Para 8(1), Sch 3 of the ITA states “and which (the capital expenditure), if the forest ceases to be used for such extraction, would be likely to be of little or no value to any person except in connection with the extraction of timber from another forest or with a business which consists wholly or partly of the working of a farm.”]</u></p> | | | | | | | | | | | | | | | | | | |
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| 5 to 7 | <p>Cessation Of Timber Extraction Business And Disposal Of Forest</p> <ul style="list-style-type: none">When the business of timber extraction ceases, an allowance equal to the balance of the capital expenditure which has not been given is allowed to be deducted in the year of cessation. The person is not entitled to claim any FA after the business has ceased. (Ref. Example 3)When a forest is disposed of, a forest charge is computed in the year of disposal. The charge is equal to the total amount of FA given for each year of assessment (YA) and on permanent cessation of the timber extraction business. For the purpose of computing forest charge, the actual sale consideration received or receivable by the person is not taken into account. (Ref. Example 4)If disposal takes place after the end of the basis period for a YA in which the business ceased permanently, the disposal is deemed to have been made in the basis period in which the business ceased. (Ref. Example 5)An election may be made to spread back (divide) the amount of forest charge equally by the number of YAs for which allowances were made. <u>[Note: Please refer to Para 32(1), Schedule 3 of the ITA for the election procedure.]</u> (Ref. Examples 6 & 7) | | | | | | | | | | | | | | | | | | |
| 8 | <p>Logging contractor who is not a licence-holder</p> <ul style="list-style-type: none">A logging contractor who does not hold a licence or concession is not entitled to claim FA even if he has incurred qualifying forest expenditure and may have made payments to the holder of the concession or license for the right to extract timber from the forest. <u>[Note: Ref. Para 8(1), Sch 3 of the Act]</u>The following is a list of expenses of a logging contractor which are deductible/non-deductible: <table><tr><th><u>Expense</u></th><th><u>Deductibility/ (Statutory Ref.)</u></th><th><u>Remarks</u></th></tr><tr><td>1. Royalty/ premium paid to State government in the name of licence-holder during extracting timber</td><td>Deductible [Section 33(1)]</td><td>Wholly and exclusively incurred in the production of income</td></tr><tr><td>2. Payment to licence-holder for purchase of timber *</td><td>Deductible [Section 33(1)]</td><td>Wholly and exclusively incurred in the production of income</td></tr><tr><td colspan="3">* Sale of the timber will be taken as part of the logging contractor’s income.</td></tr><tr><td>3. Licence fee paid to any Forest Department</td><td>Deductible [Section 33(1)]</td><td>Revenue expenditure</td></tr><tr><td>4. Survey and demarcation fees paid to any Forest Department</td><td>Deductible [Section 33(1)]</td><td>Revenue expenditure</td></tr></table> | <u>Expense</u> | <u>Deductibility/ (Statutory Ref.)</u> | <u>Remarks</u> | 1. Royalty/ premium paid to State government in the name of licence-holder during extracting timber | Deductible [Section 33(1)] | Wholly and exclusively incurred in the production of income | 2. Payment to licence-holder for purchase of timber * | Deductible [Section 33(1)] | Wholly and exclusively incurred in the production of income | * Sale of the timber will be taken as part of the logging contractor’s income. | | | 3. Licence fee paid to any Forest Department | Deductible [Section 33(1)] | Revenue expenditure | 4. Survey and demarcation fees paid to any Forest Department | Deductible [Section 33(1)] | Revenue expenditure |
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| | <p>5. Sums payable otherwise than to a State Government (SG) or with the approval of the Minister, a statutory authority, or other body or fund which is substantially owned by the SG or statutory authority for use of the licence or permit to extract timber</p> <p>Not deductible 39(1)(g)</p> |
| | <p>6 Payment to a licence-holder for the right to perform work, cut down, exploit and extract timber *</p> <p>Not deductible Capital expenditure</p> <p>* If a lump sum payment is made/agreed to be paid by a logging contractor, the amount relating to payment for the right to perform work, cut down, exploit and extract timber must be indicated.</p> |
| | <p>7. Commission to obtain timber concession</p> <p>Not deductible Capital expenditure</p> |
| | <p>8. Fine or penalty paid to any Forest Department or Authority due to infringement of the law</p> <p>Not deductible Not incurred in the production of income</p> |
| 9 | <p>One business or separate businesses</p> <ul style="list-style-type: none"> A person who carries on the activities of extracting timber in a forest and processing of sawn timber (operating a sawmill in the vicinity) is generally considered as carrying two separate businesses – one for timber extraction and the other for sawmill. The person is required to keep separate records for each business source. |

Members may view the PR at the websites of the [Institute](#) and the [LHDNM](#).

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