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## NATIONAL TAX CONFERENCE 2014

Mergers & Acquisitions

Fighting Tax Evasion through Exchange of Information

GST Special Schemes


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CHARTERED TAX INSTITUTE OF MALAYSIA

The Chartered Tax Institute of Malaysia (CTIM) is a company limited by guarantee incorporated on 1 October 1991 under Section 16(4) of the Companies Act 1965. The Institute's mission is to be the premier body providing effective institutional support to members and promoting convergence of interest with government, using taxation as a tool for the nation's economic advancement and to attain the highest standard of technical and professional competency in revenue law and practice supported by an effective Secretariat.



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# Tax Guardian

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# Tax Guardian

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OCTOBER 2014

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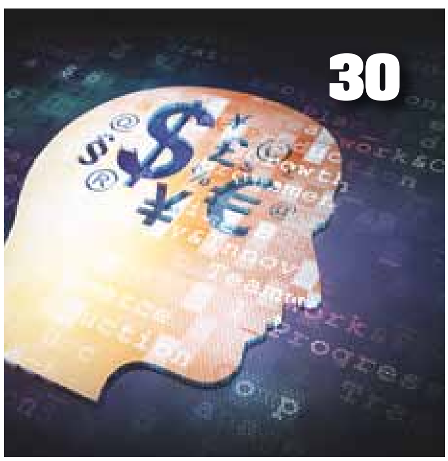



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**INVITATION TO WRITE**

The Institute welcomes original contributions which are of interest to tax professionals, lawyers, academicians and students. They may cover local or international tax developments. Article contributions should be written in UK English. All articles should be between 2,500 to 3,500 words submitted in a typed single spaced format using font size 10 in Microsoft Word via email.

Contributions intended for publication must include the author's name, contact details and short profile of not more than 60 words, even if a pseudonym is used in the article. The Editorial Committee reserves the right to edit all contributions based on clarity and accuracy of contents and expressions, as may be required.

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ARULJOTHI KANAGARETNAM

# INAUGURAL MESSAGE FROM THE PRESIDENT

Since the last issue of the *Tax Guardian*, several events and changes have taken place in CTIM. To begin with, we had our 22nd Annual General Meeting (AGM) on 14 June 2014 and I was elected as the CTIM President for the 2014-2015 term by the CTIM Council. At the same time, the CTIM Council also elected Mr. Poon Yew Hoe as the CTIM Deputy President. I would like to thank the CTIM Council for giving me their full support and confidence.

I would also like to thank past CTIM Presidents for the enduring legacy that they have built in CTIM. Special thanks go to Mr. SM Thanneermalai (CTIM President for the three years from 2011 to 2014) who has done so much to increase the profile and visibility of CTIM as a premier body for tax professionals and for enhancing services to members. Together with the CTIM Council, I look forward to continue and enhance this legacy.

The National Tax Conference (NTC) 2014 that is jointly organised by CTIM and the Inland Revenue Board Malaysia (IRBM) was attended by more than two thousand participants on 12 and 13 August 2014. For the first time in the NTC, an international speaker from OECD, Paris, spoke to the audience via live video conferencing. The key event of the NTC 2014 was the round table discussion moderated by Mr. SM Thanneermalai which involved the participation of the IRBM CEO, YBhg Tan Sri Dr. Mohd Shukor Hj Mahfar, and the Director-General of the Royal Malaysian Customs Department (RMCD), YBhg Dato' Sri Khazali Hj Ahmad.

Next, it gives me great pleasure to update you on the key goings on in CTIM over the past few months.

## TECHNICAL – DIRECT AND INDIRECT TAX

As those of you who have been following our e-CTIMs are aware, CTIM has been following up with the IRBM since the first quarter of this year on IRBM's requirement for dormant

companies to file the income tax return forms (ITRF). In its letter dated 18 August 2014, the IRBM agreed to CTIM's appeal to implement the requirement prospectively from year of assessment (YA) 2014. Further clarifications requested by members were taken up in CTIM's letter dated 3 September 2014 to the IRBM. Subsequently, CTIM led by myself met with the IRBM Deputy CEO (Tax Operations) and his senior officers on 19 September 2014. At the meeting, the IRBM conveyed to us their reasons for requiring the dormant companies to file the ITRF and verbally confirmed the following:

All dormant companies must file the income tax return form (ITRF) with effect from YA 2014. This includes companies which have not commenced operations.

Upon receipt and review of the ITRF for YA 2014, for the dormant companies, the IRBM will determine whether prior year ITRFs need to be submitted on a case to case basis.

Dormant companies are required to submit the Form CP204 with effect from YA 2016 subject to the provisions of Section 107C(4) and Section 107C(4A) of the Income Tax Act 1967 (ITA).

On a separate note, CTIM has completed the memorandum on the review of the ITA under the self-assessment system of taxation. The memorandum was submitted to the Ministry of Finance (MoF) in September 2014 with a request for a dialogue to engage both the MoF and the IRBM for their views on CTIM's proposals. We hope that this will bring about a positive outcome for taxpayers and tax practitioners alike.

With the introduction of the GST Act 2014 and the GST Regulations in June / July 2014, CTIM has been working hard to review and identify issues arising from the GST legislations. To this end, CTIM has prepared and submitted a preliminary feedback on issues arising from the GST Regulations to the RMCD and the MoF in September 2014. Issues from members on GST implementation are also welcome and can be addressed to the CTIM Secretariat.

## CONTINUING PROFESSIONAL DEVELOPMENT (CPD)

Since the NTC 2014, CTIM has

organised several other CPD events including three 6-day GST training courses with the RMCD in Kuala Lumpur and other major Malaysian cities as at 25 September 2014. Four more GST training courses are scheduled for the rest of 2014. Attending the 6-day GST training course and passing the GST examination have taken on an added significance as the authorities have made it part of the prerequisites for GST tax agent licence applications.

A key event which is the 2015 Budget Seminar was jointly organised by CTIM with input from the MoF, IRBM and RMCD. This Budget Seminar was held on 29 October 2014 at the Renaissance Hotel, Kuala Lumpur. This will be followed by Budget Seminars in other major cities around Malaysia. It may please you to note that attendees for this event will be accorded 10 CPD points which is recognised by the MoF for the purposes of applying for or renewing the tax agent licence under Section 153(3) of the ITA. Do register early to avoid disappointment.

## PUBLIC PRACTICE

June / July 2014 marked the issuance of the Guidelines and Regulations on the GST tax agent licence by the authorities. Subsequently, CTIM with the support of other professional bodies proposed amendments to the Guidelines and changes to the online registration system to enable qualified persons to apply for the GST tax agent licence. I welcome the positive and prompt action taken by the MoF and the RMCD in attending to our proposals. The amended Guidelines and the changes to the online registration system in August 2014 are evidence of the authorities' commitment on GST. We look forward to similar outcomes with the authorities as more and more issues on GST implementation come to the fore.

Members in public practice would also be interested to know that the IRBM's minutes of DESIRE Dialogue Meeting No. 1/2014 released on 19 August 2014 announced their intention to only entertain tax agents approved under Section 153(3) of the ITA on tax related matters with effect from 1 December 2014. We have heard the concerns of many members regarding this announcement and we have taken steps to write to the IRBM with our collective views. We hope to have a dialogue with the IRBM and come to an amicable position together on this matter.

## MEMBERSHIP

I am pleased to inform you that, as at 25 September 2014, the CTIM membership has increased to 3,171. I would like to thank the members for the high regard that they have for CTIM which is reflected in the increase in membership.

We successfully held our Members' Technical Dialogue on 30 September 2014 with attendance at full capacity. Technical and public practice issues addressed by our panellists together with feedback from the floor helped to make this a lively event. If the demand from members is good, we may hold these dialogues more frequently.

## EXAMINATIONS

Finally, I bring you some exciting news in the area of examinations. As announced at the CTIM AGM on 14 June 2014 and at the CTIM Graduation Ceremony on the same day, CTIM has restructured its examination syllabus, consolidated and reduced the number of examination papers from ten to eight and reduced the number of examination levels from three to two with effect from the December 2014 examinations onwards. In addition, the tax technician qualification will also be introduced with effect from the December 2014 examinations onwards for students who have completed the required number of examination papers at the intermediate level under the new syllabus. It is hoped that this would contribute to an increase in the number of competent tax professionals in our country.

## IN CLOSING

If the past few months are a reflection of what the future might be, then we are in for an exciting close to the year. I am optimistic that the 2015 Budget announcement on 10 October 2014 and subsequent events will bring the year 2014 to an end on a high note. More to come in the next issue of the *Tax Guardian*.

# Editor'sNote

K. SANDRA SEGARAN

# A DIVERSE RANGE OF TAX CONSIDERATIONS FOR THE DISCERNING PRACTITIONER

In this final issue of the year, we bring you a useful summary of the 2014 National Tax Conference. Members who missed the conference will certainly find this useful. The two-day conference was well attended. It had an array of speakers who are thought leaders from various areas and eminent personalities from overseas as well as from Malaysia. The salient issues in each session are summarised succinctly.

In this issue, Goh Kah Im provides a brief comparison of the incentives available to a Labuan entity with those in other parts of Malaysia. In addition to the preferential tax treatment, withholding tax exemption, stamp duty exemption for instruments, the discussion also includes the often overlooked indirect tax benefits. The author highlights the finer details in relation to treaty benefits that need careful scrutiny before concluding a benefit is available for a Labuan entity.

Nicholas Crist in his article outlines the key Malaysian direct tax issues relevant to mergers and acquisitions (M&As). Particular reference is made to M&As that involve Malaysian real property, whether in the form of land rich companies or direct interests in Malaysian realty. This analysis is within the confines of the prevalent laws or the lack of it in Malaysia. The scope of the article excludes discussion on Income Tax (Exemption) (Order No. 12) 2013 for qualifying services of SMEs.

Anti-avoidance continues to draw interests from taxpayers and analysts both domestically and internationally. Dr. Benjamin Poh examines in an academic style common law principles in relation to the Commonwealth courts' treatment and development

of the law in this area with particular reference to the "choice principle" and draws comparisons from several jurisdictions in the Commonwealth on the introduction of General Anti-Avoidance Rules (GAAR).

Esther A.P Koisin, a senior officer from the IRB provides some insight into the Exchange of Information (EOI) articles in our tax treaties, the pace of which has increased due to the international developments on this issue. The cooperation between taxing jurisdictions has reduced cross-border transactions to a level playing field, devoid of borders. International arrangements demand that reviews are conducted to ensure the availability of legal and compliance framework within the domestic law. With this, prospective evaders will have little to conceal, including banking information.

Our regular contributor, Dr. Nakha Ratnam critically examines IRB's Public Ruling No. 1 of 2014 on Special Classes of Income which attracts withholding tax when payments are made to non-residents. With the impending implementation of GST, Lindsey Cruickshanks analyses special schemes within the new regime, drawing from her experience in Europe. Our regular columns on other technical matters continue to adorn the *Tax Guardian* to provide the learning opportunity for discerning members and students.

**ERRATA**
Exhibit 2 (Inventory of MAP Cases at the End of Reporting Period) in the article titled **International Tax Dispute Resolution - Mutual Agreement Procedure Route** (page 31) in *Tax Guardian Vol7 No 3 (July 2014)* was erroneous. We reproduce the correct version *(on the right)*. We regret the error.

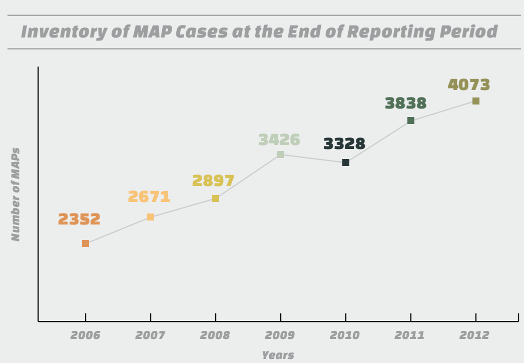


**EXHIBIT 2: INVENTORIES OF MAP CASES**


Fulfilling your needs is what we do best.
SAVINGS AND INVESTMENT
BANK ISLAM CARD-i
HOME FINANCING-i
CURRENCY EXCHANGE
TREASURY
WILL WRITING
VEHICLE FINANCING-i
PERSONAL FINANCING-i
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**President**

Aruljothi A/L Kanagaretnam

**Deputy President**

Poon Yew Hoe

**Council Members**

Thanneermalai A/L SP SM Somasundaram

Datuk Tan Leh Kiah

Prof. Dr. Jeyapalan A/L Kasipillai

K. Sandra Segaran A/L Karuppiah

Lew Nee Fook @ Liu Nee Choong

Nicholas Anthony Crist

Ong Chong Chee

Phan Wai Kuan

Renuka Thuraisingham

Seah Siew Yun

Yeo Eng Ping

Farah Rosley

Goh Lee Hwa

Datuk Harjit Singh Sidhu

# 22ND ANNUAL GENERAL MEETING

The Chartered Tax Institute of Malaysia (CTIM) held its 22nd Annual General Meeting (AGM) on 14 June 2014 at the Seri Pacific Hotel Kuala Lumpur. A total of 64 members attended the AGM.

Pursuant to Article 59, Poon Yew Hoe was re-elected to the Council.

Pursuant to Article 57 (ii), the following were elected as new members of the Council:-

1) Farah Rosley
2) Goh Lee Hwa
3) Datuk Harjit Singh Sidhu

The first Council meeting for the 2014/2015 term was held on the same day. Pursuant to Article 63, the Council elected from amongst the Council Members as listed below for the term 2014/2015, the President and the Deputy President.

***President***
Aruljothi A/L Kanagaretnam

***Deputy President***
Poon Yew Hoe

***Council Members***
Thanneermalai A/L SP SM Somasundaram
Datuk Tan Leh Kiah
Prof. Dr. Jeyapalan A/L Kasipillai
K. Sandra Segaran A/L Karuppiah
Lew Nee Fook @ Liu Nee Choong
Nicholas Anthony Crist
Ong Chong Chee
Phan Wai Kuan
Renuka Thuraisingham
Seah Siew Yun
Yeo Eng Ping
Farah Rosley
Goh Lee Hwa
Datuk Harjit Singh Sidhu

The Council Members are all committed to the Institute by pledging their own time and resources to the objectives of the Institute and in achieving its mission.

# CESSATION OF MEMBERSHIP

The following members have been excluded from the Membership Register on 30 June 2014 in accordance with Article 28 of the Articles of Association of the Institute:-

| NAMES | MEMBERSHIP NO |
|---|---|
| Jeffrey Lim Hup Choon | 0434 |
| Lou Juan Suan | 0725 |
| Lim Boon Kiat | 0767 |
| Lee Cheng Swee | 1082 |
| Lim Hiok Sen @ Ling Sik Seng | 1097 |
| Chua Lian Chooi | 1102 |
| Tham Ming Yong | 1138 |
| Nasibah Aminy Bte Jamaluddin | 1120 |
| Kamolnat Kijvanit @ Teoh Ai Koon | 1152 |
| Kwan Ming Hap | 1222 |
| Lee Voon Siong | 1239 |
| Low Ten Pow | 1275 |
| Othman Bin Abdullah | 1403 |
| Chew Theam Hock | 1611 |
| Lau Ngi Huk | 1664 |
| Mohamad Isa Bin Yeop | 1731 |
| Wong Tuck Fook | 1852 |
| Yap Fatt Lam | 1914 |
| Rohizan Binti Hamzah | 1993 |
| Ab Rahim Bin Abdullah | 2047 |
| Low Fue Cheu | 2115 |
| Norazman Bin Daud | 2249 |
| Too Chang Kit | 2264 |
| Yee Yu Ket | 2298 |
| Angie Ng Cheng Ling | 2323 |
| Loh Yui Hin @ Loh Kam Choon | 2459 |
| Lee Kok Wah | 2505 |
| Tan Ah Hong | 2524 |
| Johari Bin Padiman | 2597 |
| Wong Yok Ngo | 2779 |
| Wong Shiau Cin | 3019 |
| Hor Pey Wah | 3045 |
| Ahmad Imran Bin Zamzam | 3057 |
| Hoh Kiang Theng | 3147 |
| Sabrina Sim Siok Tiang | 3203 |


# NATIONAL TAX CONFERENCE 2014

**THE NATIONAL TAX CONFERENCE (NTC) 2014 WAS HELD AT THE KUALA LUMPUR CONVENTION CENTRE ON 12 AND 13 AUGUST 2014 AND THIS TWO-DAY SIGNATURE EVENT WAS JOINTLY ORGANISED BY THE CHARTERED TAX INSTITUTE OF MALAYSIA (CTIM) AND THE INLAND REVENUE BOARD OF MALAYSIA (IRBM).**

This year's theme was on *Taxation: Harnessing Synergies Towards Sustainable Growth*, and the sessions covered the economic outlook for Malaysia, dispute resolution, tax enforcement and the Anti-Money Laundering and Anti-Terrorism Financing Act (AMLATFA), base erosion and profit shifting (BEPS), tax cases update, tax incentives and a special round table discussion on current issues affecting taxpayers.

## CLOSE COLLABORATION AND EXPANDING AREAS OF CONCERN

***(Welcoming speech by Aruljothi Kanagaretnam, CTIM President)***

Congratulating the joint CTIM-IRBM conference organising committee, CTIM President, Aruljothi Kanagaretnam observed that it was their close cooperation and mutual respect for each other that has resulted in successful conferences since 2001. "This year's theme brings thought leaders together on many platforms within the programme," he said. "The topics affect the tax fraternity and taxpayers. AMLATFA, for instance, poses significant challenges, as does BEPS."

## IMPROVING PERFORMANCE AND SERVICE DELIVERY AND ACHIEVING SUSTAINABLE GROWTH

***(Opening address by YBhg Tan Sri Dr. Mohd Shukor Hj Mahfar, CEO of IRBM)***

Delivering the opening address, YBhg Tan Sri Dr. Mohd Shukor said that the conference theme was timely, as closer interaction between the different enforcement agencies was becoming increasingly necessary by the day, and there was a need to harness the respective agencies' synergies more effectively to improve performance and service delivery. "We also need to achieve sustainable growth," he said. "For this, we will need good connections with our partners, so that we can have more effective interaction. We are constantly looking for ways to streamline our operations so that we can provide taxation services of quality


*Presentation of souvenir to Dato' Zamani Abdul Ghani, Chairman of Bank Islam Malaysia Berhad, a platinum sponsor of the 2014 National Tax Conference.*

and integrity." He added that IRBM fully supported and was working towards voluntary compliance.

## CHANGING PUBLIC PERCEPTION

***(Keynote address by guest of honour Y.B. Dato' Seri Haji Ahmad Husni Mohamad Hanadzlah, Finance Minister II)***

Guest of Honour Y.B. Dato' Seri Haji Ahmad Husni Mohamad Hanadzlah (Finance Minister II) congratulated CTIM and IRBM on its fourteenth edition of the NTC, saying that the conference had been instrumental in changing public perception. "People are beginning to see that tax is not a burden but a responsibility," he said. "Both bodies have also been able to build better images as friendlier, more approachable and efficient organisations." He noted that tax revenues collected over the years have been increasing.

"We have high expectations of IRBM, which has shown a steady increase in revenue collection, and consistently achieved its targets. In 2013, RM129 billion was collected. The target for 2014's collection is RM140 billion. IRBM will move forward as an autonomous body. This will give it greater efficiency in collections." He urged participants to use the conference as a platform to share knowledge and gain experience.

## TOPIC 1 : ECONOMIC OUTLOOK FOR MALAYSIA - WHAT LIES AHEAD

The conference sessions kicked off with the economic outlook for Malaysia, chaired by Dr. Yeah Kim Leng (Dean of School of Business, Malaysia University of Science & Technology). "The economy saw real Gross Domestic Product (GDP) growth of 7.4% in 2010. Since then real GDP growth has been averaging around 5.2% in the last three years. Both the World Bank and the International Monetary Fund (IMF) have a fairly positive outlook of the Malaysian economy but that does not mean plain sailing. We still have to weather the approaching headwinds of possible financial straightening, and be aware of the outlook for the global economy, and how it will affect Malaysia."

The session speaker, Prof. Dr. Zakariah Abdul Rashid, is the Executive Director of the Malaysian Institute of Economic Research (MIER). His presentation covered selected key economic indicators, MIER 2Q 2014 surveys, near-term outlook, downside risks and policy directions. Remarking that Malaysia's trade balance has always been positive, with exports exceeding imports, he confirmed, however, that this gap has recently been narrowing, and in the months to come, we may see an increase in imports over exports. "We were lucky because of some degree of global economic recovery," he said. "Currently, we are experiencing slightly improved growth but imports will at some point overtake exports; trade balance is already narrowing now. Malaysia is small, and we have to rely on external demand."

"Today, we need to grow in a way that will allow us to achieve our aspirations," he continued. Pointing out that our main trading partners – Singapore, China, Japan, US and the EU – all had problems of their own, he mentioned that while trade had declined with China, goods traded with Singapore were mostly re-exported, which meant that Singapore was able to add value to them. "We are very busy, but at the end of the day, our activity is of less value compared to that of our trading partners," he said. "We have to create higher value. Import/export is just a vehicle; it is how much value we


create from it, which is the core issue. Right now, we are creating very little."

### *Inflows and outflows*

It is important to note that with the narrowing import-export margin has come an increase in investments abroad by Malaysian companies. In fact, more local companies have been investing abroad than locally. From January 2014 to May 2014, investment approvals by Malaysian Investment Development Authority (MIDA) for manufacturing projects totalled RM41.7 billion which is equivalent to 2012 approvals and hopefully will surpass 2013 approvals. Out of this amount, RM16.5 billion was from domestic investors while the remaining RM25.2 billion came from foreign applicants. These investments can potentially provide 39,567 jobs – a figure that has also declined in recent years.

