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CHARTERED TAX INSTITUTE OF MALAYSIA (225750-T)

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TO ALL MEMBERS

TECHNICAL

Direct Taxation

PUBLIC RULING NO. 3/2016 – TAX TREATMENT ON INTEREST INCOME RECEIVED BY A PERSON CARRYING ON A BUSINESS

The above Public Ruling (PR) was issued on 16 May 2016. Its objective is as stated in the title.

Definitions

Terms	Meanings
"Interest	The return or compensation for the use of or retention by a person of a sum of money belonging to or owed to another.
Assessment	Any assessment or additional assessment made under the ITA.

The other terms (person; statutory income; basis period) have meanings which are in accordance with their definitions in the ITA.

Tax treatment

The contents of the PR are summarized below:

Para No. in Ruling	Subject Matter & Summary
4	*Sources of interest income* • Paragraphs 4.1 to 4.4 provide brief explanations of the nature of the following financial products which constitute sources from which interest income is derived: 1. Financial deposit product – Fixed deposit account and savings account; 2. Negotiable instrument of deposit (NID) 3. Repurchase Agreement (Repo) 4. Debenture, mortgage and loan • Gains or profits from savings account and investments with Islamic banks: - In Islamic banking which is conducted in accordance with Syariah law, the concept of interest does not exist but Islamic banking dealings concerning the operation of savings accounts or investments are based on the relationship between the operator (bank) and the capital provider (customer). - Nevertheless, for the purposes of income tax, S2(7) of the ITA provides that any reference in the ITA with regards to interest, shall apply, mutatis mutandis, to gains or profits received and expenses incurred in lieu of interest, in transactions conducted in accordance with the Syariah principle.
5	*Tax treatment of interest* • Interest income is chargeable to tax under S4(a) or S4(c) of the ITA. (All sections referred to hereafter are sections in the ITA.) • From YA 2013, a new S4B provides that interest income cannot be charged to tax under S4(a) (business income) except for interest that falls under S24(5). • Under S24(5) interest is assessed as business income under S4(a) if – a) the debenture, mortgage or other source to which the interest relates, forms part of the stock in trade of a person; or b) the interest is receivable by a person in the course of carrying on a business

	of lending money and that business is licensed under any written law. • Other than the above, all interest received in the course of carrying on a business is to be assessed under S4(c). This includes : a) Interest charged for delay in payment of a trade debt; (Example 1) b) Interest from an easy payment plan; (Example 2) c) Interest from the Housing Development Account (operated by a housing developer), or client accounts of other professionals; d) Interest from fixed deposit placed as security; (Example 3) e) Interest arising from excess cash from working capital placed in investments (short or long term); (Examples 4 & 5) f) Interest from loans to employees; (Example 6) g) Interest received by an estate administrator after the death of a money lender (from the business of the money lender which has ceased after his demise). • *Savings and transitional provisions* Where interest that has been assessed under S4(a) is required to be assessed under S4(c) from YA 2013 (pursuant to S4B), there may be unabsorbed losses or capital allowances carried forward to YA 2013. The unabsorbed losses ("b/f loss/es") or CA ("b/f CA") relating to such interest income are dealt with as follows: a) b/f loss is deductible against the aggregate of statutory income (SI) of any other business sources for YA 2013 and subsequent years of assessment until fully absorbed. (Example 7) b) If there is no aggregate SI from a business for YA 2013 and subsequent YA, the loss can be deducted against the adjusted income from non-business sources until fully absorbed. (Example 8) c) Where there are more than one business source, the taxpayer can choose either to deduct b/f losses, or b/f CA in order to achieve optimum tax efficiency. Similarly if there is a mixture of business and non-business sources, the taxpayer is allowed to use b/f CA to reduce the SI of any of the business sources for YA 2013 and subsequent YA. If there is no business source, b/f CA can be deducted against adjusted income from other sources until the allowances are fully absorbed. (Example 9) To facilitate the application of the above, taxpayers are advised to record separately carried forward losses relating to interest income that has been assessed as business income prior to YA 2013 for ease of identifying the amount involved.

Members may read the PR in full at the website of the Institute and the LHDNM.