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CHARTERED TAX INSTITUTE OF MALAYSIA (225750-T)

e-CTIM TECH-DT 67/2015 **8 September 2015**

TO ALL MEMBERS

TECHNICAL

Direct Taxation

PUBLIC RULING NO. 2/2015 – TAXATION OF REAL ESTATE INVESTMENT TRUST (REIT) OR PROPERTY TRUST FUND (PTF)

The above Public Ruling (PR) No.2/2015 was issued on 19 June 2015 (our e-CTIM TECH-DT 47/2015 dated 24 June 2015 refers).

This PR replaces PR. No.9/2012. It is re-written to enhance clarity on the tax treatment of an approved REIT/PTF in Malaysia. Paragraphs 8.3.2 and 8.3.3 are inserted to incorporate the amendments to control transfer provisions relating to the disposal of industrial building to REIT/PTF under the Finance Act, 2013. A new paragraph is inserted to explain the filing of income tax return form TR.

Taxation of REIT/PTF

The following table summarizes the contents of the PR:

Heading (Para No)	Summary
***Introduction* (4)**	A REIT/PTF is a trust body that is constituted as a collective investment scheme that invests primarily in a portfolio of income-generating real estates. It is constituted when a trust deed is executed by the manager and the trustee. • An Islamic REIT/PTF is managed and operated based on Syariah principles. Income distributed by a REIT/PTF is a distribution of income and not a distribution of dividend.
***Basis of assessment* (5)**	The basis year (calendar year) for a year of assessment (YA) or the financial accounting period that ends on a day other than 31 Dec. is the basis period of the REIT/PTF in accordance with the provisions of S.21A, other than S.21A(5), of the Income Tax Act 1967 (ITA). (Example 1)
***Special tax treatment of rental income of a REIT/PTF* (6)**	Rental income of a REIT/ PTF derived from its investments in real property is treated as gross income from a business source, except that • Expenses allowed to be deducted is restricted to the amount of gross rental income and any excess of expenses over gross rental income is disregarded and not allowed to be carried forward. • Expenses incurred prior to commencement of the rental source is not allowable. The rental source is considered to have commenced if the building is available for rent. (Example 2) • Capital Allowances (CA) is allowed. (Example 3) – see also para. 8.
***Deductibility of expenses* (7)**	Deductibility of expenses against rental income received by a REIT/PTF is determined in accordance with the provisions of S.33(1), and hence remuneration of the REIT/PTF manager is deductible.

	• The trustee's fees is not deductible under S.33(1). • "Establishment expenditure" refers to legal, valuation and consultancy fees incurred for establishing a REIT/PTF prior to an approval by the SC and is allowable under P.U. (A) 135/2006 as a deduction in ascertaining the adjusted income from the letting of property of the REIT/PTF. It is deemed to be incurred in the basis period for the YA in which the business commenced. (Example 4).
***CA and IBA* (8)**	CA and balancing allowance (BA) under Schedule 3 is deductible from adjusted income (AI) but any excess of CA and BA over AI is disregarded and cannot be carried forward pursuant to S.63C(4) of the ITA. • A balancing charge (BC) arises upon disposal of an asset where the disposal value exceeds the residual expenditure at the date of the disposal. The amount of BC is limited to total CA allowed in respect of the asset disposed. If there is an adjusted loss, the loss cannot be deducted from the BC and is disregarded. (Example 5) • A REIT/PTF deriving rental income from an industrial building (building used by the tenant as an IB) qualifies to claim IBA in respect of that building. An IB is a building that must be used for any one of the specific purposes as provided in Schedule 3 of the ITA. IBA is deducted against AI. • Qualifying expenditure (QE) on an IB refers to the cost of construction of the building or the purchase price. QE of an IB acquired by a REIT/PTF is as follows: ✓ purchase price of building if purchased from a non-related company; ✓ residual expenditure (RE) of the IB on the first day of the disposer's final period if purchased from a related company* (if the building continues to be used as an IB). * **w.e.f. YA 2013**, a related company is one which holds not less than 50% of the residual profits or residual assets of the REIT/PTF available for distribution on winding up. The disposer's share of residual profits is determined by the formula- $\dfrac{\text{No. of issued units of a REIT/PTF held by a company}}{\text{Total no. of issued units of a REIT/PTF held by unit holders}} \times \text{Residual profits available for distribution by a REIT/PTF}$ The disposer's share of residual assets is determined by the formula – $\dfrac{\text{No. of issued units of a REIT/PTF held by a company}}{\text{Total no. of issued units of a REIT/PTF held by unit holders}} \times \text{Residual assets available for distribution by a REIT/PTF}$ (Refer to Examples 6 & 7) **From YA 2008 to YA 2012,** any company which claimed IBA and subsequently disposed of the IB to a REIT/PTF is deemed to have disposed of the IB for a sum equal to the IB's RE on the first day the company's final period (i.e.no BC or BA arises). (Example 8) • Please refer to the following examples:

	a) Example 9 – computation of BC or BA by the disposer when an IB is disposed of together with plant and machinery. b) Example 10 – deemed IB (hotel building used for the purpose of a hotel business and registered with the Ministry of Tourism). The owner of that hotel building must also operate the hotel building for the hotel business to be eligible to claim IBA in respect of the hotel building.
***Transitional provision* (9)**	From YA 2005, the transitional provision provides that: a) S.43 and S.44 of the ITA in respect of adjusted loss; and b) Para. 75 of Sch. 3 of the ITA in respect of CA of a unit trust which was ascertained prior to the coming into force of S.63C of the ITA is allowed to be deducted against income for YA 2005 and subsequent YAs.
***Exemption from income tax* (10)**	For **YA 2005 and YA 2006**, a REIT/PTF is exempted from tax on an amount of its total income which is equal to the amount of income distributed to unit holders in the basis period for the YA. The amount of income not distributed in that YA would be subject to tax at the prevailing corporate tax rate at the REIT/PTF level. W.e.f **YA 2007**, a REIT/PTF is fully exempted from tax if it distributes 90% or more of its total income to its unit holders in the basis period for that YA [S.61A(1)]. Where the distribution is less than 90% of total income, the whole chargeable income will be subjected to tax at the prevailing corporate tax rate. Examples 11 – 13 illustrate the computation of percentage of total income distributed to unit holders so as to determine whether the REIT/PTF is chargeable to tax. • Income that is specifically exempted from tax are: a) interest from specified sources (refer to para. 10.2 of the PR); b) (from 1.1.2008) – single-tier dividend distributed by resident companies Tax exempt income received by a REIT/PTF (e.g. dividends) are not included in computing the total income of the REIT/PTF. Expenses incurred in respect of exempt income will not be allowed a deduction. Examples 14 – 17 show the tax treatment of various types of income received by a REIT/PTF.
Income distribution by a REIT/ PTF (11)	Para. 11 outlines the rules and requirements to be observed when distributions of income are made to unit holders. Among the important requirements are: a) Deduction of withholding tax at the rate applicable to the unit holder (other than resident companies*) when distributing income exempted under S.61A of the ITA which is deemed to be derived from Malaysia; **The income received from a REIT/PTF is subject to tax at the prevailing tax rate applicable to the company.* (Refer to para. 11.4 for the rates applicable to different classes of unit holders.) b) Preparation of dividend vouchers for the unit holders that contain the information listed in para. 11.6 of the PR; c) Furnishing certain information relating to unit holders (resident and non-resident) to the LHDNM (listed in para 11.7 of the PR). If a REIT/PTF intends to distribute 90% or more of its total income but has fallen short of 90% at the end of the basis period, the REIT/PTF is given a grace period of two months from the closing of its accounts to distribute the balance so as to qualify for tax exemption at the REIT/PTF level.

	The undistributed accumulated income of a REIT/PTF from prior years which has been subjected to tax at the REIT/PTF level would not be subjected to any further taxes when distributed in the following years.
Withholding tax (12 – 14)	Details of requirements to be complied with in relation to withholding tax deductions when distributing income to a unit holder who is not a resident company are provided in para. 12. Among these are: a) Amount withheld must be remitted to the DGIR within 1 month after distributing the income to the unit holder; b) Payment of withholding tax is on a global basis, i.e. it will be recorded by the LHDNM as a whole without details of each recipient. c) Form CP 37E must be submitted by the payer to furnish particulars relating to the payer as well as the deduction (refer para. 12.4 of PR for details). Addresses to which the Form (together with payment of withholding tax) is to be submitted is given in para. 12.5. If the payer fails to deduct and pay withholding tax under S.109D(2), the amount which the payer fails to pay shall be increased by 10% and the amount which he fails to pay and the increased sum shall be debt due to the government and payable immediately to the DGIR [S.109D(3)]
Filing of Return Form TR (15)	*Return form for REIT/PTF* A REIT/PTF must file a return of income on Form TR within 7 months from the date following the close of its accounting period (Example 18).
Appendices	The PR contains the following Appendices: Appendix 1 – Special Tax Treatment Accorded to REIT/PTF Appendix 2 – Specimen sample of a REIT/PTF distribution voucher

Members may read the PR at the websites of the Institute and the LHDNM.

You may write to the Institute at technical@ctim.org.my or secretariat@ctim.org.my in respect of any suggestions, concern or comments you may have on the PR so that we may raise them to the LHDNM.

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