"Our short-term external debt is quite substantial," he cautioned. "As of 31 July 2014, the international reserves was USD131.8 billion which is 1.3 times the short-term external debt. We have to keep an eye on it. Also, the Ringgit has depreciated substantially against other currencies." As at June 2014, core inflation has remained at a steady 3.2%, with the Food Index and Consumer Price Index (CPI) at 3.5% and 3.3% respectively, but inflation has been rising persistently since December 2008. As for employment, the total labour force in Malaysia was 14.05 million as at May 2014, with an unemployment rate hovering around the 3% level.

### *The bigger picture*

ASEAN countries have also been exhibiting encouraging growth, making the region one to watch in the years to come. The MIER expects Malaysia's real GDP to grow 5.3% in 2014, with expansion of between 5.5% and 6.0% in 2015. In fact, GDP touched the 6.2% mark for Q1 2014, driven mainly by domestic demand. "But 6.2% growth in Q1 2014 will not be sustainable for the rest of the year," Prof. Dr. Zakariah said. "Inflationary pressures were strong in the first quarter of 2014." A careful eye has to be kept on short-term stability, as the balance of payments has deteriorated during the quarter, with stronger outflows from financial accounts. "Federal government finance remains weak," he added. Growth will be moderately higher for 2014, continuing in 2015.

### TOPIC 2 : DISPUTE RESOLUTION – AN ALTERNATIVE TO LITIGATION

The second topic of the NTC was on Dispute Resolution. Chaired by Jeremy Lee Eng Huat (CEO of the Financial Mediation Bureau), the speaker for this session was Abu Tariq Jamaluddin (Director of Dispute Resolution Department, IRBM). He stated that Dispute Resolution promotes mediation as an alternative to the lengthy litigation because court cases are difficult. "They are hard to resolve and can take at least four years, starting from the day the appeal is filed," he said. "They also depend on many things. From my experience, certain cases can be resolved if the parties involved can accept the pros and cons of the situation."

He said every case had its strengths and weaknesses; it was therefore important to consider an alternative to the legal process. "The most important element of dispute resolution is to have a platform for the process," he continued, adding that this was something the authorities were encouraging, and for which the Dispute Resolution Department had recently been established. "Dispute resolution is a platform to resolve an appeal once the matter has been raised against the taxpayer," he said. His comprehensive presentation on dispute resolution covered the sources of dispute, right of


appeal, procedure of appeal, the dispute resolution process, legal status, benefits and issues resolved, among others.

"There is no amendment to the Income Tax Act to allow for the dispute resolution process," he clarified. "An appeal is normally filed because the taxpayer does not agree with IRBM's findings, and the taxpayer is of the view that they acted in good faith." Many instances can lead to disputes in court, with the taxpayer challenging IRBM, and proving that he/she is not chargeable or liable to the assessment made by IRBM. Taxpayers can file a notice of appeal (Form Q) within 30 days of the date of assessment. "It is easier to fill in a Form Q than to draft a letter stating the problem," advised Abu Tariq. "You can do this at any branch. Once a Form Q is filed, the Director-General can then determine whether the taxpayer has grounds for appeal." He added that all appeals must be submitted in a Form Q as a letter of objection is no longer accepted.

### *Finding solutions*

The dispute resolution process does not involve third parties. When a Form Q is received, it goes to the Appeal Review Panel (ARP) or the Dispute Resolution Proceeding (DRP). The ARP may decide on one of three possible outcomes: that the appeal is allowed; that the matter be forwarded to the Special Commissioners for

Income Tax (SCIT); or that the appeal be sent to the DRP. The taxpayer will be informed of the next step of the process. "Notwithstanding whatever has been said, the DRP can be held at the request of the taxpayer," he explained. "Both sides will be heard and a workable solution will be found." Dispute resolution aims to resolve or limit issues in the dispute, and make things more accessible while using resources more efficiently.

Although the procedure is quite informal, the outcomes are lawful, and usually effective and acceptable to all parties. The rule of evidence is not strictly followed, and the process is confidential and without prejudice, with parties bearing all costs. Taxpayers are informed of the decision within one month. "This procedure saves costs and time as it is simple although a great deal of expertise is applied," Abu Tariq said. "It gives taxpayers the opportunity to be heard in a non-formal environment by experienced officers." So far, 38 cases have been selected for dispute resolution, and of these, 25 have been settled. Mediation is preferred in some countries like the

UK, Australia and the Netherlands, whose best practices are the basis of the dispute resolution process locally.

### TOPIC 3 : FORUM - TAX ENFORCEMENT & ANTI-MONEY LAUNDERING AND ANTI-TERRORISM FINANCING ACT

The AMLATFA was the focus of Topic 3 of the conference. Moderated by Adzhar Sulaiman (Co-Organising Chairman of NTC 2014 and Director of Malaysian Tax Academy, IRBM), its panellists were Abdul Rahman Abu Bakar (Director of Financial Intelligence & Enforcement Department, Bank Negara Malaysia (BNM)), Amnah Tawil (Director of Enforcement Cooperation Division, Investigation Department, IRBM) and Anand Raj (a partner with Shearn Delamore & Co). In a quick overview of AMLATFA, Adzhar Sulaiman said that it was not new, having first been enacted in 2001. What was of interest today were the current amendments to the Act, which was gazetted on 8 August 2014. AMLATFA is intended to stem revenue leakage, especially when it threatens the security and stability of the country, through enhanced policing of financial instruments, cross-border financing and ensuring the transparency of agencies seizing assets for investigations.

#### *A matter of national security*

Abdul Rahman Abu Bakar stressed, "Money laundering erodes a country's financial stability. It encourages crime and distorts the economic sector, particularly in external trade. Countries like Malaysia, which have offshore financial centres, especially need anti-money laundering policies." A total of 299 serious crimes from 47 legislations are covered by the AMLATFA, including Sections 112, 113 and 114 of the Income Tax Act (ITA). "In 2009/2010, BNM started investigations of money changers," said Abdul Rahman. "It found a lot of individuals and companies used money changers to remit money overseas to avoid the IRBM from being able to trace the movement of funds. BNM

then engaged the IRBM and started looking at it. That is one of the reasons why the offences of Sections 112, 113 and 114 were brought into serious crimes under the AMLATFA. "

Under the AMLATFA, there is a provision for organisations to submit reports of suspicious activities by their clients. This information, as well as information received about financial institutions which are experiencing irregularities, is shared among the authorities because of national security concerns and the implications of these actions. "Tax evasion deprives the state of revenue, and is a risk for the country. If there is no compliance, the country runs the risk of being "grey listed" by other countries and international finance bodies like the World Bank and IMF." He noted that in countries like Australia, Singapore and the US, tax crimes were the basis of anti-money laundering laws.

Tax enforcement is a very wide topic covering detection, auditing, investigation and enforcement. Said Amnah Tawil, "You cannot do the first three without doing the enforcement part." She confirmed that the emphasis today was on investigating money laundering activities; information-sharing and joint operations between various government agencies were increasing. "Working in silos is history," she confirmed. One of the basic offences under money laundering was when a tax agent was aware of a client concealing money but keeps silent about it. This will make the tax agent liable to prosecution as well. "Taxpayers often query why they have been picked," she revealed. "But selection of cases is never random; due diligence is done before investigations start."

#### *Far-reaching implications*

Under AMLATFA, the power of IRBM's Investigation Department is wide, to the extent of allowing it to seize property and freeze accounts to assist in investigations. "Bank accounts of taxpayers are no secret," she confirmed. "When suspects engage in unlawful activity, and bring suspicious funds into the country, they can be charged, and their property can be forfeited." The vigilance of the authorities resulted in 106 cases worth RM341 million brought to book in 2011, 31 cases totalling RM218 million in 2012, and 86 cases worth RM210 million in 2013. "Please inform your clients so that they will be more compliant taxpayers," she advised. Even seemingly minor infringements can bring about heavy penalties.

Anand Raj, traced the evolution of AMLATFA from 2001 to the present, clarifying details of what constitutes a reporting institution and what does not. "If certain Acts are violated, this is also considered money laundering," he remarked. He identified Sections 112, 113 and 114 of the ITA as possible areas of contention, pointing out that even if tax agents gave bad advice to clients, which resulted in clients evading tax, the tax agents could be considered money launderers. With this in mind, he is of the view that taxpayers would "resist penalties under Section 113(2) to avoid the possibility of imprisonment."

To mitigate the situation on how Section 113(2) may be applied inadvertently, he suggested that amendments be made to introduce a decriminalised set of penalties. Proffering IRBM's perspective, Amnah Tawil reiterated that AMLATFA-related cases were not randomly selected. "They are actually very carefully picked," she said. "In many instances, there are other reasons related to the parties involved, or aspects of the matter to be considered, which is done before selecting which case to bring before the Courts."

Day 2 of the conference started off with a recap of day 1 by Yeo Eng Ping (Co-Organising Chairman of NTC 2014). She quoted the CEO of IRBM, "We aim to see compliance driven by knowledge not just regulations. Taxpayers to be kept informed through relationships, not through authority. We look to deliver service through partnerships, not just through procedures. Compliance has to be founded in a sense of responsibility, not achieved through mere strict enforcement." She added, "Prof. Dr. Zakariah and Dr. Yeah shared the big picture on the Malaysian economy and how taxes play a critical role in managing the macroeconomy." "We heard that tax offenses attract the operation of the AMLATFA. But at the same time we heard the message that the powers that are there will be exercised judiciously." "It was also positive to hear the IRBM embarking on a bold move to create the dispute resolution process to provide greater accessibility for taxpayers to be heard by the IRBM on tax disputes."

## TOPIC 4 : BASE EROSION AND PROFIT SHIFTING

Topic 4 on BEPS was chaired by Poon Yew Hoe (CTIM Deputy President). This session saw international speakers Paul Drum and David Bradbury talk about the background of BEPS, and the efforts that are being put in place internationally to combat this trend. Drum is the Head of Policy at CPA Australia; Bradbury is the Head of Tax Policy & Statistics Division, Centre for Tax Policy and Administration, Organisation for Economic Co-operation and Development (OECD). Bradbury spoke via video conference link from his office in Paris. The panellist for this session was Noor Azian Abdul Hamid (Director of Multinational Tax Department, IRBM). BEPS is primarily arising from multinational corporations (MNCs) attempting to reduce their tax obligations.

Big companies have been accused of paying less than their fair share of taxes, which is detrimental to the countries they are operating in. Said Drum, "One example is an American MNC in Australia. It made billions but may have paid less than one per cent of what was due in taxes. This is not fair when seen in the light of the fact that taxes on individuals and small and medium enterprises (SMEs) have increased in many countries in Europe in recent years. Everyone is trying to capitalise on whatever loopholes they can find, and multinationals are getting particularly good at this." He conceded, however, that BEPS was not an easy thing to handle despite being addressed at global level. "It is a smart way of operating, and currently is not illegal," he continued. "Big companies can avoid it; small ones can't. This is unfair and damages the economy."

MNCs can end up paying less tax than even local companies as they are able to shift their profits around the world to avoid taxation. To mitigate the situation, OECD has come up with a plan, the OECD/G20 BEPS Action Plan. "Most of these profit-shifting activities are currently legal," said Bradbury. "But all this is occurring against a backdrop of countries having to balance their fiscal positions. So if companies are seen to be evading their tax responsibilities in their host country, it gives rise to dissatisfaction. All countries have the sovereign right to impose taxes as they choose. Governments and citizens are beginning to demand action."

***International response***

As commerce becomes more global and involves cross-border trade, conflicts between the taxing rights of trading countries have increased and bilateral treaties have evolved to avoid double taxation. Over time, MNCs have identified and taken advantage of some of the gaps that exist between the domestic tax laws and tax treaties, resulting in "double non-taxation," "less than single taxation" and "stateless income" – terms that essentially describe shifting of costs to high-tax countries while shifting profits to low-tax countries. The current situation, Bradbury said, was creating an uneven playing field, as SMEs which were at an economic disadvantage, were being forced to compete with MNCs. "Flaws in the system undermine a country's ability to tax, which results in a decrease in revenue," he contended. "This presents risks to businesses, and a climate of growing uncertainty. It could also give rise to unilateral action which will increase business risks."

Countries, he said, would start taking matters into their own hands, which would not augur well for global commerce. The OECD/G20 BEPS Action Plan seeks to avoid this by engaging with as many organisations, governments and monetary authorities as possible to align policies and strategies to provide a higher level of predictability and certainty worldwide. The 15 point Action Plan deliverables include seven action items in 2014 and another eight in 2015. Action items for 2014 cover addressing tax challenges in a digital economy, hybrid mismatches, harmful tax practices, treaty abuse, transfer pricing intangibles, transfer pricing documentation and multilateral instruments, while deliverables for 2015 ranged from transfer pricing risks to making dispute resolution mechanisms more effective.

"We have had regional consultations about the OECD/G20 BEPS Action Plan. It is not a simple issue to address, and Malaysia is contributing in several areas." divulged Noor Azian. She pointed out that Malaysia had been invited to be in several OECD working parties on the OECD/G20 BEPS Action Plan, the UN sub-committee on BEPS for developing countries and other UN sub-committees. The decision of the 15 point Action Plan is not binding on Malaysia as Malaysia is neither an OECD member nor a G20 country. Nine out of 15 of the action items relate to transfer pricing. The IRBM is focusing on several of the action items, types of base eroding payments and enforcement issues. There are existing domestic legislations for countering BEPS. She also said that where foreign companies are in a master-servant relationship with their parent companies, it was difficult to make them fully disclose or comply. One observation from the floor was that countering BEPS could be an effort by developed countries to recover some of the funds that had been moved to different parts of the world. Developing countries stand to lose a great deal if no action is taken.

## TOPIC 5 : TAX CASES UPDATE

YBhg Datuk Francis Tan (CTIM Council Member) chaired the session on "Tax Cases Update". The speaker was Hazlina Hussain (Director of Litigation and Tax Appeals Department, IRBM) while the panellist was Saravana Kumar (a partner with Lee Hishamuddin Allen

& Gledhill).

Hazlina spoke on several notable and pertinent tax case decisions in relation to: (i) Section 4A of the ITA in the Federal Court decision of *LHDN v Alam Maritim SB* and the Court of Appeal decision of *KPHDN v Teraju Sinar;* (ii) Cash loss in the Court of Appeal decision of *Holiday Tours & Travel SB v DGIR;* (iii) Section 140 of the ITA in the Court of Appeal decisions of *Port Dickson Power Bhd v DGIR* and *Ibraco Paremba SB v DGIR;* (iv) Penalty under Section 113(2) of the ITA in *Syarikat Pukin Ladang Kelapa Sawit SB v KPHDN* and *Sri Binaraya SB v DGIR;* (v) Appeal procedure in the Court of Appeal decisions on *Bandar Nusajaya Development SB v DGIR* and *Ta Wu Realty SB v DGIR;* (vi) Section 108 of the ITA in the Court of Appeal decision of *Positive Vision Labuan Ltd v DGIR;* and (vii) Schedule 7A of the ITA in the Court of Appeal decision of *DGIR v Success Electronics & Transformer SB.*

Panellist Saravana commented it was interesting to note that the cash loss arising from embezzlement by the employee in *Holiday Tours & Travel SB v DGIR* was held to be not deductible. He observed that negligence on the employer's part was a contributing factor to the cash loss in that case. He also pointed out that the Federal Court decision of *LHDN v Alam Maritim SB* was adopted in *KPHDN v Teraju Sinar* as all lower courts are bound by that decision until the law is amended or another case goes to the Federal Court. Commenting on *Ibraco Paremba SB v DGIR,* he mentioned the Commonwealth courts generally take the position that a transaction undertaken purely for tax efficiency purposes is tax avoidance driven. Where a transaction has a commercial purpose and tax benefit is incidental to it, courts take the view it is tax mitigation. The key thing is to establish that the transaction has a commercial purpose. Tax minimisation should not be the motive of the transaction.

## TOPIC 6 : TAX INCENTIVES – THE WAY FORWARD

Chairing the session on "Tax Incentives – the Way Forward," Nor'aini Ja'afar (Director of Tax Policy Department, IRBM) assured participants that "Tax incentives will result in less taxes." Malaysia, she said, has had a long history of giving incentives to encourage economic activity, but it was necessary to measure the impact of these incentives, and if they have been abused.  Speaker Khodijah Abdullah (Deputy Under-Secretary of the Tax Division, Ministry of Finance) said, "Incentives promote economic growth, but their long-term impact can be detrimental. Sometimes tax is waived to encourage direct domestic or foreign investment. But this means that the tax revenue stemming from the investments has to be foregone."

Tax incentives are categorised as subsidies and should be targeted at promoting economic activities which are contributing to sustainable, long-term growth, but many companies stop production when the timeframe for tax incentives runs out. After the tax incentive period, companies must contribute to the generation of revenue for the government. Both domestic direct investment (DDI) and foreign direct investment (FDI) are equally important. "We don't discriminate; tax incentives are available to both foreign and domestic investors," she said. Incentives today are usually pre-packaged but they are also more flexible and can be tailored to the needs of the investor or investment being made. They could also be based on certain locations, like the identified growth corridors in the country, such as the East Coast Economic Region or the Iskandar Development Region. Labour intensive industries such as simple manufacturing activities with low level technology are no longer incentivised.

### *Incentives must spur growth*

Tax incentives are for the facilitation of private sector-led growth; businesses need to be resilient and able to carry on even after the expiration of the incentive period. Ideally, companies should also be able to penetrate the global market. While taxpayers contribute towards these incentives as a matter of national growth, tax incentives need to be transparent and efficiently executed. Monitoring and oversight of compliance is strict, Khodijah added, with zero tolerance on deviations. "If you are self-assessing and find yourself wanting in some areas, don't claim tax incentives," she advised.

Panellist, Amarjeet Singh (a partner with Ernst & Young Tax Consultants Sdn Bhd), was of the opinion that whether incentives should be given or not was debatable. "Globally, many countries are giving incentives for agriculture, tourism and technology to encourage job creation, technology transfer and promotion of exports," said Amarjeet. "We need to look at our competitiveness, as well as that of our neighbours, and decide what to do. For example, the Multimedia Super Corridor, has reaped RM3 billion in new investments in 2013, and created 138,071 jobs as at 2013. By comparison, the Iskandar Development Region has attracted RM25.3 billion in new investments in 2013, and created 554,796 jobs as at 2012.

He also spoke on "outcome-based incentives" citing South Korea as an example where tax rates were reduced for corporations which were able to meet/exceed certain agreed outcomes. "Today, when we ask for incentives, there has to be an illustration of what the advantages of this are. There will also be increased scrutiny of companies with regard to compliance. Please remember that tailor-made incentives require tailor-made conditions, so don't stick too rigidly to set plans. Be flexible," he advised. He also made a request for: (i) a system to be in place to ensure taxpayers' compliance with the tax incentive conditions; (ii) clarity and guidance on the interpretation of the tax incentive conditions; and (iii) flexibility even if one of the tax incentive conditions was missed.

The last word on tax incentives was that the country had limited financial resources, and therefore the tax incentive environment was changing. "Incentives can be given only if we are sure there is long-term benefit. We are becoming more selective," Khodijah said.

## TOPIC 7 : ROUND TABLE DISCUSSION ON CURRENT ISSUES AFFECTING TAXPAYERS

The highly-touted "Round Table Discussion on Current Issues Affecting Taxpayers" saw, for the first time ever, the heads of the two major revenue-collecting authorities in Malaysia, on the same stage. "A total of RM180 billion is (targeted) to be collected by IRBM and RMCD," said session chairperson SM Thanneermalai (immediate past President of CTIM). "Between them, YBhg Tan Sri Dr. Mohd Shukor Hj Mahfar, CEO of IRBM, and YBhg Dato' Sri Khazali Hj Ahmad, Director-General of RMCD, are responsible for tax collection and tax policy implementation.

Thanneermalai began with the MoU signed by IRBM and RMCD to carry out joint audits. Tan Sri Dr. Mohd Shukor confirmed that the MoU was signed in June 2013 and joint audits had already started. Dato' Sri Khazali added that so far, four joint audits had been conducted. "A joint audit committee decides which company is to be audited," Dato' Sri Khazali said, "And when GST kicks in next year, there will be more joint efforts in this area." While both bodies are revenue collectors, RMCD concentrates on transaction-based matters; IRBM looks at income-based matters.

Touching on the exchange of information between IRBM and RMCD under the MoU, Thanneermalai asked to what extent information can be shared without walking into the net of confidentiality provisions in the tax legislations. Tan Sri Dr. Mohd Shukor clarified that in addition to the confidentiality provision under Section 138 of the ITA, he was empowered under Section 81 of the ITA to call for information. He also clarified that, although the MoU provided a mechanism for sharing information between IRBM and RMCD, the information would not be passed to other persons. Dato' Sri Khazali added that IRBM and RMCD have to follow protocols to maintain confidentiality under Section 138 of the ITA. Thanneermalai summed up the discussion with an observation that the sharing of information between IRBM and RMCD was for the benefit of the nation.

Noting that the requirements of the income tax agent licence and GST agent licence would result in an increase in training expenditure and CPD hours, Thanneermalai asked whether there is any possibility of merging the licences into a single licence. "Having the two licences adds to cost. As time goes by, there is a possibility to look at the point raised by the professional bodies on the question of why we should have two types of licences", said Dato' Sri Khazali. Thanneermalai also urged the IRBM and RMCD heads to think about reducing the number of CPD hours as it is burdensome in terms of the time involved and the cost attached. The IRBM and RMCD heads agreed that there are possibilities for different permutations of CPD hours to be considered.

Referring to recent media reports, Thanneermalai asked about self financing within IRBM and underlying facts in setting up the IRBM investment panel. Tan Sri Dr. Mohd Shukor said that contrary to the media reports, the investment panel does not invest the collections from taxpayers. Instead, the investment panel will invest the surplus agency fees IRBM receives from the government for collecting tax revenue. This would enable IRBM to be self financing and independent in its operational and human resource matters. Thanneermalai observed that this was similar to the practice of revenue collecting agencies in a neighbouring country.

There had been unconfirmed indications that the RMCD would exercise leniency in imposing GST penalties in the first two years. Dato' Sri Khazali responded to Thanneermalai's query on this matter, "We want to be firm but fair in exercising our powers. We want to create confidence. Initially, of course, we expect teething problems. Some people are making it look as if GST will make things more expensive, but theoretically, prices should go down. We will provide a lot of advice." He also urged for the GST registration of businesses to be done early and not wait until 31 December 2014. Late registration would be penalised.

Responding to Thanneermalai's query on how income tax revenue collection will keep going in light of GST, Tan Sri Dr. Mohd Shukor indicated that it was anticipated to increase. Since 2002, collection was on the uptrend although tax rates had been reduced and new tax incentives had been introduced. He also explained that the marginal reduction of tax rates would increase the tax base for income tax revenue collection and the introduction of GST would bring about better income tax compliance in the future.

Thanneermalai closed the final session of the NTC 2014 by saying, "I'm really pleased this NTC has brought the IRBM and RMCD heads together and we will remember this as a historical event that is the beginning of better things to come."

***(Note: The NTC 2015 will be held on 25 and 26 August 2015.)***

# Direct Taxes and Indirect Taxes

## A COMPARISON BETWEEN ENTITIES IN MALAYSIA AND LABUAN

Goh Ka Im

Much has been written about the beneficial tax treatment currently enjoyed by Labuan entities in the Labuan International Business and Financial Centre (Labuan IBFC), particularly under the Labuan Business Activity Tax Act 1990 (LBATA). Such beneficial tax treatment is in relation to the direct tax on profits imposed on Labuan entities. However, there are other beneficial tax treatments relating to indirect taxes that are also made available to Labuan entities, which will be highlighted in this article together with a comparison of the different tax treatments for Labuan entities and Malaysian entities.

### LABUAN BUSINESS ACTIVITY TAX ACT 1990 (LBATA)

Under the LBATA, a Labuan entity carrying on a Labuan trading activity is charged tax at a rate of 3% on the net audited profits reflected in the audited accounts of the Labuan entity for each year of assessment. However, a Labuan entity carrying on a Labuan trading activity has the option of electing to be charged tax at a fixed rate of RM20,000 (approximately USD6,000) for each year of assessment. Once this option has been exercised, a Labuan entity would not be subject to the 3% tax charge.

In the case of a Labuan entity carrying on a Labuan non-trading activity (which would basically include all investment activities), there is no charge to tax.

### INCOME TAX ACT 1967 (ITA)

Other Malaysian non-Labuan entities deriving income from Malaysia are subject to tax under the ITA where the usual rate of tax applicable to companies is currently 25%. However, it has been proposed that the rate be reduced to 24% from the year of assessment 2016.

For Labuan entities that prefer to enjoy benefits under a Malaysian double tax treaty rather than the tax benefits under the LBATA, they may opt to make an irrevocable election for their profits to be taxed under the ITA instead of the LBATA. With such an election, all of the Labuan entity's profits, whether arising from a Labuan trading activity or a Labuan non-trading activity, would be subject to tax at the usual rate of 25% under the ITA.

### EXEMPTION ORDERS UNDER THE ITA

Ordinarily, payments of interest, royalties, technical fees and other gains or profits not coming within the specified classes of income, which are derived from Malaysia and paid to non-residents, would be subject to withholding tax in Malaysia.

However, Labuan entities are exempted from withholding tax on those specified payments made to non-residents.

Under the Income Tax (Exemption) (No. 22) Order 2007 (2007 Exemption Order), due to the terminology used which refers to "offshore company" instead of "Labuan entity", Labuan companies and Labuan trusts are amongst the types of entities specified as being exempted from withholding tax on interest, royalties and technical fees paid to non-residents. This exemption, however, does not apply to Labuan foundations.

As such, a new exemption order known as the Income Tax (Exemption) (No. 4) Order 2012, which was gazetted in 2012, used the term "Labuan entity" in relation to exemption from withholding tax on other gains or profits not coming within the specified classes of income so that where those payments are concerned, the exemption from withholding tax is made available to all Labuan entities as defined, including Labuan foundations, Labuan companies and Labuan trusts. The anomaly affecting the 2007 Exemption Order is known to the Labuan authorities and should hopefully be resolved soon.

## DOUBLE TAX TREATIES

Some countries that have entered into double tax treaties with Malaysia have specifically excluded Labuan entities from enjoying the benefits provided under their double tax treaties.

One of the latest examples is the double tax treaty between Malaysia and India known as the Double Taxation Relief (The Government of the Republic of India) Order 2012 (India Order). The Protocol to the India Order specifies that persons who are entitled to tax benefits under the LBATA are not entitled to benefits under the India Order but an exception is made for Labuan companies which have made an irrevocable election to be charged tax in accordance with the ITA.


In contrast, other countries which have excluded Labuan entities from enjoying the benefits under their double tax treaties do not make any exceptions for Labuan entities which elect to be taxed under the ITA instead of the LBATA.

One such example is the double tax treaty between Malaysia and South Africa known as the Double Taxation Relief (The Government of the Republic of South Africa) Order 2005 (South Africa Order), which specifies that the benefits of the South Africa Order shall not be made available in relation to the carrying on of any offshore business activities (as defined in the LBATA as at 26 July 2005).

As no exception was provided in the South Africa Order, Labuan entities wishing to enjoy benefits under the South Africa Order or other similar double tax treaties without provisions for an exception, should be aware that electing to be taxed under the ITA instead of the LBATA may not necessarily enable them to enjoy treaty benefits.

## INHERITANCE TAX AND GIFT TAX

There is no inheritance tax or estate duty in Malaysia, including Labuan, so any estate planning does not have to take into account such taxes.

There is also no gift tax per se in Malaysia, including Labuan, but if the gift involves real property or shares in a real property company, the Real Property Gains Tax Act 1976 may need to be considered.

## STAMP DUTY

Stamp duty is imposed on certain types of instruments in Malaysia as specified in the Stamp Act 1949. Common instruments which are subject to stamp duty would be conveyances or transfers on sale of property such as shares and real estate. For such instruments, the rate of stamp duty is imposed on the value of the property in question so the total stamp duty payable could be quite substantial depending on the value of the property.

For Labuan entities, an exemption order known as the Stamp Duty (Exemption) (No. 3) Order 2012 (Stamp Order) is in force which exempts all instruments executed by a Labuan entity in connection with a Labuan business activity from stamp duty.

In addition, under the Stamp Order, all instruments of transfer of shares in a Labuan entity, as well as the constituent documents for the establishment of a Labuan entity, are exempted from stamp duty.

## CUSTOMS DUTIES

Customs duties, the most common of which are import duty and export duty, are imposed on certain goods imported into or exported from Malaysia.

However, once again there is special treatment in relation to Labuan; as stated in the Customs Act 1967, the "principal customs area" in Malaysia is defined to exclude Labuan so that no export duty is payable on any goods exported from Labuan and generally no import duty is payable on goods imported into Labuan.

## SALES TAX

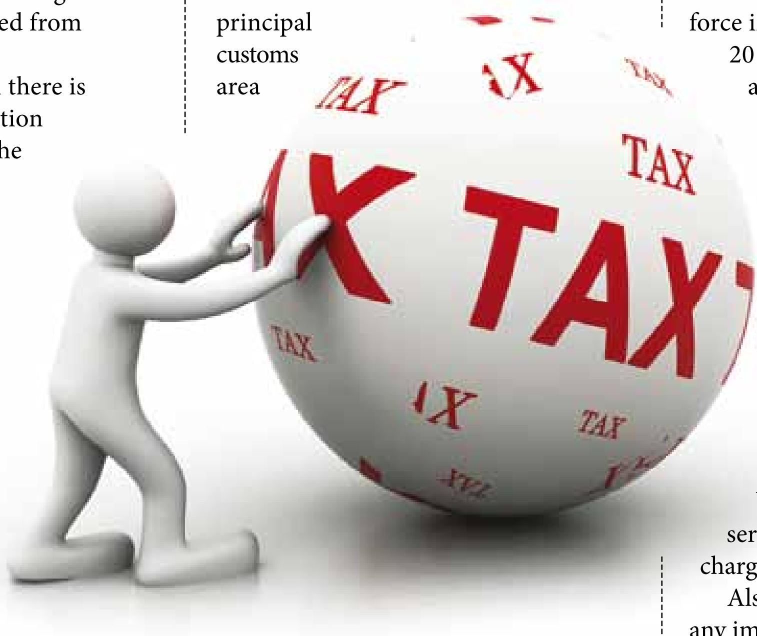
Sales tax is imposed on specified goods which are manufactured in Malaysia or imported into Malaysia for home consumption but Labuan enjoys special treatment as it is excluded from the definition of "principal customs area" for purposes of the Sales Tax Act 1972.

Generally, no sales tax would be payable on any taxable goods imported or transported to Labuan from the principal customs area of Malaysia.

## SERVICE TAX

Service tax is imposed on prescribed taxable services provided by prescribed taxable persons in Malaysia. Common examples of taxable services include legal services and accounting services, while common examples of taxable persons include advocates and solicitors as well as public accountants.

The Service Tax Act 1975 is specified as not applying to Labuan. Additionally, the Minister of Finance had exercised his powers to exempt all taxable services provided by persons in the principal customs area




in relation to matters in Labuan from service tax. The Minister further specified that all taxable services provided by persons in the principal customs area to persons in Labuan are not subject to service tax.

The exemption from, and non-application of, service tax in relation to Labuan as described above would remain until the introduction of the goods and services tax (GST).

## GOODS AND SERVICES TAX (GST)

It was announced in the Malaysian Budget 2014 that the goods and services tax (GST) will come into force in Malaysia effective 1 April 2015. To facilitate this, the Goods and Services Tax Bill 2014 (GST Bill) was passed by the Malaysian Parliament in April 2014.

Pursuant to the GST Bill, GST would be levied on any supply of goods or services made in Malaysia, including any importation of goods into Malaysia. With the introduction of GST, the Sales Tax Act 1972 as well as the Service Tax Act 1975 would be repealed so that sales tax and service tax would no longer be chargeable.

Also, GST shall not apply to any importation of goods or supply of imported services into Labuan unless specifically prescribed by the Minister of Finance by an order laid before Parliament. However, GST is chargeable on all goods supplied from Labuan to Malaysia or taxable services made by a taxable person in Labuan to Malaysia.

## CONCLUSION

There is a comprehensive range of tax benefits both in relation to direct taxes and indirect taxes available to Labuan entities, which makes Labuan IBFC a very attractive jurisdiction for a variety of business and financial activities. Strategically located in the heart of Asia Pacific, Labuan IBFC is well positioned to tap into one of the fastest growing regions in the world, presenting the perfect opportunity for businesses seeking to connect with Asia's economies and beyond.

***Goh Ka Im**, Partner and Head of Tax and Revenue Practice Group, Messrs Shearn Delamore & Co.*

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# MERGERS & ACQUISITIONS

Nicholas Anthony Crist

The purpose of this article is to outline the key Malaysian direct tax issues relevant to mergers and acquisitions (M&As). Particular reference is made to M&As that involve Malaysian real property, whether in the form of land rich companies or direct interests in Malaysian realty.

The expression "M&A" is often used in a non-technical sense to refer to a disposal by one party and a simultaneous acquisition by another. While US company law and many civil law codes provide for the concept of a merged entity, this is not the case under the Malaysian Companies Act 1965. Instead, in the Malaysian context, M&As at their core typically involve either (1) a sale of shares or (2) a sale of business assets. There may be subsequent post acquisition restructurings to avoid a duplicity of entities and to achieve business synergies.

## INCOME TAX

Where the M&A involves a disposal of shares, it would be appropriate to review the tax treatment of any gain which might arise. While regard must always be had to the facts, generally gains on the disposal of shares in a company that has been held as a long term investment would be capital in nature. While capital gains may not be subject to income tax, it is appropriate to consider Real Property Gains Tax (RPGT) being the secondary tax.

A similar principle applies to the disposal of a business if the assets include buildings such as an office or a factory. Where the real property represents the premises from which the business is conducted, any gain on disposal is likely to be capital in nature, such that RPGT rather than income tax is applicable.

Where the building being disposed of has qualified for industrial building allowances or capital allowances, it would be necessary for the vendor to determine the extent of any balancing allowance or charge.

## RPGT

A sale is clearly contemplated by the definition of "disposal" in Section 2 of the Real Property Gains Tax Act, 1976 (RPGTA). Where pursuant to an M&A, shares are disposed of, it is important to determine whether the company disposed of is a Real Property Company (RPC). The RPGTA defines an RPC as:

- a controlled company which, as at 21 October 1988, owns real property or shares or both, the defined value of which is not less than 75% of the value of its total tangible assets; or
- a controlled company to which subparagraph (a) is not applicable, but which, at any date after 21 October 1988, acquires real property or shares or both whereby the defined value of real property or shares or both owned at that date is not less than 75% of the value of its total tangible assets;
  provided that where

at any date the company disposes of real property or shares or both whereby the defined value of real property or shares or both owned at that date and thereafter is less than 75% of the value of its total tangible assets, that company shall not be regarded as a real property company as from that date.

It is therefore necessary to determine whether 75% or more of a company's total tangible assets comprise:

- interests in Malaysian real property;
- shares in another RPC; or
- a combination of (1) and (2) above.

Collectively the above are termed "chargeable assets". The 75% ratio must be tested at the date of acquisition (as defined) of any chargeable asset. At such time, it would be necessary to determine the market value of the other chargeable assets held by the company in order to apply the 75% ratio.

As is apparent, the RPGTA, like many other capital tax acts, derives its force from a number of technical definitions. In this respect, it must not be forgotten that the "date of acquisition" for RPGT purposes is deemed by the RPGTA to coincide with the date of disposal (Paragraph 15(2), Schedule 2 RPGTA).

A disposal shall be deemed to take place on;

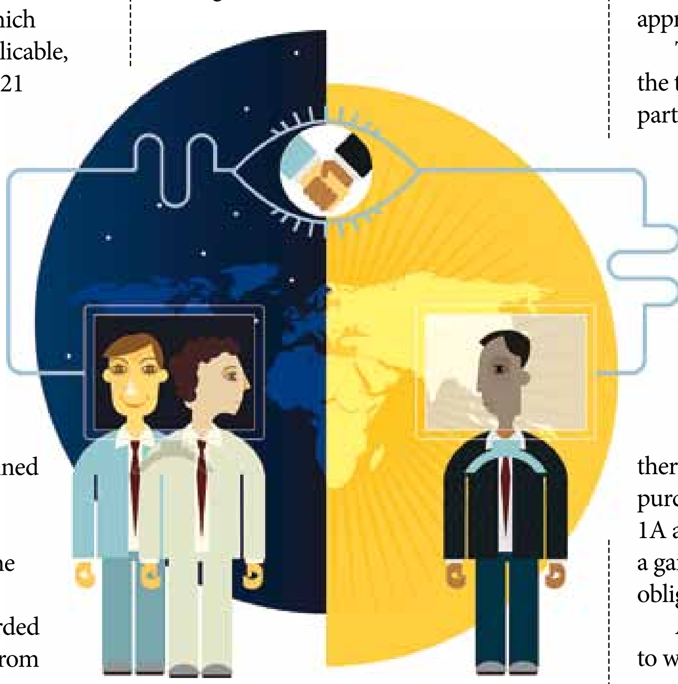
- the date of the written agreement; or
- where there is no written agreement, on the date of completion of the disposal.

Where a contract for the disposal of an asset is conditional and the condition is satisfied by the exercise of a right under an option or otherwise, "the acquisition and disposal of the asset shall be regarded as taking place at the time the contract was made, unless the acquisition or disposal requires the approval by the government or a state government or an authority or committee appointed by the government or a state government, the date of disposal shall be the date of such approval."

The above has the effect of advancing the time of acquisition. This is a particular concern where contracts for the acquisition of land contain conditions precedent other than government approvals. This can be a trap for the unwary, who may only address the issue of RPC status after having committed to buy Malaysian real property interests including shares in RPCs.

Where a target company is an RPC there is an obligation on the vendor and purchaser to file RPGT returns, CKHT 1A and CKHT 2A respectively. Where a gain arises, the vendor would have tax obligations as in **Table A**.

A purchaser of an RPC is required to withhold the lesser of the monetary component of the consideration or 2% of the total value of the consideration. The tax withheld must be remitted to the Malaysian Inland Revenue Board (MIRB) within 60 days.



| HOLDING PERIOD OF CHARGEABLE ASSET | RPGT RATES | | |
|---|---|---|---|
| | COMPANIES | INDIVIDUAL A | INDIVIDUAL B |
| Within 3 years from date of acquisition | 30% | 30% | 30% |
| In the 4th year | 20% | 20% | 30% |
| In the 5th year | 15% | 15% | 30% |
| In the 6th and subsequent years | 5% | 0% | 5% |

*A: Malaysian citizens and permanent residents* *B: Non-Malaysian citizens*

**Table A**

Determination of RPC status can require a detailed analysis of historical records which may not be available to a purchaser. This problem is exacerbated where the ownership structure involves foreign holding companies, as incorporation outside Malaysia does not protect a company from being an RPC (Section 2(1) RPGTA). It is therefore common practice to seek a warranty from the vendor to confirm the RPC status of the target company; this should be reinforced by a suitable indemnity.

Where interests in Malaysian real property are acquired, the RPGT position may be more clear cut than on an acquisition of shares. However, the MIRB has on many an occasion litigated over whether income tax rather than RPGT should apply. Where RPGT is applicable, the comments above relating to filing and withholding tax obligations generally remain applicable.

In addition to the above, it is important to determine whether the acquisition of real property assets would cause the acquiring company to become an RPC.


## STAMP DUTY

Stamp duty is payable by the party acquiring shares at 0.3% ad valorem. This is significantly lower than stamp duty on the acquisition of Malaysian real property where the following rates apply **(Table B)**.

Unlike some countries, Malaysia does not levy a higher rate of stamp duty on the transfer of shares in land rich companies.

Where the M&A is a "reconstruction" or an "amalgamation", relief from stamp duty may be available under Section 15 of the Stamp Act 1949. For this relief to be available, in addition to the definition requirement, a number of other conditions must be met including that at least 90% of the consideration be in shares. A pro-forma statutory declaration is also required.

| ASSET VALUE | RATE % |
|---|---|
| RM1 – RM100,000 | 1 |
| RM100,001 – RM500,000 | 2 |
| > RM500,000 | 3 |

**Table B**

## FINANCING

The consideration for an M&A transaction may be by way of paper (e.g. share for share exchange or loan notes) or cash or a combination of the two. Where cash is involved, this can come from either the acquirer's internally generated funds, a rights issue, or through borrowings (either domestic or offshore). In the case of borrowed funds, the opportunities to claim tax relief for the interest expense and withholding tax implications (for offshore borrowings) need to be considered.

By now, all Malaysian companies are on the single tier dividend system. Paragraph 12B, Schedule 6 of the Income Tax Act 1967 (ITA), provides an exemption from tax for such dividends and also that "… any expenses incurred in relation to such dividends shall be disregarded…". Consequently, where borrowings are used to acquire shares, a tax deduction for the interest expense is not claimable.

In contrast, where borrowings are used to acquire business assets, Section 33(1)(a) ITA provides a deduction for:

"Interest upon any money borrowed… and

- employed in that period in the production of gross income from that source, or
- laid out on assets used or held in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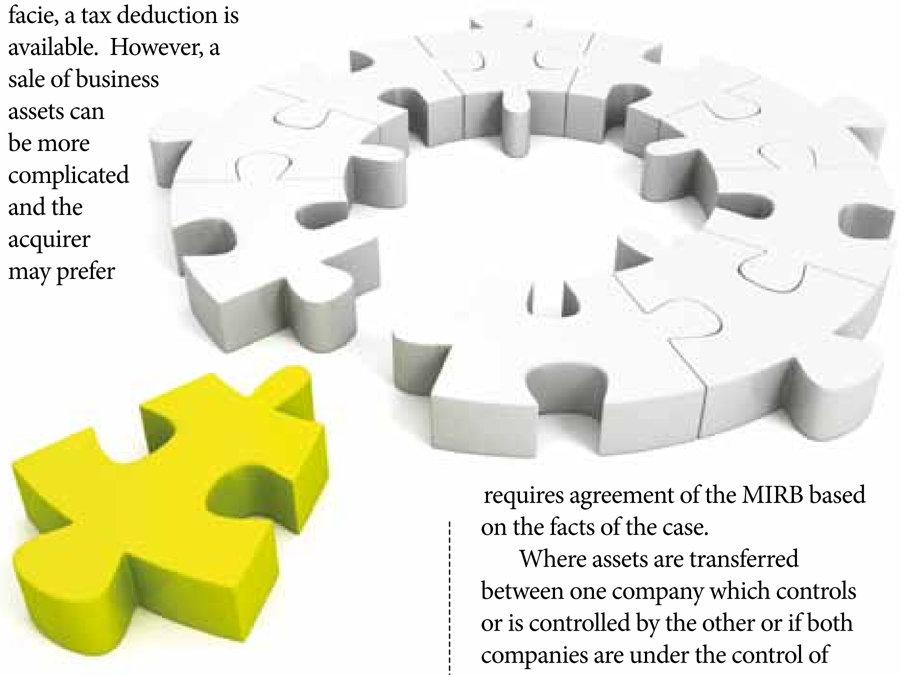
> that period for the production of gross income from that source."

There is therefore a sharp contrast between borrowings used to purchase shares where the interest expense is not deductible and borrowings used to purchase business assets where, prima facie, a tax deduction is available. However, a sale of business assets can be more complicated and the acquirer may prefer to purchase shares, particularly where the target company holds licenses or tax exemptions. This decision would need to be considered in tandem with the ability to claim a tax deduction on interest.



## RELATED PARTY TRANSACTIONS

Where M&A transactions are between related parties, it is appropriate to consider the various tax reliefs available.

From a RPGT perspective, Paragraph 17, Schedule 2 RPGTA deems qualifying disposals within groups to be on a no gain and no loss basis. There is the requirement that the chargeable asset is "transferred…to bring about greater efficiency in operation for a consideration consisting of shares or substantially of shares". This relief also requires the prior approval of the Director-General of the MIRB. The RPGTA recognises a consideration as being "substantially of shares" where 75% or more of the consideration is in shares. The RPGTA does not provide a mechanism to determine "greater efficiency in operation" which instead requires agreement of the MIRB based on the facts of the case.

Where assets are transferred between one company which controls or is controlled by the other or if both companies are under the control of a third party, the controlled transfer provisions apply (Paragraphs 38-48, Schedule 3 ITA). The controlled transfer provisions have the effect that an asset, on which capital allowances have been claimed, is deemed to be transferred at its tax written down value (TWDV) regardless of the actual transfer consideration. This means that the vendor is sheltered from balancing charges in the event of, for example, the sale of an "industrial building". However, as the application of the controlled transfer provisions is mandatory, a purchaser's claim to future capital allowances is restricted to the TWDV taken over.

In instances of related party M&As, the stamp duty cost may be relieved through Section 15A of the Stamp Act 1949. Section 15A is aimed at allowing qualifying transfers to occur within corporate groups where there is at least 90% common ownership, without any liability to stamp duty. Amongst other things, a pro-forma statutory declaration must be filed with the Stamp Office in support of an application for relief under Section 15A. This relief can be particularly important in the case of intragroup disposals of Malaysian real property given the relatively high stamp duty rates and escalating property values.

## CONCLUSION

Where Malaysian real property is a feature of an M&A transaction, the tax costs and obligations of both the vendor and purchaser must be determined as the uninformed run the risk of unanticipated tax exposures and the associated penalties. The need for comprehensive tax advice at an early stage is apparent.

Where the transaction is by way of an acquisition of assets, the tax costs to both the vendor and particularly the purchaser, are likely to be higher than in the case of an acquisition of shares. On the upside, the assets would generally be rebased, (for the purposes of the purchaser's industrial building allowance or capital allowance claims on qualifying assets) while in a share acquisition the tax base remains unchanged. Significantly, where gearing is involved a tax deduction should be available in an asset deal but generally not in a share acquisition. However, in view of regulatory and licensing requirements, an asset deal is not always practical.

The tax costs associated with an M&A transaction should be determined as part of the acquisition strategy and may ultimately flow through to the pricing of the transaction.

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# FIGHTING TAX EVASION THROUGH EXCHANGE OF INFORMATION

Esther A.P. Koisin

IT WOULD BE A PERFECT SCENARIO IF EVERYONE COMPLIES WITH THEIR TAX OBLIGATIONS. HOWEVER IN REALITY, ALTHOUGH MANY DO, THERE REMAIN MANY MORE WHO DO NOT FOR A VARIETY OF REASONS. TAX EVASION WHICH OFTEN ENTAILS THE DELIBERATE MISREPRESENTATION OF THE TRUE STATE OF A TAXPAYER'S TAX AFFAIRS EITHER THROUGH NON-REPORTING OR UNDERREPORTING OF INCOME, PROFITS OR GAINS, OVERSTATING OF DEDUCTIONS OR HIDING AWAY WEALTH OFFSHORE IS A PERENNIAL ISSUE INVOLVING HUGE AMOUNT OF TAX LOSS. IN RECENT YEARS MANY COUNTRIES ESTIMATED THAT THEIR TAX LOSS DUE TO TAX EVASION AMOUNTS TO BILLIONS OF DOLLARS YEARLY.

Tax evasion scandals such as the LGT case and the UBS case in 2008 have placed the fight against tax evasion high on the political agenda of the G20. Following that, G20 has urged the Organisation for Economic Co-operation and Development (OECD) to strengthen its work on tax evasion and the implementation of the internationally agreed tax standard for transparency and exchange of information.

Against this background, tax administrators and policymakers around the globe are working closer together with OECD to fight tax evasion and protect their revenue base which is fundamental in ensuring public confidence in the fairness and equity of the tax systems.

## THE INTERNATIONALLY AGREED TAX STANDARD FOR TRANSPARENCY AND EXCHANGE OF INFORMATION (IATS)

In 2009, Malaysia committed to the IATS. The standards provide for international exchange on request of foreseeably relevant information for the administration or enforcement of the domestic tax laws of a requesting jurisdiction. Fishing expeditions are not authorised but all foreseeably relevant information must be provided, including bank information and information held by fiduciaries, regardless of the existence of a domestic tax interest or the application of a dual criminality standard.

The commitment to IATS necessitates Malaysia to actively seek to update and extend its network of double taxation agreements. Malaysia has since signed 22 Double Tax Agreements (DTAs)/protocols to existing DTAs and one TIEA, all of which fully conform to the standard, 17 of which are in force and six are not in force but have already been ratified. A further 24 agreements are under various stages of negotiation. Malaysia has also reviewed its domestic policies that restricted access to bank information in order to ensure that it is able to exchange information to the standard in respect of all of its EOI agreements. However, effective 1 July 2013 Malaysia has made a policy change enabling the rest of its 52 more treaties to meet the IATS.

Under the IATS, tax jurisdictions are not only required to ensure that ownership and identity information for all relevant entities and arrangements is available but that reliable accounting records must be kept by those entities and arrangements. These records should be kept for a minimum period of five years. Penalties and sanctions under the law must be imposed on non-compliant entities and arrangements. Further, tax jurisdictions are also required to ensure that detailed banking information should be available for all account holders.

The IATS naturally demands that the legal framework of a tax jurisdiction should provide power for the Competent Authority to obtain and provide information that is the subject of a request under an EOI arrangement from any person within their territorial jurisdiction who is in possession or control of such information. This power must be exercised efficiently to ensure that information is provided in a timely manner so that that information received remains relevant in the investigation process of its EOI partners.

## MONITORING PROCESS

To ensure that jurisdictions who have committed to the IATS and also those jurisdictions OECD has identified as relevant to its work maintain high standard of compliance to the IATS, a monitoring process has been put in place. The monitoring process is done through peer review in two phases. Phase 1 reviews the quality of a jurisdiction's legal and regulatory framework for the exchange of information, while Phase 2 reviews look at the practical implementation of that framework. The ultimate goal of these reviews is to help jurisdictions to effectively implement the IATS for EOI.

Malaysia has undergone the Phase 1 review in 2011 and Phase 2 in 2013.

The Phase 1 Review acknowledged that Malaysia's Competent Authority has broad powers to obtain relevant information from any person who holds the information and has measures to compel the production of such information. In particular, since 10 February 2012, with the amendment to Section 81 of the Income Tax Act 1967, the Malaysian Competent Authority is empowered to collect information that is under the control of a person within its territorial jurisdiction, even if the information is held outside Malaysia. The review also acknowledged that Malaysia's legal framework is in place to ensure the availability of information.

Under the Phase 2 review, it was reported that some of the penalties provided in Malaysian law are relatively low. This seemed to have impacted the exchange of information in some cases. It is therefore recommended that Malaysia reviews the adequacy of its penalty regime to ensure that they are effective in providing deterrence against non-compliance.

The report also observed that during the period under review (2010-2013), Malaysia has not been able to reply to all EOI requests in a timely manner. One of the reasons for this inability was that a dedicated EOI team was not established earlier. This issue has since been addressed with the establishment of the EOI unit in July 2013 at Headquarters level of the Inland Revenue Board of Malaysia and the appointment of EOI officers at branch level throughout the country. This dedicated team has made it possible for IRBM to obtain the requested information by our EOI partners in a timely manner. More importantly with this development, IRBM is set to benefit much more from EOI. Steps have been taken by IRBM to sensitize its auditors and investigators about EOI and to avail themselves to this mechanism to get relevant information that will be helpful in their audit or investigation work. These will include information that is necessary to verify certain transactions claimed by taxpayers or any information including bank information that is foreseeably relevant in concluding the audit and investigation work. The requesting for information between treaty partners has now become part of the standard working process in audit and investigation of many tax administrations and Malaysia is no exception.

It is important to note that in terms of rights and safeguards of taxpayers and third parties, the review has found that this is respected by the Malaysian EOI mechanism.

## NEW STANDARD OF EXCHANGE OF INFORMATION

Records show that the information provided by EOI partners has been useful and contributed to the recovery of significant amount of tax unpaid in the relevant cases being investigated or audited by requesting jurisdictions.

The positive results of EOI on request and the intergovernmental implementation of the US Foreign Account Tax Compliance Act (FATCA) have encouraged political leaders to call for a single standard of automatic exchange of information (AEOI).

On 13 February 2014 the OECD unveiled the new global standard for AEOI. The new standard obliges countries and jurisdictions to obtain all financial information from their financial institutions and exchange that information automatically with other jurisdictions on an annual basis.

On 6 May 2014, Malaysia joined 34 OECD member countries along with Argentina, Brazil, China, Colombia, Costa Rica, India, Indonesia, Latvia, Lithuania, Saudi Arabia, Singapore and South Africa in supporting the declaration to commit to the implementation of the new single global standard on automatic exchange of information.

As at June 2014, 45 countries and jurisdictions have committed to the early adoption of the standard. Early adopters are expected to exchange bank information automatically in 2017 in respect of bank information for 2016. Malaysia has not made a decision yet to join the early adopters. However, like other countries that have supported the declaration to commit to the implementation of AEOI, Malaysia would be expected to implement AEOI swiftly.

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## CONCLUSION

Tax is a legal obligation, not a moral choice. Tax evasion is both legally and morally wrong. The tax administration and the tax paying community have an obligation to honour this and until we can achieve total voluntary compliance, mechanisms such as the international exchange of information will remain relevant in the tax ecosystem.

# WITHHOLDING TAX ON SPECIAL CLASSES OF INCOME

## A REVIEW OF THE PUBLIC RULING NO. 1 OF 2014

Dr. Nakha Ratnam Somasundaram

THIS 37-PAGE RULING IS A REVAMPED RULING, REPLACING OR COMBINING THE CONTENTS OF EARLIER RULINGS[1]. THE FOCUS IS ON THE INTERPRETATION OF SECTION 4A[2], ITS DERIVATION, AND ASPECTS RELATING TO SERVICES RENDERED, RENTS, REIMBURSEMENT, DISBURSEMENT, DEPOSITS AND ADVANCE PAYMENTS MADE AS WELL AS TAX RATES, REMITTANCES, DEDUCTION OF TAX AND PENAL PROVISIONS. SOME OF THESE MATTERS ARE REVIEWED IN THE FOLLOWING PARAGRAPHS.

*This article looks at some salient features of the Inland Revenue Board's recently issued Public Ruling No. 1 of 2014 on withholding tax on special classes of income under Section 4A ('the ruling')*[3].

### SECTION 4A(i)

This section deals with amounts paid in consideration of services performed in Malaysia and rendered by a non-resident person or his employees in connection with the use of property or rights belonging to the non-resident person or the installation or operation of any plant, machinery or other apparatus purchased from the non-resident.

It is apparent that in acquiring a plant or machinery from a non-resident and installing them, a distinction in the payment must be made as the cost of the plant and machinery itself does not suffer any withholding tax – it being a purchase of an asset – but the installation and commissioning aspects of the deal would be subject to withholding tax and evidence must be available to show this as a separate category of payment.

Where the services are performed through a project and a permanent establishment exists, or alternatively a business presence exists in Malaysia, the applicable withholding tax provisions are in Section 107A and not 109B.

### SECTION 4A(ii)

This covers payments for technical advice, assistance or services rendered in connection with the technical management or administration, and are covered rather comprehensively.

A major issue encountered in Section 4A(ii) is whether services rendered are technical, or non-technical in nature. The ruling stresses that it is only technical services or services related to specialised services that fall within the scope of Section 4A(ii) and accordingly would suffer withholding tax.

But it may be unclear when Para 8.2 of the ruling speaks of the scope of payment under Para 4A(ii) as covering payments for technical assistance, *non-technical* assistance, technical services or *non-technical services* rendered in connection with scientific, industrial or commercial undertakings, ventures, projects or schemes[4].

Technical advice and assistance for example is explained as those services connected with technical management of any scientific, industrial or commercial undertaking and as including the passing over or utilisation of expert or specialised knowledge, skill or expertise. This will include marketing, legal and supply of technical personnel and inter-company technical services.


Administration, i.e. the non-technical part of the services is explained as covering management and administration functions like planning, direction, control, accounting and financial consultation including labour negotiation.

The distinction between technical and non-technical aspects in the allocation of head office expenses by a non-resident company to its Malaysian branch or subsidiary for example, is couched in vague terms in the ruling. The only clear indicator is that services provided which 'is in no way related to the performance of any specialised services' would be non-technical, and may not fall within the scope of Section 4A(ii).

Non-technical and administration services are those that relate to ordinary day to day or routine expenses like clerical and book-keeping functions. An example is given of an overseas company providing some bookkeeping services for its Malaysian branch office as being non-technical in nature. Another nine examples are given to illustrate the distinction between technical and non-technical services and covers marketing and management services, consultancy services and reimbursements.

This distinction between technical and non-technical payments can be disconcerting at times. It must be handled with care because Section 4A(ii), while talking about 'payments for technical advice, assistance or services rendered', it apparently does not provide for a splitting of the expenses between technical and non-technical parts. The issue of the distinction between technical and non-technical and the temptation to split the expenditure as between technical and non-technical is legally fraught with danger as was illustrated in the case of *AIACL v KPHDN*[5].

This can cause problems for the deduction of withholding tax from payments made to non-residents, and becomes particularly serious in view of the heavy penalties prescribed under Sections 109B and 109H as well as the disallowance of the payments in arriving at the adjusted income of the taxpayer.

One can take some guidance from *AIACL v KPHDN* where the Special Commissioners found that Section 4A, and Section 109B which mirror Section 4A, do not provide for the splitting up of invoices into technical and non-technical portions.

This decision is important in view of the explanation in the ruling where apparently Section 4A(ii) covers both technical and non-technical assistance or services.

In *TS Sdn Bhd v KPHDN*[6], the Special Commissioners also confirmed their view that Section 4A(ii) covers both technical and non-technical services. The Special Commissioner's decision was based on an earlier decision in the case of *EPM Inc. v KPHDN*[7].

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[1] *The earlier rulings were Public Ruling No. 4 of 2005 (issued on 12 September 2005), Addendums to Public Ruling No. 4 of 2005 (issued on 30 November 2011) and the second addendum to the said ruling (issued on 4 January 2010).*

[2] *All sections quoted in this article refer to the Income Tax Act 1967 (as amended) unless otherwise specified.*

[3] *The Inland Revenue Board's Public Ruling No. 1 of 2014 was issued on 23 January 2014. A Public Ruling is issued under Section 138A of the Income Tax Act 1967 (as amended) and provides guidance for the public and the officers of the Inland Revenue Board, setting out the interpretation of the Director-General of Inland Revenue on aspects of the law, policy and procedures applicable.*

[4] *The emphasis in italics is that of the writer's.*

[5] *(2002) MSTC 3438*

[6] *[2008) MSTC 3707]*

[7] *Supra*

In contrast, Indian case laws have emphasised that payments to non-residents must incorporate an element of technical services involving some human intervention before it could be subject to withholding tax[8].

Thus given this legal precedents, one could take comfort in the ruling's explanation of the distinction being made between technical and non-technical services – but nonetheless it appears to be a dicey one for practical applications unless one could clearly ascertain that the particular charges are 'in no way related to the performance of any specialised services'. This may leave much room for dispute.

Further, in situations where the services under a contract are performed both within Malaysia and outside Malaysia, only that portion of the contract value attributable to the services performed in Malaysia is liable to income tax. The apportionment must be ascertained in a manner that is fair and 'justifiable' (the ITA usually uses the word 'reasonable'). According to examples in the ruling, an apportionment on a time basis or cost basis would be acceptable to the Inland Revenue Board - which means such apportionment does not require separate invoices and separate bills[9].

## PHOTOSHOOT AND TECHNICAL MANAGEMENT

If a non-resident individual person poses as a model for a one day photo-shoot in Malaysia, will that be services rendered in connection with technical management or administration or otherwise?

For the IRB '...it is considered a special class of income for a commercial undertaking as there is no element of entertainment during her photoshoot.' The Example 12 in the Ruling concludes with a note to say that generally, there is no element of entertainment in photoshoots –tax practitioners will not have any problem with that - but they are also of the view that for a deduction under Section 109B, all the three conditions for a deduction must exist – namely,

- the amount was paid in consideration of technical advice, assistance or services;
- it was rendered in connection with technical management or administration, and
- that it was in respect of any scientific, industrial or commercial undertaking, venture, project or scheme.

In this context, photoshoots may turn out very blur.


## SECTION 4A (iii)

This section refers to payments relating to rent and other payment for the use of movable property such as oil rigs, boats, ships, cars and aircrafts whether within Malaysia or outside Malaysia.

The ruling explains clearly the various types of hire charges and the treatment to be accorded for purposes of Section 4A (iii).

Owing to the stiff competition in the shipping industry[10], certain payments by a resident person to a non-resident are specifically exempted from withholding tax under certain exemption orders. This includes pooling arrangements, income received from a Malaysian shipping company[11] and income derived from the rental of ISO containers by a Malaysian shipping company.

## REIMBURSEMENTS

Reimbursements are described as 'out of pocket' expenses incurred by the payee or service provider in the course of rendering service to the taxpayer or in respect of the use of movable property which are then subsequently reimbursed by the taxpayer. Typical reimbursements would include airfare, travelling expenses, accommodation, telephone and office charges like photocopying and printing.

With effect from 1 January 2009, reimbursement excludes expenses on hotel accommodation and withholding tax need not be deducted[12].

## DISBURSEMENT

Disbursement has to be distinguished from reimbursement.

Disbursement is out of pocket expenses incurred by the taxpayer and paid to a third party on behalf of the employee in connection with services rendered by the payee or service provider, or for the use of any movable property. For example, a payment of an airfare incurred by the payee and claimed from the taxpayer would be a reimbursement. However, if the payment is made by the taxpayer directly to the airline on behalf of the employee, then it becomes a disbursement.

As disbursements are considered to be part of the Section 4A income, it has significant income tax implication (and could be tricky too!). Example 15 in the ruling explains the situation quite satisfactorily.

In practice, it would appear that one should stick to reimbursement rather than disbursement because of the added administrative work, possibility of non-compliance, and the inevitable penalties for non-compliance.

## DEPOSIT AND ADVANCE PAYMENTS

In situations where non-refundable deposit and advance payments are made to the payee for services rendered or in respect of movable properties, these payment would fall within the meaning of Section 4A and would be subject to withholding tax.

## PAYMENTS NOT SUBJECT TO WITHHOLDING TAX

There is a long list of payments to non-resident persons which are outside the scope of Section 4A income, and not subject to withholding tax. These include commissions paid to a non-resident general commission agent, guarantee fee connected with any loan or indebtedness and letters of credit as well as deposits paid on the signing of an agreement for technical services which are refundable upon completion of the service.

Income of a non-resident individual who is an expert in Islamic finance and non-residents providing training approved by the Minister is also exempted.

## TAX RATES AND PAYMENTS

The chargeable income falling under Section 4A received by a non-resident and which are derived from Malaysia would be taxed at 10% on the gross amount. Where Malaysia has signed a Double Tax Agreement with a relevant country and a preferential rate is specified in the said agreement, then that preferential rate would apply. To be eligibile for the preferential rate the IRB would require a letter or Certificate of Residence from the treaty partner's jurisdiction.

The taxpayer is responsible for deducting and remitting the withholding tax to the Director-General of Inland Revenue (DGIR) under Section 109B within one month, and pay the non-resident recipient the net amount. Remittance must be accompanied by a form CP37 (available on the IRB's website) that details some administrative requirement.

## WITHHOLDING TAX BORNE BY THE TAXPAYER

The ruling makes a point of mentioning situations where the taxpayer, owing to trade competitions, might willingly bear the withholding tax and in such instances, the amount paid is treated as net, and needs to be re-grossed to determine the amount of income on which the tax should be charged[13].

***Example***

Malaysia Technologies Sdn Bhd (MTSB) received technical advice from an Indian firm on the design of a chip. The agreed payment was RM600,000. The full amount will be paid to the Indian firm and MTSB would absorb the withholding tax.

In the profit and loss account for the year ended 31 December 2013, MTSB claimed the following charges ***(see Table 1)***.

| PARTICULARS | RM |
|---|---|
| Technical fees | 600,000 |
| Add: Withholding tax paid to the DGIR (at 10%) | 60,000 |
| Total charges | 660,000 |

***Table 1***

The taxes were paid within one month to the DGIR.

For income tax purposes, the amount that can be allowed in determing the adjusted income of MTSB is only RM600,000 and not RM660,000.

## TAX CONSEQUENCES OF NON-DEDUCTION AND NON-REMITTANCE

Where withholding tax should have been deducted and remitted to the DGIR but was not done, there are some serious consequences for the taxpayer.

***(a) Increase of 10% on the tax not withheld or not remitted in time***

If the withholding tax is not withheld and remitted to the DGIR under Section 109B within the specified time, the amount that was not paid would be increased by a sum of 10% of the withholding tax and both the tax and the increased amount now remain a debt due to the government.

The increased amount is now a lower figure being based on the increase of

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[8] *See Hutchinson Telecom East Ltd v ACIT [(2007) 16 SOT 404] and Commissioners of Income Tax v Bharti Cellular Ltd. [(21) SOT 152]*

[9] *However, this may be an issue with scope of charge under Section 4A(ii) as illustrated by the case of AIACL v KPHDN [(2002) MSTC 3438] and other cases.*

[10] *See Dr. Nakha Ratnam Somasundaram, Ships and Water Snakes, Tax Guardian, Vol. 6/No. 2/2013/Q2*

[11] *The income from a Malaysian shipping company is exempted under the [Income Tax (Exemption) Order 2007] and includes income for the use of the ship on a voyage or time charter and bare boat charter. Accordingly, withholding tax does not apply to these incomes.*

[12] *'Hotel accommodation' includes accommodation in a hotel, apartment hotel, service apartment, motel, or hostel. This would include both reimbursement and disbursements. The ruling explains that this was done with a view to reducing the cost of services provided by non-residents.*

the tax that should have been withheld and remitted to the DGIR. Prior to 2 September 2006, the increase was imposed on the payment liable to deduction of tax ***(see Table 2)***.

***(b) Disallowance of the expenditure***

If a payment falling under Section 4A is made to a non-resident and the payer fails to deduct tax in accordance with Section 109B, then such payment made will be disallowed as an expense in computing the adjusted income of the taxpayer under Section 39(1)(j)[14].

However, a proviso to that section allows a deduction if the taxpayer subsequently pays the withholding tax together with any increase imposed thereon.

***(c) Penalty for incorrect returns under Section 113(2)***

A penalty may now be imposed if a taxpayer files a tax return within the due date for the relevant year of assessment but the withholding tax deduction was not made or was made after the due date for the submission of the tax return, and a deduction of the expenses on which withholding tax should have been made, was claimed in arriving at the adjusted income for the relevant year of assessment. The taxpayer's claim of an expense in the tax returns where withholding tax was not deducted renders the taxpayer's return 'incorrect" and is subject to this new penalty. This provision came to effect from 1 January 2011.

The penalty may also be imposed where the tax return has been filed late but the withholding tax has not been deducted or has not been paid at the relevant time.

The maximum penalty is 100% of the tax undercharged resulting from the claim.

If the withholding taxes are subsequently paid, including any increase, the assessment may be discharged but the incorrect return penalty remains (it being now charged on the revised chargeable income).

***Table 2***

| PARTICULARS | BEFORE 2 SEPTEMBER 2006 | FROM 2 SEPTEMBER 2006 |
|---|---|---|
| Payment made to a non-resident | 100,000 | 100,000 |
| Amount of withholding tax deductible (say 10%) | 10,000 | 10,000 |
| Net amount remitted | 90,000 | 90,000 |
| Assuming non-compliance, the increase would be | 10,000<br>(10% of RM100,000) | 1,000<br>(10% of RM10,000) |

***Example***

Assume an original chargeable income of RM30,000 where the taxpayer had wrongly claimed technical fees of RM400,000 on which withholding tax was not deducted.

| ORIGINAL ASSESSMENT (BEFORE TAX AUDIT) | RM |
|---|---|
| Chargeable income | 30,000 |
| Tax charged at 25% | 7,500 |

Assume that after a tax audit, the Inland Revenue Board disallowed the technical fee claimed by the company.

| ADDITIONAL ASSESSMENT (AFTER TAX AUDIT) | RM |
|---|---|
| Chargeable income | 30,000 |
| Add: Technical fees disallowed | 400,000 |
| Adjusted chargeable income | 430,000 |
| Tax charged at 25% | 107,500 |
| Less: Tax under the original assessment | 7,500 |
| Tax undercharged | 100,000 |
| Add: Penalty under Sec 113(2) at 100% | 100,000 |
| Additional tax payable | 200,000 |

Further, assume that withholding tax and related penalties were subsequently paid. The technical fees would now be allowed, and the revised assessment, discharge of tax and the revised penalty would be computed as follows:

| ADDITIONAL ASSESSMENT (AFTER TAX AUDIT) | RM |
|---|---|
| Adjusted chargeable income | 430,000 |
| Less: Technical fees now allowed | 400,000 |
| Chargeable income | 30,000 |
| Tax charged | 7,500 |
| Add: Penalty under Sec 113(15) | 7,500 |
| Tax payable | 15,000 |
| Less: Tax previously charged (7,500+200,000) | 207,500 |
| Tax discharged | 192,500 |

## PECULIAR SITUATIONS

Payments from which withholding taxes were not deducted and therefore if disallowed, has the obvious effect of increasing the adjusted income. In situations where the person is enjoying tax incentive say by way of a full exemption of the statutory income, the same effect now increases the exempted income by a sum equal to the amount disallowed giving rise to an irony which the Inland Revenue Board is not excited about.

Amendments are put in place where the deduction disallowed would now not be applicable to such taxpayers.

However, the deductions disallowed under paragraphs 39(1)(f), 39(1)(i) or 39(1)(j) of the ITA 1967 are still applicable to the taxpayer who enjoys tax exemption on income equal to the capital expenditure incurred or taxpayers who have no chargeable income i.e. have incurred a loss. [16]

## APPEAL ON PAYMENT OF WITHHOLDING TAX

Previously on the issue of payment of withholding tax a taxpayer had no recourse to an appeal if for some reasons the taxpayer is of the view that withholding tax does not apply to the payment. A taxpayer who is not satisfied with the matter has to apply to the High Court by way of an Order of Certiorari[17] to have the matter reviewed.

However, with effect from 1 January 2013, a taxpayer who is of the view he need not make payments of withholding tax under Section 109B may appeal to the Special Commissioners. While there are some conditions under which such appeal can be made, the new provision under Section 109H is a good move allowing the taxpayer recourse to an appeal.

## EFFECTIVE DATE AND OTHER MATTERS

The effective date is not mentioned in the Ruling. However, in the IRB's website the issue of effective date is addressed in a complicated manner with reference to the particular legislation to which the ruling applies. As some public rulings issued are also amended vide subsequent Addendums, it would help if effective dates are made specific and stated clearly in the rulings issued. [18]

Time is of the essence when making payments, and so Para 19 of the Ruling provides clarification that if the last day of the period for remitting payment is a weekly holiday or a public holiday in Malaysia, the period will include the next working day. The fact that some states in Malaysia have different weekends is apparently taken into account in the clarification.

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*[13] For a litigated case on the payer bearing the withholding tax, see EPM v KPHDN [(2001) MSTC 3306]*

*[14] See Ketua Pengarah Hasil Dalam Negeri v Teraju Sinar Sdn Bhd, Court of Appeal, Malaysia Civil Appeal No: W-01-200-2010*

*[15] Notice that the penalty is still at the rate of 100% of the tax charged.*

*[16] The words 'payers who have no chargeable income (incurred a loss)' is not included in section 39(3), and therefore may not be in line with the law. Furthermore, in Example 33, a taxpayer who is eligible to claim investment tax allowance and who has not deducted and paid the withholding tax on a technical fee paid to a non-resident has its income adjusted by not adding back the technical fee, which is contrary to what is stated in Para 16.5 of the Ruling.*

*[17] An Order of Certiorari is an application to the court to review a point of law. Such a situation arose, for example, in the case of Alam Maritim (M) Sdn Bhd v KPHDN.*

*[18] For example, the preliminary page of the Public Ruling 1 of 2014 states that the Public Ruling No 1 of 2014 (treated as a first edition) was published on 23 January 2014 and the Public Ruling No. 4/2005 dated 12.9.2005, Addendum to Public Ruling No. 4/2005 dated 30.11.2007 and Second Addendum to Public Ruling No. 4/2005 dated 4.1.2010 has been replaced with the publication of this First Edition.*

*Reference*

- *Veerinderjeet Singh, Veerinder on Taxation, 3rd Ed., CCH.*
- *Jayapalan Kasipillai, a Guide to Malaysian Taxation, 2nd Ed., McGraw Hill.*
- *Public Ruling No. 1 of 2014, Withholding Tax on Special Classes of Income, 23 January 2014*
- *CCH Malaysia-Singapore case laws on-line.*

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## CONCLUSION

This is a good ruling that assists taxpayers and the practitioners with some of the kinks in the application and compliance of Section 4A and withholding taxes under Section 109B properly explained and clarified. However, there are still some issues giving rise to uncertainties, and it is hoped that these could be ironed out in time for the next tax filing.

# CHOICE PRINCIPLE IN TAX JURISPRUDENCE

Dr. Benjamin Poh

This paper seeks to analyse how the judicially developed choice principle in tax jurisprudence of a few leading common law countries has been eroded and narrowed over the years by the supreme courts of these countries, especially the recent influential decision by the Singapore Court of Appeal in *Comptroller of Income Tax v AQQ [2014].*

The erosion of choice principle does provide the Revenue enhanced powers and discretions to invoke the general anti-avoidance rules (GAAR) to raise revenue but to the detriment of businesses and individuals living in a country without clarity and consistency in its tax laws. The invocation of GAAR is more likely today especially after the 2008 economic crisis that various economic reforms and financial austerities have been undertaken by the governments in the West to rebalance their budget deficits in the past and to regain their international competitiveness. Part I will briefly review the choice principle in tax jurisprudence; Part II will discuss the two approaches to statutory GAAR in Australia and New Zealand and why the Singapore Court of Appeal in the AQQ case chose to follow the New Zealand approach; Part III will discuss the major concerns of a tax advisor in advising tax planning facing uncertainty in GAAR; Part IV will review the UK approach and experience of introducing a statutory GAAR and Part V offers the author's opinion on why the Malaysia government should look into its current GAAR with the commitment to provide clarity and consistency to its people and foreign investors.

## PART I: CHOICE PRINCIPLE IN TAX JURISPRUDENCE

The choice principle in tax jurisprudence has been well recognised by our local judiciary and the judiciaries in the common law countries since Lord Tomlinson's famous dictum in *The Commissioners of Inland Revenue v The Duke of Westminster [1936]* that "every man is entitled to if he can order his affairs so as that the tax attaching under the appropriate Acts is less than it otherwise would be". Subsequently, the choice principle was qualified by *WT Ramsay Ltd v Inland Revenue Commissioner [1979]* where a complex series of transactions were carried out to reduce tax liability without any commercial substance was held by the House of Lords to be unacceptable tax avoidance. In *Furniss v Dawson*

*[1984],* the principle of commercial substance in tax avoidance was further enunciated by Lord Brightman, that "first, there must be a pre-ordained series of transactions; or, if one likes, one single composite transaction. This composite transaction may or may not include the achievement of a legitimate commercial (i.e. business) end … Secondly, there must be steps inserted which have no commercial (business) purpose apart from the avoidance of a liability to tax – not "no business effect". If those two ingredients exist, the inserted steps are to be disregarded for fiscal purposes. The court must then look at the end result. Precisely how the end result will be taxed will depend on the terms of the taxing statute sought to be applied." UK's GAAR was derived from common law until recently when a statutory GAAR was enacted on 17 July 2013[1]. Facing lack of commonly acceptable guidance on how to differentiate between legitimate tax planning and illegitimate tax avoidance, a number of inconsistent decisions were developed after Ramsay. Oxford Professor Judith Freedman in her article[2] stated that "the line drawn between legitimate tax planning (Barclays Mercantile Business Finance Ltd v Mawson [2004]) and illegitimate tax avoidance (IRC v Scottish Provident Institution [2004]) is based on the judicial view of the intention of Parliament, but that view does tacitly include the issue of whether the legislation could have imposed upon it an intention to look at legal concepts only or whether it can be applied to the transaction in question so as to take account of economic substance. The approach here is wider than a normal purposive construction. It is arrived at partly by looking at the legislation in context, in the normal way, but in part by a review of the nature of and manner of carrying out the scheme in question so as to reach an assessment of its economic substance."

Common law countries like Australia, New Zealand, Hong Kong, Singapore and Malaysia have statutory GAAR. The challenge for the judge when interpreting statutory GAAR is when a taxpayer is given a choice for a reduced tax liability by a specific provision of the Act, could the GAAR be invoked to defeat the choice given to the taxpayer in compliance with the legal form of the specific provision of the Act? In the Australian case of *W P Keighery Proprietary Limited v Federal Commission of Taxation [1957]*, where the choice principle was stated as giving effect to the principle of statutory construction expressed in the maxim *generalia specialibus non-derogant.* The Australian court's approach tends to look at whether the legal requirements of the specific provisions of the Act are fully complied and if it is, then Section 260 will not apply to defeat the whole scheme or arrangement.

In New Zealand, prior to Ben Nevis, the Privy Council in *Commissioner of Inland Revenue v Challenge Corporation Ltd [1987]* looked at whether the


by Dixon CJ, Kitto and Taylor JJ that "Whatever difficulties there may be in interpreting Section 260 (GAAR), one thing at least is clear: the section intends only to protect the general provisions of the Act from frustration, and not to deny to taxpayers any right of choice between alternatives which the Act itself lays open to them." The choice principle was subsequently expanded in Australian High Court Cases such as *Mullens v Federal Commissioner of Taxation [1976], Slutzkin v Federal Commissioner of Taxation [1977], Cridland v Federal Commissioner of Taxation [1977] and Federal Commissioner of Taxation of the Commonwealth of Australia v Gulland [1985]* , where the application of the choice principle was described

taxpayer incurred economic cost (e.g. reducing his income or incurring expenditure) to obtain the tax advantage and if so then it is a tax mitigation rather than tax avoidance plan. The main criticism is that the line between tax mitigation and avoidance is often difficult to draw as the taxpayer can incur economic cost or expenditure but if viewed as a whole of the entire scheme especially when the scheme involved related parties, that economic

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1 *Antony Seely, Tax Avoidance: A General Anti-Abuse Rule, (House of Common Library, 2014), 1.*

2 *Professor Judith Freedman, Interpreting Tax Statutes: Tax Avoidance and The Intention of Parliament, (Law Quarterly Review, January 2007), 70.*

cost or expenditure may be artificially created to serve the end purpose of tax reduction. In the recent case of Ben Nevis v Commissioner of Inland Revenue [2008], the Supreme Court of New Zealand looked at not only whether the legal form of the specific provisions has been complied with but whether the arrangement or scheme is consistent with the purpose behind the intended tax policy viewed in a commercially and economically realistic way.

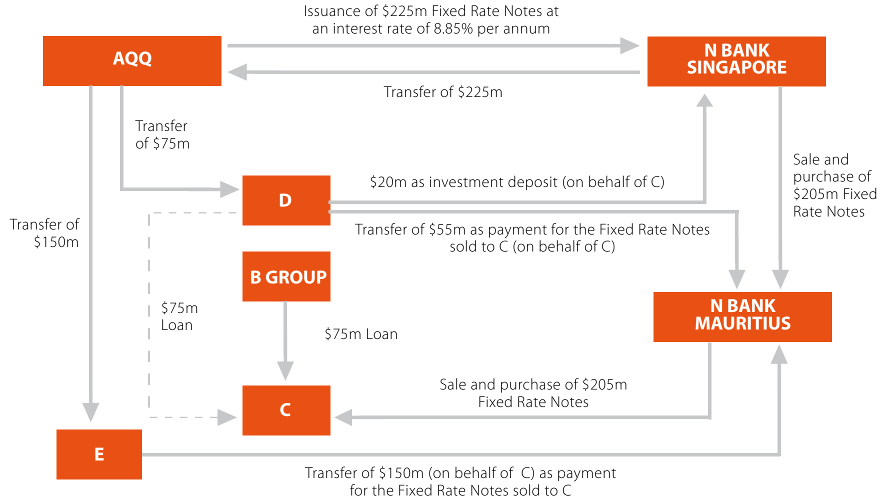


**Diagram 1**

## PART II: THE LEGAL CHOICE PRINCIPLE VS THE PURPOSIVE CHOICE PRINCIPLE

The Legal Choice Principle favoured by the Australian courts seems to have its advantages of certainty and consistency but will encourage a more aggressive tax avoidance scheme to be marketed to the detriment of government revenue. The Purposive Choice Principle favoured by the New Zealand courts is conceptually sound and may discourage aggressive tax avoidance schemes but may create more uncertainty and inconsistency to the taxpayers in practice. The reason being that for the judge to discern the intention of the Parliament, he is required to go through the history and purpose of the legislation which may be obscure, inconsistent due to numerous debates by members of the Parliament, amendments by the Minister after numerous consultations and drafting procedures. In addition, he should also consider whether the transaction was carried out in an artificial or contrived way without economic substance which may sometimes very much depend on his value judgement at the particular point of time. The UK court's approach seems to choose somewhere between the approach taken by the Australian and New Zealand courts and prefers to assess and treat the facts of each individual case differently before deciding whether the transaction is legitimate or illegitimate tax planning, a result that will always create inconsistency and uncertainty.

This has prompted the government to undertake a statutory GAAR study[3] and finally enact as law on 17 July 2013.

In *Comptroller of Income Tax v AQQ [2014]*, the Singapore Court of Appeal (CA) was confronted with a decision to choose between the Legal Choice Principle and Purposive Choice Principle. The CA finally settled the case by adopting the Purposive Choice Principle. The case involved a series of corporate restructuring exercises and financing arrangements to extract the available dividend tax credit in a number of companies within a group before the implementation of single tier corporate tax system in Singapore. The main issues that arose from the tax appeal are whether the corporate restructuring

THE MOST IMMEDIATE CONCERN FOR EVERY TAX ADVISOR IS WHETHER THE TAX PLANNING ADVICE ACCORDING TO A SPECIFIC PROVISION OF THE INCOME TAX ACT 1967 IN MALAYSIA COULD TRIGGER THE STATUTORY GAAR AFTER THE AQQ CASE.

[3] *Graham Aaronson, UK GAAR Study, (The National Archives, 2011).*

exercises, dividends distribution to AQQ (the holding company of the subsidiaries after restructuring) after offsetting the interest incurred on the financing arrangements, leaving tax credit to be refunded by the Revenue authority were considered tax avoidance schemes. Initially the Income Tax Board of Review dismissed the taxpayer's appeal on the corporate restructuring exercises, dividends distribution and financing arrangements (see **Diagram 1**) as being artificial and contrived and fell within the statutory GAAR. The High Court allowed the taxpayer's appeal on the corporate restructuring exercises and dividends distribution schemes but held that the financing arrangements were implemented in an artificial and contrived manner. The CA finally decided that all the three schemes should be viewed as a whole, the schemes were not carried out for bona fide commercial reason but with the main purpose of tax avoidance. The end result of these financing arrangements was that AQQ obtained $225m from N Bank and the entirety of this sum was effectively returned to N Bank on the same day, albeit following a circuitous route. The payment of interest expenses did not incur any real economic costs within the group as a whole.

## PART III: TAX ADVISOR'S ROLE IN ADVISING TAX PLANNING

The most immediate concern for every tax advisor is whether the tax planning advice according to a specific provision of the Income Tax Act 1967 in Malaysia could trigger the statutory GAAR after the AQQ case. Currently there is no public ruling issued by the Malaysia Inland Revenue on GAAR although a number of cases have been challenged in courts in the past regarding GAAR. One of the hallmark cases on GAAR was *SB Sdn Bhd v Ketua Pengarah Hasil Dalam Negeri [1995]* on whether by complying with the legal requirements of Section 44(6) on donation, could the Revenue invoke Section 140 to override Section 44(6) of the Act. After extensive discussion on Section 140(6) (a deeming provision that will trigger statutory GAAR) by the Special Commissioners of Income Tax on whether the donation had been made at arm's length basis, the answer given was a negative one by virtue of the special relationship between the two organisations and it was held that Section 140 overrides Section 44(6). This was however overruled by the Court of Appeal where the main issue centred on the case was whether the donations made over a number of years were tax avoidance or tax mitigation plan. The Court of Appeal adopted the approach taken by the Privy Council in *Commissioner of Inland Revenue v. Challenge Corp Ltd [1986]* and held that the donation was real and actually incurred rather than a pretence, therefore it was a tax mitigation plan.

However, the approach taken by the Privy Council in Challenge Corp Ltd was not actually adopted in Ben Nevis, whereas the purposive interpretation was adopted in the Ben Nevis and AQQ cases. The author is of the view that this approach will more likely be accepted by the Malaysian judiciary partly due to its conceptual clarity and partly due to the purposive interpretation in accordance with Section 17A of Interpretation Acts 1948 & 1967.

One might think that if the SB Sdn Bhd case were to be presented to the court after the decisions of the Ben Nevis and AQQ cases, the appeal outcome might be different. This is mainly because the donation paid out may be in contemplation of the parliamentary intention, but if viewed commercially and economically might not be consistent with Section 44(6) by virtue of the parent-subsidiary group relationship and the excessive money donated was still within the group without actually flowing out to any independent third party. Comparing the scope of the Malaysian and Singapore GAAR, the Malaysian GAAR seems to have a wider scope to catch tax avoidance schemes as Section 140(6) of the Malaysia Income

Tax Act only requires whether the transaction is at arm's length basis before triggering the statutory GAAR, whereas the Singapore Income Tax Act, Section 33(3)(b) gives an exception if the scheme is carried out for bona fide commercial reasons and had not as one of its main purpose the avoidance or reduction of tax. This exception is however measured subjectively by looking through the intention of the taxpayer.

If purposive interpretation were to be adopted by the Malaysian courts in future, the tax advisors in Malaysia could face the dilemma of whether to advise their clients to mitigate their taxes especially when they are uncertain of the legislative intention and whether the court will view the whole scheme as lacking in economic substance . Could the tax advisors prefer to be silent to their clients? In *Hossein Mehjoo v. Harben Barker & Another [2014]* the case involved negligence where a non-domiciled individual, missing much out, contended that he should have been advised to enter into a tax avoidance scheme involving offshore bearer warrants. The High Court judge held in this case that the tax advisors were negligent in not advising the non-domiciliary to use such a scheme and held that any reasonably competent accountant holding himself out as having expertise in advising non-UK domiciles should have recommended the tax planning scheme. This decision however was overruled by the Court of Appeal which held that the accountant's terms of engagement only provided general tax planning advice on the best use of reliefs rather a specialist tax planning services. This seems to be good news for tax advisors providing general tax planning advice, but for the tax advisors who hold themselves out as tax specialists providing specialised tax advisory services, they are more likely to be sued for professional negligence if they prefer to be silent to their clients.

## PART IV: UK APPROACH TO STATUTORY GAAR

In view of the unsatisfactory position of the current GAAR due to lack of clarity , uncertainty and inconsistency, a reference to how a leading common law country such as the United Kingdom approaches her statutory GAAR historically may provide us some guidance of possible future reforms of our GAAR.

The following extract[4] summarised the historical background of introducing a statutory UK GAAR (readers interested in understanding more details on UK GAAR could refer to the document at the endnotes):-

"UK tax law is specifically targeted rather than purposive in tackling the exploitation of loopholes in the law, governments have legislated against individual avoidance schemes as and when these have come to light. Often the response has been the creation of new schemes to circumvent the law, which in turn has seen further legislative action – an 'arms race' between the revenue authorities and parliamentary counsel on one side, and on the other, taxpayers aided and abetted by the legal profession. Over the past twenty years many commentators have suggested having legislation to counter tax avoidance in general: by providing certainty as to the tax consequences of any transaction, a GAAR might dissuade the most egregious efforts to avoid tax, encourage taxpayers and legal counsel to redirect their energies to more productive activities and allow the authorities to simplify the law without fear of it being systematically undermined.

In the late 1990s the Labour government consulted on a GAAR before deciding against the idea. By 2003, evidence of the scale of tax avoidance – particularly schemes targeted at individuals working in the financial sector – rekindled interest in a GAAR, though in its 2004 Budget the Labour government announced a new 'disclosure regime' as an alternative, whereby

[4] *Antony Seely, Tax Avoidance: A General Anti-Abuse Rule, (House of Common Library, 2014), 1.*

tax avoidance schemes would be required to be disclosed to the revenue departments. This note looks at the debate on the case for a GAAR over these years.

In its first Budget in June 2010 the Coalition government stated it would explore the case for a GAAR, and in November 2011 published the report of a study group, led by Graham Aaronson QC, to advise on this question. Aaronson argued in favour of a 'moderate' rule 'targeted at abusive arrangements'. The government confirmed its plans at the time of the Autumn Statement in December 2012. Provisions in the Finance Bill 2013 for the new General Anti-Abuse Rule were agreed, without changes, and the new rule came into force on 17 July 2013."

In commenting on the overarching GAAR[5] principle, Aaronson said "I have concluded that a GAAR which is appropriate for the UK must be driven by an overarching principle. This is that it should target those highly abusive contrived and artificial schemes which are widely regarded as intolerable, but that it should not affect the large centre ground of responsible tax planning. Critically, I consider that this overarching principle must be supported by the simple proposition that where there can be reasonable doubt as to which side of the line any particular arrangement falls on, then that doubt is to be resolved in favour of the taxpayer so that the arrangement is treated as coming within the unaffected centre ground."

The key features[6] of the UK GAAR are summarised below:

- The burden of proof that a taxpayer has entered into abusive arrangements will be with HM Revenue & Customs (HMRC).
- The courts can take into account any relevant material in applying the GAAR. There is a broad carve-out from the GAAR in so far as a transaction / arrangement may be established practice at the time it was entered into.
- HMRC is required to consult a newly-appointed Advisory Panel as to whether the GAAR should apply. The Panel will consist of experienced tax professionals and will provide views on whether a course of action was reasonable (a so-called single reasonableness test). It should be noted, however, that HMRC are not bound by the views of the Advisory Panel since the Panel is not sitting in a judicial capacity.
- There will not be a pre-transaction clearance procedure which would allow taxpayers to determine whether the GAAR applies to their circumstances.
- If the GAAR is invoked successfully, a taxpayer's liabilities will be adjusted on a just and reasonable basis.
- While there are no penalties associated with application of the GAAR, if the GAAR is invoked and a taxpayer is not considered to have taken due care with their tax affairs (e.g. self -assessment), then penalties may be applied under the relevant regime.


Currently the UK HMRC has developed a number of guidances[7] relating to tax avoidance for taxpayers' reference and assessment if they intend to carry out any tax planning or mitigation plan:-

***PART A*** Purpose and status of the guidance *(Mainly stating the purpose and status of GAAR)*

***PART B*** Summary of what the GAAR is designed to achieve and how it operates to achieve it.

***PART C*** Specific points *(Clarifications on what constitute a tax advantage, tax arrangement, abusive tax arrangement, counteraction of tax advantages)*

***PART D*** Examples *(Examples of legitimate tax planning and abusive tax avoidance)*

***PART E*** GAAR procedure *(Counteraction, consultation and representation procedures)*

Interested readers may go to HMRC's website to read more details on the guidances.

## PART V: TIME TO CLARIFY OUR GAAR

Tax law is a complicated area of law that affect many aspects of a country and its international competitive position, its industry, business and choice of individuals who choose to conduct their lives in that country. Though certainty in tax law may not be easily attained, but clarity and consistency is certainly a paramount requirement for every individual and business to plan their tax affairs by

entering into any agreement, arrangement and transaction to effectively carry out their tax planning.

The Malaysian government has through its Economic Transformation Plan and Vision 2020 promoted Malaysia as a preferred investment region in Southeast Asia and committed to be a developed nation by year 2020. With that mission in mind, the government has entered into various trade and tax treaties with its major trading partners to be in line with the best practice adopted by the OECD countries. It's time now for our government to relook into the current GAAR framework and clarify its position to the domestic and international taxpayers rather than leave the decision to the judiciary. The UK statutory GAAR experience has shown us that unclear position has created inconsistency in judicial precedents in the past that created difficulties for taxpayers to plan their tax affairs. This position if still left open, will definitely create unnecessary tax litigation in the future if the Revenue were to invoke Section 140 aggressively to raise revenue to balance our budget deficits in the past, and worse still discouraging domestic and foreign direct investments.

The Malaysian government may refer to GAAR experience in UK, Australia and New Zealand and the latest judicial precedents developed there to gain some general principles and guidance on how to make further clarifications on our GAAR (such as examples of legitimate and illegitimate tax planning, voluntary disclosure on tax planning schemes without penalty, etc.) and provide some critical indicators to be considered when invoking GAAR (such as the manner of scheme entered into, form and substance of the scheme, length of period of the scheme, financial position of the related parties after the scheme was carried out, whether the agreements are consistent with the function, risks and returns of the contracting parties, etc.) and guidance on what relevant materials will be considered when determining whether a scheme will fall within the GAAR. With that commitment, a fair and efficient system of tax administration will facilitate its people and foreign investors to better plan their tax affairs so as to minimise future tax controversies with the Revenue.

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[5] *Graham Aaronson, UK GAAR Study, (The National Archives, 2011), 28.*

[6] *Dixon Wilson, The UK's New General Anti-Abuse Rule (GAAR) (Dixon Wilson, 2013 ), 2.*

[7] *Part A to D has been approved by the GAAR Advisory Panel with effect from 15 April 2013*

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# GST
## SPECIAL SCHEMES

Lindsey Cruickshanks

The introduction of GST brings potential GST cash flow savings opportunities for qualifying businesses. I would like to highlight five opportunities – i) GST grouping, ii) warehousing, iii) approved trader, iv) toll manufacturing and v) jewellery manufacturing schemes - which as exceptions to the general GST rules where GST is normally charged.

These schemes require an application to and approval from The Royal Malaysian Customs ("Customs"). Specific conditions have been put in place in order to qualify for each of these schemes and to prevent potential abuse and fraud. To provide an international context, I have compared each scheme with that currently available in the Netherlands.

## GST GROUPING

For companies with multiple legal entities established in Malaysia that perform a significant volume of intercompany supplies of goods and services, it could be beneficial for them to apply for registration as a GST group. Under this scheme, qualifying companies are treated for GST purposes as a single taxable person and no GST applies on transactions among group members as these transactions are outside the scope of the Malaysian GST.

In order to qualify for group registration:

- Each company must make wholly taxable supplies. However, where a company makes incidental exempt supplies, that company is also allowed to be a member of the group.
- Each company must be GST-registered individually before they register as a group.
- One person, partnership or another company must have controlling power over the other companies and hold more than 50% of the shares.
- Members of the group cannot be members of another GST group.

According to the current versions of the General Guide and the Guide on Registration from Customs, group registration is allowed regardless of the type of taxable supplies made by companies within the same group.

The GST group must appoint a representative member. Any taxable supply by or to a member of the group will be treated as a supply by or to the representative member. Supplies to non-group members or third parties are considered regular supplies for GST purposes and subject to GST, unless subject to specific zero rating or exemption or other treatment applies.

***Note:*** *There is a possibility for venturers performing petroleum related activities to apply for registration as a joint venture. I will not address the specifics of this within the scope of this article; however, information can be found in Section 69 of the GST Act 2014 and within the Petroleum Upstream Guide. Similar to GST grouping, any taxable supplies between the venturer and the venture operator will be disregarded.*

### *Advantages*

The advantage of grouping is mainly the GST cash flow benefit since normally GST on intercompany supplies would be charged and have to be paid by one company to Customs with later recovery by the intercompany counterpart. Group members do not need to account for GST on goods and services supplied between them. This is especially useful if the accounting system is centralised. An arrangement such as this generally removes the necessity of issuing tax invoices in respect of inter-group transactions. Also, in terms of GST return filing, companies within a GST group only need to submit one GST return for the entire group.

### *Potential costs / risks*

Under GST grouping, all group members are jointly and severally liable with respect to any GST due or payable. There are specific costs and administrative efforts necessary to consolidate the GST reporting and to set up the IT condition table and tax coding for GST group and non-group transactions. Furthermore, monitoring should be performed over time to ensure that the group members still fulfill the necessary requirements in order to be part of the group.

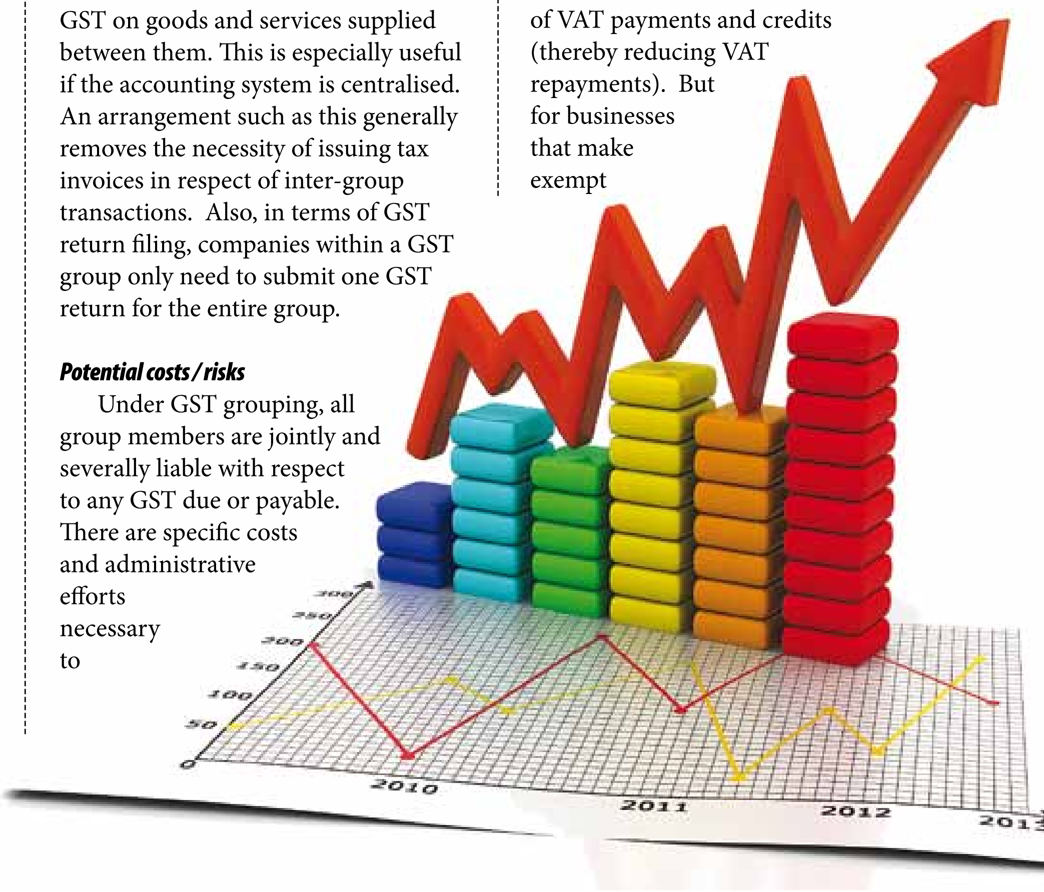
### *Initial actions required*

Given their current business model, companies need to determine:

- Whether GST grouping would be feasible and beneficial
- Which companies could or should be included in the group and ensure that prior to application all necessary requirements would be met.

### *Comparison to Dutch / EU legislation*

In most EU member states where grouping exists, the effect is to allow related legal entities to make inter-company supplies of goods and services without charging Value Added Tax ("VAT"). For businesses that can recover VAT in full, this can ease cash flow or allow the offset of VAT payments and credits (thereby reducing VAT repayments). But for businesses that make exempt



supplies (such as those in the financial and insurance sectors), VAT grouping is far more significant as it prevents the addition of irrecoverable VAT cost to charges made between group members. As such, grouping has long been held to be an important provision for exempt and partly exempt taxpayers. The Malaysian GST Act only allows for companies performing wholly taxable activities (incidental exempt activities allowed) to form a group. However, under the Malaysian GST Act, banks and other financial institutions which provide loans or financing to businesses can reclaim the input GST charged to them according to the Fixed Input Tax Recovery (FITR) method.

Unlike in Malaysia, in the Netherlands there is a requirement for VAT group members to satisfy an economic link criteria whereby the activities of the group companies essentially serve the same economic purpose (e.g. same client group – similar or related supplies aimed at the same public) or the activities of the one group company are performed essentially for the purposes of the other group company.

## GST WAREHOUSING SCHEME

Under the GST Act, goods are subject to 6% GST upon importation into Malaysia. The only exceptions are with respect to those imported goods to which the 0% GST applies according to the Zero-Rating Order (e.g. rice, vegetables, fish, etc.) or where Special Relief applies.

In order to alleviate GST cash flow difficulties upon import into Malaysia, since the recovery of input tax occurs after submission of the GST return, any GST payment on imported goods deposited into a qualified licensed warehouse or moved from one such warehouse to another will be suspended. While located in such warehouse, there is a list of value added activities which can be performed on the goods which consist of bulk breaking, repacking, relabelling, sales within the warehouse under suspension, consolidation, re-export of imported goods and internal transport and handling within the warehouse.

Any goods which are later released from the warehouse as Customs cleared for sales within Malaysia (other than the Designated Areas of Labuan, Langkawi and Tioman) are subject to 6% import GST on top of customs duties and excise duties where applicable. Goods intended for sale to Designated Areas or overseas are subject to 0% GST as exports.

All goods and services such as handling and storage charges which are consumed in the warehouse will be standard rated.

This scheme is applicable to customs warehouses, licensed warehouses, duty free shops and inland clearance depots (ICDs) under Sections 63, 65, 65D and 65E of the Customs Act 1967 respectively.

If there are multiple sales which take place in the warehouse, assuming the last sale is for domestic consumption, only that last sale which causes removal from the warehouse will trigger the customs duty and GST tax points.

### *Advantages*

As indicated above, storing goods under the warehousing scheme provides a GST cash flow advantage until the point of removal from the warehouse for consumption in Malaysia. If the goods are not imported into Malaysia, then no Malaysian GST will apply. Inter-warehouse movements of goods will not attract GST.

### *Potential costs / risks*

Warehouse operators must:

- Furnish a bank guarantee or bond to cover the estimated duty and/or GST payable on the imported goods held at any one time.
- Maintain lot number records. A lot number is a unique transaction number assigned by the warehouse operator for each product in a shipment of goods. It is required for the purpose of tracking the particular goods of a shipment.
- Submit a monthly return on the movement of goods and a discrepancy report (when applicable). Operators are also required to furnish an audit report to the GST officer or proper officer of Customs. The operator's account may be audited by the GST officer whenever necessary.

### *Initial actions required*

Warehouse operators need to ensure that their warehouses qualify under the definition of the Customs Act. Goods owners and / or their agents need to communicate with their logistics providers and to seek clarification as to whether the warehouse facilities used by them qualify under the warehousing scheme or not.

### *Comparison to Dutch / EU legislation*

The Netherlands has numerous warehousing schemes available. Similar to the Malaysian approach, these types of warehousing schemes are attractive cash flow incentives for foreign companies that bring goods into the country for storage and onward selling purposes within the region.

## APPROVED TRADER SCHEME (ATS)

Companies registered under the Approved Trader Scheme can suspend GST on importation. This scheme has been introduced to alleviate the GST cash flow burden of frequent exporters who would otherwise seek to claim

significant input tax credit pertaining to the import of goods.

Parties qualifying for consideration as Approved Traders consist of:

- All companies operating in the Free Industrial Zones (FIZs) according to paragraph 10 (1)(b) of the Free Zones Act 1990
- All Licensed Manufacturing Warehouse (LMW) operators licensed under Section 65A of the Customs Act 1967
- International Procurement Centres (IPCs) and Regional Distribution Centres (RDCs) approved by the Malaysian Investment Development Authority (MIDA)
- Toll manufacturers registered under the Approved Toll Manufacturer Scheme (ATMS)
- Jewellery manufacturers registered under the Approved Jeweller Scheme (AJS)
- Companies with turnover above RM25 million and more than 80% of their supplies made are zero-rated
- Any other person or class of persons as approved by the Minister

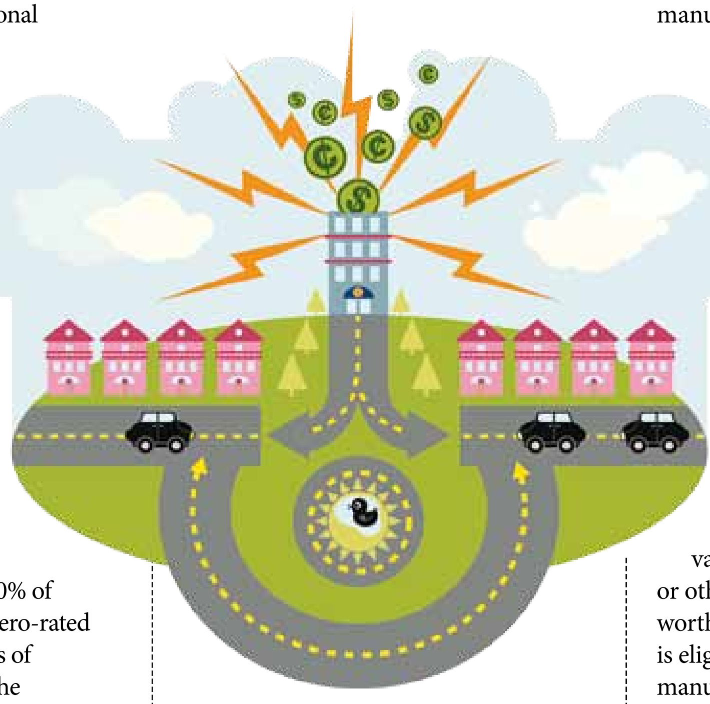
With regard to specific conditions required to apply for the ATS, please refer to the Appendix.

***Advantages***

The main advantage is GST cash flow in nature as the normal GST charge upon import will be suspended. This scheme allows regular exporters to minimise their GST refund position as no input tax would need to be reclaimed with respect to "imports" which are subsequently exported overseas or sold to Designated Areas.

***Comparison to Dutch / EU legislation***

Dutch VAT legislation offers an import VAT deferment scheme to Dutch established traders. Foreign traders can also apply for such a scheme, provided that they appoint a fiscal representative which is established in the Netherlands. This requires reporting of the import VAT payable and offsetting input VAT in the relevant VAT return (no cash flow impact). Such a scheme is widespread and there is no requirement to act as a



major exporter. Even companies who only sell their products domestically can benefit from this scheme. Otherwise, for major exporters, they could use a bonded warehouse to mitigate the payment of import GST on goods to be exported. Other European countries such as France and Italy have frequent exporter schemes similar to the Malaysian approach where GST on imports can be disregarded. In addition, GST on local purchases can be disregarded provided certain administrative procedures are met.

The ATS will help to further establish Malaysia as a distribution hub within the ASEAN region.

## APPROVED TOLL MANUFACTURER SCHEME (ATMS)

A toll manufacturer is a manufacturing service provider from whom an owner of raw materials can request services in order to carry out the manufacturing process. A principal party is the owner of the goods and maintains ownership to these goods while they are undergoing manufacturing services at the toll manufacturer's location. The toll manufacturer will invoice the principal for the supply of services. Because of cost advantages in Malaysia, despite the cost of transport to and from the toll manufacturer's location, it can still be beneficial to have these services performed here. This typically involves the import and export of products into the toll manufacturer's country.

Any toll manufacturer who has contracted with overseas principals to perform value added processing, assembling or other manufacturing related activities worth RM 2 million or more per annum is eligible to apply for the approved toll manufacturer scheme (ATMS) subject to approval by the Director-General of Customs. Malaysian customers of the overseas principal must apply together with the toll manufacturer for ATMS status in order to ensure that correct recipient accounting takes place.

For specific conditions to be satisfied in order to qualify for the ATMS status, please refer to the Appendix.

***Services performed by the Malaysian toll manufacturer***

This scheme is provided to disregard GST on any supply of services made by the local toll manufacturer to the overseas principal.

***Imports***

Regarding the import of goods from overseas to Malaysia, the toll manufacturers can apply for ATS facilities (refer to above), and once approved, import GST can then be suspended. Otherwise, the toll manufacturer would have to pay import duties and GST on the goods consigned and sent by the overseas principal at the time of importation.

***Domestic purchases made by an overseas principal under ATMS***

A domestic supply of raw materials or components concluded with an overseas principal but delivered to the Malaysian toll manufacturer is expected to be treated as zero rated supply. Otherwise, if the ATMS were not in place the domestic purchase would be subject to 6% GST which the overseas principal potentially could not recover unless it were to be GST registered in Malaysia by means of a tax agent.

***Export and sales subsequent to manufacturing***

- Under the conditions for the ATMS facility, at least 80% of the manufactured or processed goods must be exported to the overseas principal in his country of origin or to any other countries as instructed by the principal. For this export, the ATM has no GST reporting or payment liability as the goods are owned by the foreign principal.
- Also, when processed goods are delivered by the toll manufacturer on behalf of his overseas principal to a Malaysian customer, the toll manufacturer need not account for GST on the domestic supply. The local recipient needs to account for GST by way of "recipient accounting".
    - In the case where the local recipient is GST registered, the local recipient will need to account for GST in his GST return (GST-03) as offsetting output tax and input tax entries.
    - If the local recipient is not GST registered, this recipient must account for GST in a special form (GST-04).

***Advantages***

Without this scheme, the toll manufacturer would need to charge 6% GST on the services it provides to its overseas principal. This is because the services are provided by a Malaysian taxable person in direct connection with goods and these services are performed while the goods are in Malaysia.

***Comparison to Dutch / EU legislation***

There is no special scheme for toll manufacturers in the Netherlands. Toll manufacturers are seen as service providers and the VAT treatment for their manufacturing services would fall under the scope of the general Business to Business (B2B) rules of "place of supply is where the recipient of the services is established". There would be no VAT charged on the supply of such services to an overseas principal.

## APPROVED JEWELLER SCHEME (AJS)

This scheme has been introduced in order to provide GST cash flow relief to approved jewellery manufacturers (AJM) as they would otherwise be in an ongoing GST reclaimable position given the nature of their business. Jewellery manufacturers would typically incur input GST upon their purchases upfront and would only charge GST to clients at a later date as sales take place.

Under this scheme, where prescribed precious metals consisting of gold containing at least 99.5% purity, silver containing at least 99.9% purity and platinum containing 99% purity are supplied by a gold bullion house, bank or refiner to an AJM for the purpose of manufacturing jewellery, GST is accounted for by way of "recipient accounting". What this means is that upon the local purchase of the prescribed precious metals, the AJM is required to account for output tax and can offset this with the deemed input tax credit on the acquisition of the precious metals in the course of his business. On the invoice from the gold bullion house, bank or refiner directly to the AJM, GST should be shown together with the statement "The buyer as stated in this invoice shall account for the output tax on the supply to the Director-General in accordance with Section 73 of the Goods and Services Tax Act 2014."

***Initial actions required***

Provided the jewellery manufacturer is a taxable person, he may apply for the AJS subject to approval from the Director-General using the required application form.

***Comparison to Dutch / EU legislation***

Under the Dutch VAT Act and the EU Directive, there are special rules for the sale of investment gold (defined as gold in the form of bars and plates with purity of at least 995/1000 and in the form of securities and certain gold coins with a purity of at least 995/1000). According to the main rule, the supply of gold in the above forms is exempt from VAT.

However, if the buyer is a taxable person, the supplier of investment gold may opt for taxation in writing to the tax authorities. If he opts for taxation, he has the same rights to recover input VAT as do taxable persons according to the general rules in the VAT Act. An option for taxation prevents an accumulation of input VAT in the price of investment gold.

In the Netherlands, the reverse charge mechanism applies to the following domestic transactions:

- The supply of gold or a semi-finished product from gold with

a purity of at least 325/1000 to a taxable person (e.g. jewellery manufacturer); and
- The supply of investment gold after an option for taxation has been exercised

Unlike the Malaysian approach, the EU Directive and Dutch approach only apply to gold and not to silver and platinum.

***Conclusion***

Advisors should discuss and review the relevant facilities with their clients. Some companies will likely be familiar with such schemes as they relate to other jurisdictions and may require clarification on the Malaysian definitions, eligibility and specific requirements and implications for their day to day business.

**Appendix**

There are five (5) common conditions which are mandatory for the ATS, ATMS and AJS:

1. GST registered person
2. Must be a monthly GST filer
3. Submits its returns electronically
4. Has performed and complied with all duties and obligations to account for and pay tax
5. Accounting and internal controls are able to meet the required accounting and auditing standards

Approval under these schemes is limited to a two (2)-year period. Should the participant wish to prolong its participation under any of these schemes, the company would need to re-apply at least two (2) months prior to the expiry date in order to ensure uninterrupted continuation of benefits.

Furthermore, the specific requirements for each are outlined as follows:

***ATS – specific conditions***

- The goods imported must be for the purpose of making taxable supplies; the import of goods for personal use of staff or directors is not allowed.

- The import and export of goods must be in the name of the Approved Trader.
- The Approved Trader must make wholly taxable supplies. Incidental exempt supplies that fall within the *de minimis* limit will be allowed.
- The net value of goods brought into Malaysia under the ATS and the amount of GST which has been suspended must be reported in the GST return (Boxes 14 and 15 respectively).
- Turnover of more than RM25m
- Must make at least 80% zero rated supplies (either exports, local zero-rated supplies or international services)
- Imports must be declared electronically

***Note:*** *The total value of goods brought into Malaysia under the ATS must be declared in the monthly GST return along with the amount of GST which has been suspended.*

***ATMS – specific conditions***

Other conditions which must be satisfied include:

- The value of processing supplies for and to overseas companies must be RM2m per annum or more and
- At least 80% of goods must be exported from Malaysia by the toll manufacturer.

***AJS – specific conditions***

Jewellery manufacturers must:

- Acquire the precious metals for manufacturing jewellery in the furtherance of a business. Any acquisition of precious metals other than for the purpose of manufacturing jewellery does not come under the scope of AJS, and is thus subject to GST. For example, AJS approval cannot be used on any acquisition of precious metals for investment purposes.
- Acquire the precious metals either from overseas or locally, to manufacture jewellery in their name. All imports and exports must be declared under the approved jeweller's name. However, authorised forwarding agents duly appointed can sign the import / export forms on the approved jeweller's behalf, but the approved jeweller will still remain liable for any tax and duties due or payable on the imports.

**The above is based on information provided by Customs, available at the time of writing.**

*The views reflected in this article are the views of the author and do not necessarily reflect the views of the global EY organisation or its member firms.*

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This column only covers selected developments from countries identified by the CTIM and relates to the period 16 May 2014 to 15 August 2014.

## CHINA (PEOPLE'S REP.)

### Notice on enhancing tax collection in respect of transfer of equity interest

The SAT issued Shui Zong Han [2014] No. 318 on 8 July 2014 concerning the tax collection on transfer of equity interest. The Notice intends to provide guidance on the tax collection policy that the local tax authorities should adopt and is generally administrative in nature. However, the Notice does stress that transfer of equity interest transactions should be considered high priority and that the administration should focus on investment by shares, distribution of dividends/profits, alteration of shareholders, restructuring and liquidation. The tax authorities should ascertain the time of realisation of the gains, price, tax base and amount of the gains. Additionally, careful attention should be paid to the following risky points:

- equity investment using non-monetary assets;
- capital gains on equity interest held for less than 12 months;
- shift of equity interest between group companies without compensation;
- low transfer price; and
- shifting of shareholding to a low tax jurisdiction.

### New rules on reporting foreign participation and foreign income

The SAT issued SAT Gong Gao [2014] No.38 on 30 June 2014 regarding information requirements for foreign income and foreign participation. The announcement applies from 1 September 2014.

Resident enterprises that have incorporated or participated in or disposed of an existing interest in foreign companies are required to complete the new "Information Form on Foreign Participation of Resident Enterprise" to provide information where:

- the direct or indirect participation in a foreign company exceeds 10% of share capital or share capital with voting rights of the foreign company; and
- the direct or indirect participation in a foreign company has increased from less than 10% to 10% or more or vice-versa.

The participation and income must be calculated in accordance with the Chinese accounting rules and the form must be filed together with the annual corporate income tax return. In addition, a resident enterprise is required to complete the "Information Form on Controlled Foreign Company (CFC)" in cases where the CFC rules under Art. 45 of the Corporate Income Tax Law or Art. 84 (Guo Shui Fa [2009]) No.2 on Implementation Rules of Special Tax Adjustment apply. Article 84 (Guo Shui Fa [2009]) No. 2 states that the CFC rules do not apply if the foreign company is situated in a country listed as a non-low tax country by the SAT, or the income is mainly generated from business operations or the annual amount of profits is less than CNY5 million.

The date for submitting the information forms can be extended if justified. However, the prohibition of providing such information by foreign laws and regulations would not constitute sufficient justification.

Finally, the announcement equally applies to Chinese permanent establishments or branches of non-resident companies deriving foreign income which is effectively connected with such establishments/branches.

### Tax treatment of dividends of unlisted SMCs amended

The Ministry of Finance (MoF), the SAT and the China Securities Regulatory Commission jointly issued Cai Shui [2014] No.48 on 27 June 2014 regarding the new tax treatment of dividends of small and medium-sized companies (SMCs) registered with the Share Transfer System. From 1 July 2014 until 30 June 2019, such dividends are taxed as follows:

- only 25% of the above dividends are taxable if the underlying shares are held for more than 1 year;
- only 50% of the above dividends are taxable if the underlying shares are held between 1 month and 1 year; and
- the full amount is taxable if the underlying shares are held for less than 1 month.

The security companies are required to withhold the taxes.

### Stamp duty for transfer of preferred shares

The MoF and SAT jointly issued Cai

Shui [2014] No. 46 on 27 May 2014 clarifying that the documents on transfer of preferred shares by virtue of purchase and sale, inheritance or donation are subject to stamp duty at a rate of 1% from 1 June 2014. The transferor is liable to the duty.

## HONG KONG

### Inland Revenue (Amendment) Bill 2014 passed

The Inland Revenue (Amendment) Bill 2014 was passed by the Legislative Council on 25 June 2014 and includes:

- a one-off reduction of 75% of profits tax, salaries tax and tax under personal assessment for the year of assessment 2013/14, subject to a maximum of HKD10,000 per case; and

- increase of allowances for maintaining a dependent parent/grandparent and raising the deduction ceiling for elderly residential care expenses under salaries tax and tax under personal assessment.

### Stamp Duty on property transactions

The Hong Kong Inland Revenue Department (HKIRD) has issued the following in relation to Stamp Duty:

***Stamp Duty (Amendment) (No. 2) Bill 2014***

The amending Bill was gazetted on 25 July 2014 and its amendments include:

- an increase of the ad valorem stamp duty (AVD) rates (Scale 1) on certain instruments dealing with immovable property executed on or after 23 February 2013. Unless specifically exempted or otherwise provided, AVD is payable at Scale 1 on an agreement for sale for the acquisition of any residential property or non-residential property, if the agreement is executed on or after 23 February 2013. Scale 1 also applies to a conveyance on sale of such a property executed on or after that date. The Scale 1 rates range from 1.5% to 8.5%
- the timing for charging of AVD on non-residential property transactions from the conveyance on sale to the agreement for sale executed on or after 23 February 2013.

***Stamp Office Interpretation and Practice Notes No. 5 (SOIPN 5)***

On 31 July 2014, SOIPN 5 on Special Stamp Duty (SSD) was gazetted by the HKIRD. SSD applies to residential properties of all values acquired on or after 20 November 2010 and resold or transferred within 24 months or 36 months after acquisition, in addition to the current ad valorem stamp duty. The SSD payable is calculated based on the stated consideration for the transaction or the market value of the residential property as assessed by the Commissioner of the Inland Revenue, whichever is higher, at progressive rates. The applicable rates depend on the date of purchase and the period of holdings and the Payment of the SSD is exempted in select cases and the vendor and the purchaser are both jointly and severally liable for paying SSD.

### Stamp Office Interpretation and Practice Notes No. 7 (SOIPN 7)

On 31 July 2014, SOIPN 7 on Buyer's Stamp Duty (BSD) was gazetted by the HKIRD. BSD is chargeable on an agreement for sale or a conveyance on sale for the acquisition of any residential property acquired on or after 27 October 2012 by any person (including enterprises) except a Hong Kong Permanent Resident (HKPR).

The BSD payable is calculated based on the stated consideration for the transaction or the market value of the residential property as assessed by the Commissioner of the Inland Revenue, whichever is higher, at a flat rate of 15% in addition to the ad valorem stamp duty and the special stamp duty (SSD) if applicable.

Payment of the SSD is exempted in select cases and the vendor and the purchaser are both jointly and severally liable for paying SSD.

### Departmental interpretation and practice notes on taxation of specified alternative bond schemes released

The HKIRD issued Departmental Interpretation and Practice Notes No. 50 (DIPN 50) on taxation of specified alternative bond schemes on 11 July 2014. The DIPN 50 sets forth the HKIRD's views and practice on the taxation of specified alternative bond schemes. The key features of DIPN 50 are:

***Alternative bond scheme***

The term "alternative bond scheme" (ABS) is used in the amendment ordinance to represent the arrangements which will be treated as debt arrangements for profits tax purposes upon fulfillment of certain conditions. Generally, the ABS is a tripartite structure with the originator (which may be, in substance, the borrower); the bond issuer (the BI) which must be a special purpose vehicle (the SPV); and the bondholder (the BH).

Under the ABS, the BI and the BH enter into a bond arrangement (the BA) while the BI and the originator enter into an investment arrangement (the IA). Under the BA, alternative bonds are issued to the BH. Under the IA, assets are acquired and managed to generate income or gains to fund the payments to the BH in the BA.

***Specified investment arrangements***

DIPN 50 specifies and details four types of IAs: (i) a lease arrangement; (ii) a profits sharing arrangement (iii) a purchase and sale arrangement; or (iv) an agency arrangement.

DIPN 50 also sets out the qualifying conditions for a bond arrangement and a special investment arrangement.

***Advance rulings***

The application for an advance ruling is available when the information of the specified ABS and details of each type of specified IA are provided.

***Interest article in the concluded taxation agreements***

In DIPN 50, the qualifying BA and qualifying IA in a specified ABS are regarded as debt arrangements. Thus, the definition of "interest" in the interest article of taxation agreements entered into by Hong Kong should be applicable to additional payments and investment return made under qualified BA and qualified IA.

## INDIA

### Budget for 2014-15 – details

The Budget for fiscal year 2014/15 was presented on 10 July 2014. Some of the more significant taxation proposals are detailed below. Generally, the direct tax proposals when passed are to take effect when ratified by Parliament, whilst the indirect tax proposals are to have immediate effect.

***Direct taxation***

- The personal income tax exemption limit for individual taxpayers below the age of 60 years and senior citizens is to be increased from INR200,000 to INR250,000 and from INR250,000 to INR300,000 respectively.
- The investment limit under Section 80C (i.e. deductions available to individuals and Hindu undivided family in respect of contributions to

certain investments) is to be increased from INR100,000 to INR150,000.
- The deduction limit on account of mortgage interest on loans for a self-occupied home is to be increased from INR150,000 to INR200,000.
- The rate of tax on long-term capital gains arising from the transfer of units held for more than 12 months in the case of mutual funds other than equity oriented funds is to be increased from 10% to 20%. The period of holding in respect of the units of the mutual fund is also to be increased from 12 months to 36 months.
- Income arising to foreign portfolio investors from transactions in securities is to be treated as capital gains.
- A 10-year tax holiday is to be extended to undertakings which begin generation, distribution and transmission of power by 31 March 2017.
- In the case of non-deduction of tax on specified payments to non-residents, 30% of such payments will be disallowed instead of 100%.
- Income and dividend distribution tax is to be levied on the gross amount instead of amount paid net of taxes.
- A roll-back provision is to be introduced in the Advance Pricing Agreement scheme.
- The arm's length range concept is to be introduced for determination of the arm's length price. However, the arithmetic mean concept will continue to apply where the number of comparables is inadequate.
- Multiple year data analysis is to be introduced for the purposes of transfer pricing comparability.

***Indirect taxation***

Service tax on loading, unloading, storage, warehousing and transportation of cotton is to be exempted.

The scheme of advanced ruling in indirect taxes is to be expanded to cover resident private companies. The scope of settlement commission is to be enlarged to facilitate quick dispute resolution.

- Goods and services tax is most likely to be introduced in fiscal year 2014/15.

*Tax administration*

A high-level committee is to be set up which will interact with the trade and industry on a regular basis and ascertain areas where clarity on tax law is required.

All fresh cases arising out of the retrospective amendments (i.e. based on Finance Act 2012) in respect of indirect transfers and coming to the notice of the assessing officer are to be scrutinised by a high-level committee to be constituted by the CBDT.

*Advance ruling and other tax-related measures*

- The advance ruling scheme is to be extended to resident taxpayers.
- The scope of the Income Tax Settlement Commission is to be enlarged.

## INDONESIA

### Tax audit plan and strategy in 2014

The DGT has unveiled its audit plan and strategy for 2014 through its Circular No. SE-15/PJ/2014 dated 21 March 2014. The Circular, which states that this year's revenue target from tax audits is IDR24 trillion, describes the following:

A. Audit Plan - Generally, the focus of tax audits will be on any business sectors with low tax compliance, significant contributions to the economy and tax revenue, good prospects in 2014 and/or high growth. Regional audit focus will be decided by the head of the regional tax office based on the taxpayer's compliance risk.

For entities, the focus of tax audits will be on the property business and financial services industry. For individuals, tax audits will focus on entrepreneurs, shareholders and notaries.

B. Audit Strategy - The DGT's head office may issue instructions for special audits on: (i) domestic related-party transactions, (ii) oil and gas companies; (iii) transfer pricing; and (iv) joint audits with external auditors.

Instructions for special audits may also be given as a result of the development and analysis of information, data, reports and complaints from the DGT's intelligence and investigation unit as well as any government institution.

### Requirement to use electronic VAT invoices

The DGT has announced its plan to require all taxpayers to use electronic VAT invoices. The first phase of the plan will be applied to certain taxpayers from 1 July 2014 and eventually electronic VAT invoices will have to be used by taxpayers nationwide by 1 June 2016.

## SINGAPORE

### Income tax treatment of hybrid instruments


The Inland Revenue Authority of Singapore (IRAS) issued an e-Tax Guide on 19 May 2014 that sets out the income tax treatment of hybrid instruments, including the factors generally used to determine whether such instruments should be treated as debt or equity for income tax purposes. At present, there are no specific provisions in the Income Tax Act (ITA) that stipulate the considerations or factors for determining the nature of a hybrid instrument.

The Comptroller of Income Tax (CIT) will take the approach that the characterisation is first determined based on its legal form. If the legal form is not indicative of, or does not reflect, the legal obligations and rights, then the characterisation of the hybrid instrument would be determined based on, but not limited to, the following: (i) nature of interest acquired; (ii) right to participate in issuer's business;(iii) voting rights conferred by the instrument;(iv) obligation to repay the principal amount;(v) payout;(vi) investor's right to enforce payment;(vii) classification by another regulatory authority; and (viii) ranking for repayment in the event of liquidation or dissolution.

It is not sufficient to classify the hybrid instrument as debt or equity based on the presence of any single factor as listed above. A combination of factors, the facts and circumstances of the case have to be taken into account in order to determine the characteristics of the instrument.

*Issuer of hybrid instruments*

The CIT will apply the approach mentioned above to a Singapore-based issuer. Where a foreign issuer issues a hybrid instrument, the CIT will examine the facts and circumstances, including the characterisation of the hybrid instrument in the country of the issuer, as well as the factors listed above, in order to determine the characterisation of the distribution derived by investors in Singapore.

In the event of a mismatch between how both jurisdictions classify the hybrid instrument, the CIT will evaluate the basis for different characterisations taking into consideration the specific facts of the case, before it determines the character of the instrument for income tax purpose in Singapore.

***Tax treatment for hybrid instruments characterised as debt***

For tax purposes, when a hybrid instrument is characterised as a debt instrument, the distribution from the issuer to the investor will be regarded as interest. The Singapore-based issuer of such instrument may be allowed a tax deduction on the interest expense incurred subject to the conditions under Sections 14(1) and 14(1)(a) of the ITA, and provided that the deduction is not prohibited under any other provisions of the ITA.

The interest income is taxable in the hands of the investor unless it is specifically exempt from tax under the ITA.

***Tax treatment for hybrid instruments characterised as equity***

For tax purposes, when a hybrid instrument issued by a company or Real Estate Investment Trust (REIT) is characterised as an equity instrument, distributions from the issuer to the investor are regarded as either dividends or REIT distributions. In this regard, no deduction will be allowed to the Singapore-based issuer in respect of distributions paid to investors.

Dividend paid by a resident company in Singapore, being one-tier dividend, is exempted from tax in the hands of the investor. In all other cases, the dividend received by investors in Singapore will be subjected to tax. However, foreign-sourced dividend may qualify for tax exemption under either Sections 13(7A), 13(8) or 13(12) of the ITA.

The tax treatment for REIT distributions depends on the underlying receipts from which the distribution is made and the profile of the investors.

## VIETNAM

### Decree No. 218 and Circular No. 78 on CIT

The MoF issued Circular No. 78/2014/T-BTC (Circular No. 78) on 18 June 2014. Circular No. 78 provides supplementary implementation guidance in respect of Decree No. 218/2013/ND-CP (Decree No. 218) which was issued on 26 December 2013.

***Taxable income*** - Losses arising from the transfer of real estate, investment projects or rights to participate in an investment project may be offset against business profits. Gains arising from the transfer of real estate, however, may not be used to offset business losses except in the case of liquidation.

***Revenue recognition*** - Revenue relating to the provision of services

which spans across a number of years may either be fully recognised upon receipt of the payment or may be apportioned accordingly over the relevant number of years. However, only the latter treatment applies to incentivised enterprises.

***Deductions***

- Non-cash payments of over VND20 million must be properly documented/ evidenced before a deduction is allowed.
- Land use right expenses incurred during a period where the business has or construction works are deductible.
- Kindergarten tuition fees for an enterprise's expatriate's children will be deductible if properly documented/ evidenced.
- Provisions for salary must be fully utilised within six months from the financial year end. Any unused balance will be used to reduce the deductible amount allowed in the following year.
- Contributions made to voluntary pension, life insurance and social security funds are deductible up to VND1 million per person per month.
- The advertising and promotions deductible expenditure cap has increased to 15%.
- Licensed casinos and gambling outlets may deduct management fees up to a cap of 4% of revenue.

Corporate income tax (CIT) rate - The standard CIT rate of 22% applies from 1 January 2014. This means that enterprises whose financial year overlaps 2013 and 2014 will be required to apply the old rate of 25% until 31 December 2013 and the new rate of 22% from 1 January 2014 onwards.

CIT incentives - Circular No. 78 also provides detailed guidance on the CIT incentives available for new investment projects and business expansion. Circular No. 78 is currently only available in the Vietnamese language.

*By **Rachel Saw** and **Nina Haslinda Umar** of the International Bureau of Fiscal Documentation (IBFD). The International News reports have been sourced from the IBFD's Tax News Service. For further details, kindly contact the IBFD at ibfdasia@ibfd.org*

# TechnicalUpdates

*The technical updates published here are summarised from selected government gazette notifications published between 16 May 2014 and 15 August 2014 including Public Rulings and guidelines issued by the Inland Revenue Board (IRB), the Royal Customs Department and other regulatory authorities.*

## INCOME TAX

### Fund Management Services - Income Tax (Exemption) Order 2014

Income Tax (Exemption) Order 2014 [P.U. (A) 150/2014], gazetted on 4 June 2014, provides a 100% tax exemption on the statutory income derived by a qualifying company from the business of providing fund management services to a business trust (BT) or real estate investment trust (REIT) in Malaysia which is managed in accordance with *Syariah* principles and certified by the Securities Commission. The Order takes effect from the year of assessment 2014 until the year of assessment 2016.

### RAPID Complex- Income Tax (Exemption) (No. 2) Order 2014

Income Tax (Exemption) (No. 2) Order 2014 [P.U.(A) 166/2014], gazetted on 20 June 2014, provides a 50% tax exemption on statutory income derived from a qualifying activity carried out in the RAPID Complex for five consecutive years of assessment commencing immediately after the 15 years of assessment exemption period under the Income Tax (Exemption) (No. 7) Order 2013 has ended. The Order took effect from the year of assessment 2011.


### Angel Investor - Income Tax (Exemption) (No. 3) Order 2014

Income Tax (Exemption) (No. 3) Order 2014 [P.U.(A) 167/2014], gazetted on 20 June 2014, provides an income tax exemption on the aggregate income of a qualifying angel investor for the basis period of the second year of assessment following the year of assessment in which a qualifying investment is made. The amount of tax exempted shall be equal to the amount of the investment made in an investee company. Where the amount of the investment is more than the aggregate income of the angel investor for the aforementioned second year of assessment, the excess amount shall not be refunded or be made available for tax credit purposes and is effectively lost. The Order took effect from 1 January 2013.

### Income Tax (Deduction for Expenditure in relation to Vendor Development Programme) Rules 2014

Income Tax (Deduction for Expenditure in relation to Vendor Development Programme) Rules 2014 [P.U.(A) 169/2014], were gazetted on 24 June 2014. The Rules provide a double deduction on qualifying expenditure such as product quality development, business process re-engineering and vendor skills training for a period of three consecutive years of assessment, commencing from the year of assessment in which the expenditure is first incurred. The total qualifying expenditure for each year of assessment is, however, capped at RM300,000. The Rules are applicable to a qualifying resident anchor company that participates in the approved Vendor Development Programme under a memorandum of understanding signed with the Ministry of International Trade and Industry from 1 January 2014 to 31 December 2016. The Rules take effect from the year of assessment 2014.

### Income Tax (Deduction For Expenditure In Relation To Minimum Wages Rules 2014

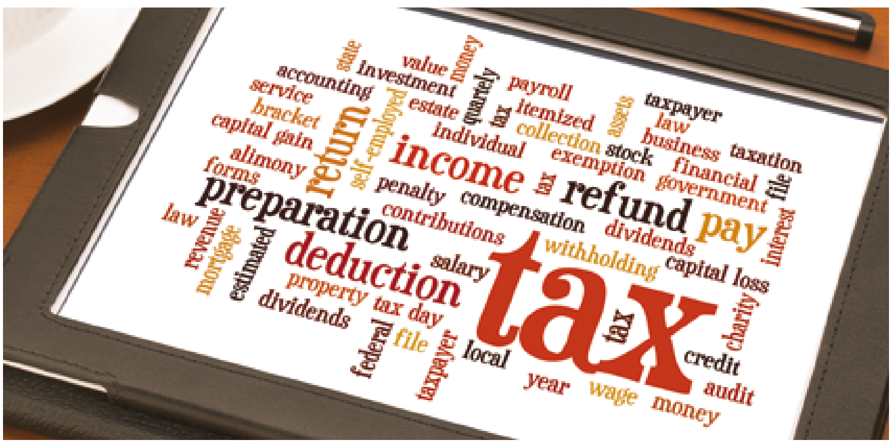
Income Tax )Deduction for Expenditure in Relation to Minimum Wages) Rules 2014 [P.U. (A) 206/2014], gazetted on 14 July 2014, provides a further deduction to qualifying emplyers on the expenditure incurred to pay minimum wages, (i.e. the difference between the orginal salary paid to qualifying emplyee for the month of December 2013, and the minimum wage paid to the same emplyee for the month of January 2014, between the months of January 2014 until December 2014 in that basis period for that year of assessment. The deduction is in addition to the wages to the employee which is allowable for deduction under section 33 of the Act. The Rules take effect from the year of assessment 2014.

### Income Tax (Asset-Backed Securitization) Regulations 2014

Income Tax (Asset-Backed Securitization) Regulations 2014 [P.U.(A) 170/2014], gazetted on 24 June 2014, provide clarification on the tax treatment of the income of an originator and a special purpose vehicle in an asset-backed securitization (ABS) transaction authorised by the Securities Commission. The regulations are deemed to have come into operation from the year of assessment 2013 and refer to ABS transactions authorised by the Securities Commission on or after 1 January 2013.

### Income Tax Leasing (Amendment) Regulations

Income Tax Leasing (Amendment) Regulations 2014 [P.U.(A) 171/2014], gazetted on 24 June 2014, amend the Income Tax Leasing Regulations 1986 [P.U.(A) 131] by inserting a new




Regulation 5 on "Non-application". Based on the new Regulation 5, the Leasing Regulations will not apply to a lease transaction that relates to an ABS transaction authorised by the Securities Commission on or after 1 January 2013. The amendment is deemed to have come into operation from the year of assessment 2013.

### Income Tax (Accelerated Capital Allowance) (Information and Communication Technology Equipment) Rules 2014

Income Tax (Accelerated Capital Allowance) (Information and Communication Technology Equipment) Rules 2014 [P.U.(A) 217/2014], gazetted on 21 July 2014, provide that capital expenditure increased for the purchase (and installation) of information and communication technology equipment (as specified in the Schedule to the Rules) qualifies for 100% capital allowance (made up of an initial allowance of 20% and an annual allowance of 80%) for the years of assessment 2014 to 2016.

### Promotion of Investments (Amendment) Act 2014

The Promotion of Investments (Amendment) Act 2014 (Act A1468) was gazetted on 22 August 2014. The amendments aim to update the Promotion of Investments Act 1986, to reflect policy changes as well as the introduction of new provisions, in respect of incentives granted to promoted activities and products.

### Public Ruling No. 2/2014 – Taxation of investors on income from foreign fund management company

Public Ruling (PR) No. 2/2014 published on 28 April 2014 provides an explanation on the tax treatment of the various types of income which may be received by  foreign or local investors.

### Public Ruling No. 3/2014 – Taxation of limited liability partnership

PR No. 3/2014 published on 3 May 2014 provides a detailed explanation on the tax treatment of a limited liability partnership.

### Public Ruling No. 4/2014: Deferred Annuity

PR No. 4/2014 published on 24 June 2014 explains the deductibility of premiums paid by an individual for deferred annuity, the exemption of annuity income for an individual, and the exemption of income of a life insurer and a takaful operator from an investment made out of a life fund or family fund in respect of deferred annuity.

### Public Ruling No. 5/2014: Ownership and Use of Asset for the Purpose of Claiming Capital Allowances

PR No. 5/2014 published on 27 June 2014 replaces PR No. 1/2001 captioned "Ownership of Plant & Machinery for the purpose of claiming Capital Allowance" issued on 18 January 2001. The PR comprehensively explains the provisions on eligibility to claim capital allowance and the tax treatment.

### Guideline on compensation on late refund of overpayment of tax

The IRB has issued a guideline titled "Guideline on Compensation on Late Refund of Overpayment of Tax' dated 15 May 2014 (GPHDN 1/2014). The guideline provides an explanation on Section 111D of the ITA that was effective from the year of assessment 2013. Under Section 111D of the ITA, taxpayers who file their tax return for a year of assessment by the due date will be eligible for a compensation of 2% per annum on any tax overpaid (to be computed on a daily basis after 90 days from the due date for e-Filing and after 120 days from the due date for manual tax filing).

### Settlement of employees' income tax arrears via CP38 deduction

The IRB has issued a media release dated 2 June 2014 captioned "Instruction to deduct salary (CP38 instruction) for settlement of income tax arrears", to inform all taxpayers earning income from employment sources that an instruction to deduct salary (CP38 Instruction) will be issued to employers for their unpaid taxes. The CP38 instruction directs employers to make additional deductions from the salary of employees (on top of the Monthly Tax Deductions) in order to settle the employees' income tax arrears. The deduction is effective from July 2014 until December 2014.

### Update on Malaysia's DTA with Poland

On 8 July 2013, Malaysia signed a new double tax agreement (DTA) with Poland for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income. This new DTA is intended to replace the original Malaysia – Poland DTA, which was signed on 16 September 1977. On 23 June 2014, pursuant to Section 132(1) of the ITA, the Double Taxation Relief (The Government of the Republic of Poland) Order 2014 [P.U.(A) 168/2014] was gazetted. The new DTA will come into force in the tax year following the calendar year in which the relevant ratification procedures are completed.

### YA 2014 Form C updated

The income tax return form for companies (Form C) has been updated to reflect recent tax law changes. To monitor taxpayers' compliance with the requirement to prepare contemporaneous transfer pricing (TP) documentation, an additional question in Part R (Other Particulars – see R4) of the year of assessment 2014 Form C has been included, wherein the taxpayer has to indicate whether it has prepared TP documentation.

With the introduction of the new Section 99(4) of the ITA wherein an appeal may only be made where a taxpayer is aggrieved by a tax treatment provided in a PR, the requirement to confirm compliance to PRs has been removed from Page 1 of Form C.

## PETROLEUM INCOME TAX

### Guidelines for upstream petroleum industry tax incentive claims

The IRB has issued guidelines captioned "Garis Panduan Tuntutan Insentif Bagi Industri Petroleum Huluan Di Bawah Akta Petroleum (Cukai Pendapatan) 1967" dated 22 May 2014. The guidelines provide clarification on whether chargeable persons undertaking petroleum operations in marginal fields and in fields that require intensive capital investment would qualify for the incentives listed in the guidelines.

## CUSTOMS AND EXCISE DUTIES

### Customs (Anti-Dumping Duties) (Expedited Review) Order 2014 1967 [P.U. (A) 155/2014]

The Order provides for the non-imposition of anti-dumping duties under the Customs (Anti-Dumping Duties) (No.3) Order 2013 [P.U. (A) 339/2013] on imports from Novowell ETP Limited, producer of electrolytic tinplate from the People's Republic of China for the period 5 June 2014 to 12 September 2014 while the expedited review is being carried out.

Customs (Anti-Dumping Duties) (No.3) Order 2013 [P.U. (A) 339/2013] requires importers to pay anti-dumping duties in cash in respect of


the goods specified in the Schedule exported from specified countries into Malaysia by specified exporters at the specified rates. The imposition of anti-dumping duties shall be without prejudice to the imposition and collection of import duties under the Customs Act 1967 and sales tax under the Sales Tax Act 1972 [ Act 64].

Please refer to P.U (A) 339/2013 and 155/2014 for details.

### Customs (Import License Fee for Motor Vehicle) (Amendment) Regulations [P.U. (A) 159/2014]

The Order provides for an amendment in No. 11 of the Schedule to the Customs (Import License Fee for Motor Vehicle) Regulations 2009

[P.U. (A) 491/2009] and is deemed to have come into operation on 18 June 2014.

The Schedule to the Customs (Import License Fee for Motor Vehicle) Regulations 2009 [P.U. (A) 491/2009] lists current import license holders who, by Regulation 2, will be subject to a fee for each unit of motor vehicle imported. The 2014 Amendment substitutes the words "IBM Automobiles Sdn. Bhd." in No. 11 with the words "Ismo Automobiles Sdn. Bhd.".

Please refer to P.U (A) 491/2009 and 159/2014 for details.

### Customs (Amendment) Regulations 2014 [P.U. (A) 160/2014]

The Order provides for an amendment in Regulations 19(1) and 25(3) of the Customs Regulations 1977 [P.U. (A) 162/1977] and is deemed to have come into operation on 1 July 2014.

Regulation 19(1) of the Customs Regulations 1977 [P.U. (A) 162/1977] pertains to the fee chargeable to obtain a license for the importation of intoxicating liquor, tobacco and denatured spirit where such license is obtained on the basis of monthly or six consecutive months issuance. The 2014 Amendment substitutes the words "$10" and "$48" with the words "RM20.00" and "RM96.00" respectively.

Regulation 25(3) of the Customs Regulations 1977 [P.U. (A) 162/1977] pertains to the fee payable by an owner requesting further survey to confirm the quantity of his intoxicating liquors imported after an official application has been made. The 2014 Amendment substitutes the words "$20" with the words "RM40.00".

Please refer to P.U (A) 162/1977 and 160/2014 for details.

### Customs (Prohibition of Imports) (Amendment) (No. 2) Order 2014 [P.U. (A) 172/2014]

The Order provides for an amendment in Part II of the Fourth Schedule to the Customs (Prohibition of Imports) Order 2012 [P.U. (A) 490/2012] and is deemed to have come into operation on 1 July 2014.


Part II of the Fourth Schedule to the Customs (Prohibition of Imports) Order 2012 [P.U. (A) 490/2012] pertains to the conditional prohibition of goods listed from importation except those conforming to the Malaysian Standard and/ or other standards approved by the Malaysian Authorities and in the manner provided and does not apply to the free commercial zones. The 2014 Amendment substitutes the particulars related to items 1 and 2 covering iron and steel products, aluminium products in Part II of the Fourth Schedule with new particulars as listed in Section 2 of the Customs (Prohibition of Imports) (Amendment) (No. 2) Order 2014.

Please refer to P.U (A) 490/2012 and 172/2014 for details.

### Customs (Amendment) (No. 2) Regulations 2014 [P.U. (A) 218/2014]

The Order provides for an amendment in Regulation 3(1), Regulation 3(4) and Part I of the First Schedule within the Customs Regulations 1977 [P.U. (A) 162/1977] and is deemed to have come into operation on 1 August 2014.

Regulation 3(1) of the Customs Regulations 1977 [P.U. (A) 162/1977] pertains to the ordinary hours during which customs offices and warehouses are opened to the public. The 2014 Amendment inserts a line detailing the operating hours of the office located at the Teluk Rubiah Maritime Terminal, Perak to be 24 hours on any day.

Regulation 3(4) of the Customs Regulations 1977 [P.U. (A) 162/1977] pertains to the ordinary hours during which goods other than personal effects of bona fide travellers can be loaded, unloaded or shipped. The 2014 Amendment inserts a line detailing the ordinary hours for such activity at the Teluk Rubiah Maritime Terminal, Perak to be 24 hours on any day.

Part I of the First Schedule to the Customs Regulations 1977 [P.U. (A) 162/1977] represents a list of recognised customs ports and legal landing places within the States of Malaya. The 2014 Amendment recognises Teluk Rubiah, Perak as such a port with details of goods and legal landing place given as per Regulation 3 of the Customs (Amendment) (No. 2) Regulations 2014.

Please refer to P.U (A) 162/1977 and 218/2014 for details.

### Customs (Amendment) (No. 3) Regulations 2014 [P.U. (A) 235/2014]

The Order provides for an amendment in Regulation 3(6) and Part VI of the First Schedule to the Customs Regulations 1977 [P.U. (A) 162/1977] and is deemed to have come into operation on 15 August 2014.

Regulation 3(6) of the Customs Regulations 1977 [P.U. (A) 162/1977] pertains to the ordinary hours during which goods, other than the personal effects of bona fide travellers which are not deposited in a customs warehouse may be removed from customs control. The 2014 Amendment inserts a line detailing the ordinary hours at Nilai Inland Port to be 24 hours on any working day.


Part VI of the First Schedule to the Customs Regulations 1977 [P.U. (A) 162/1977] pertains to a listing of Inland Clearance Depots as recognised by Customs in Malaysia. The 2014 Amendment substitutes the particulars relating to the word "Seremban" with the particulars as prescribed in Regulation 3 of the Customs (Amendment) (No. 3) Regulations 2014.

Please refer to P.U (A) 162/1977 and 235/2014 for details.

### Customs Duties (Exemption) (Amendment) Order 2014 [P.U. (A) 236/2014]

The Order provides for an amendment in item 66, Part I of the Schedule to the Customs Duties (Exemption) Order 2013 [P.U. (A) 371/2013].

Part I of the Schedule to the Customs Duties (Exemption) Order 2013 [P.U. (A) 371/2013] pertains to persons exempted from paying customs duty on the goods specified. The 2014 Amendment inserts into item 66 a new line item "(xvi) Hess Exploration and Production Malaysia B.V.".

Please refer to P.U (A) 371/2013 and 236/2014 for details.

## GOODS AND SERVICES TAX

### Appointment of Effective Date for Imposition of Goods and Services Tax [P.U. (B) 320/2014]

The Effective Date for Imposition of GST, which was published in the Government Gazette on 30 June 2014, shall come into operation on 1 April 2015.

Please refer to P.U (B) 320/2014 for details.

### Goods and Services Tax (Amount of Taxable Supply) Order 2014 [P.U. (A) 183/2014]

The GST (Amount of Taxable Supply) Order 2014 which was published in the Government Gazette on 30 June 2014 and came into operation on 1 July 2014, states that the amount of taxable supply for the purpose of registration under subsection 20(1) of the GST Act 2014 shall be five hundred thousand ringgit.

Please refer to P.U (A) 183/2014 for details.

### Goods and Services Tax (Rate of Tax) Order 2014 [P.U. (A) 184/2014]

The GST (Rate of Tax) Order 2014 which was published in the Government Gazette on 30 June 2014 and that came into operation on 1 July 2014, states that the rate of tax shall be fixed at six per cent on the supply of goods or services or on the importation of goods.

Please refer to P.U (A) 184/2014 for details.

### Goods and Services Tax (Application to Government) Order 2014 [P.U. (A) 185/2014]

The GST (Application to Government) Order 2014 which was published in the Government Gazette on 30 June 2014 and came into operation on 1 July 2014, provides that the supply of scheduled goods or services by the Government (Federal Government and State Government) is subject to the provisions of the GST Act 2014.

Please refer to P.U (A) 185/2014 for details.

### Goods and Services Tax (Tax Agent Application Fee) Order 2014 [P.U. (A) 186/2014]

The Goods and Services Tax (Tax Agent Application Fee) Order 2014 which was published in the Government Gazette on 30 June 2014 and came into operation on 1 July 2014 provides that the fee for the application or renewal of an approved tax agent status under subsection 170(2) or (4) of the GST Act 2014 shall be two hundred ringgit.

Please refer to P.U (A) 186/2014 for details.

### Goods and Services Tax (Imposition of Tax for Supplies in respect of Designated Areas) Order 2014 [P.U. (A) 187/2014]

The GST (Imposition of Tax for Supplies in respect of Designated Areas) Order 2014 which was published in the Government Gazette on 30 June 2014 and came into operation on 1 July 2014, states that tax shall be imposed at the rate fixed under subsection 10(1) of the GST Act on the following:

(a) The supply of petrol, diesel and liquefied petroleum gas within or between the designated areas or the importation of such goods into the designated areas

(b) Freight services supplied between designated areas

(c) Telecommunication services supplied within or between designated areas

(d) The importation of cement, marble or rubber into Langkawi; and

(e) The supply of motor vehicle to or within, or the importation of motor vehicles into, Tioman

Please refer to P.U (A) 187/2014 for details.

### Goods and Services Tax (Advance Ruling) Regulations 2014 [P.U. (A) 188/2014]

The GST (Advance Ruling) Regulations 2014 which were published in the Government Gazette on 30 June 2014 and that came into operation on 1 July 2014, are aimed at providing greater clarity and certainty to taxpayers. They provide written interpretations on how specific provisions of the GST Act 2014 will apply for a particular business arrangement or a specific transaction.

Please refer to P.U (A) 188/2014 for details.

### Goods and Services Tax (Review and Appeal) Regulations 2014 Goods and Services Tax Act 2014 [P.U. (A) 189/2014]

The GST (Review and Appeal) Regulations 2014 which were published in the Government Gazette on 1 July 2014 and came into operation on the same day, set out the review and appeal procedures under the GST Act 2014.

Please refer to P.U (A) 189/2014 for details.

### Goods and Services Tax Regulations (GSTR) 2014 [P.U. (A) 190/2014]

The GSTR 2014 were published in the Government Gazette on 1 July 2014 .

- Regulations 11 and 12 and Parts VI,VIII,IX and X will come into operation on 1 April 2015
- Other regulations not mentioned above came into operation on 1 July 2014

Please refer to P.U (A) 190/2014 for details.

*Contributed by **Ernst & Young Tax Consultants Sdn. Bhd.** The information contained in this article is intended for general guidance only. It is not intended to be a substitute for detailed research or the exercise of professional judgement. On any specific matter, reference should be made to the appropriate advisor.*

# OTHER BUSINESS DEDUCTIONS

## Annual General Meetings

Siva Subramanian Nair

In this article we shall look at the tax treatment of expenditure relating to annual general meetings, printing of financial accounts and the listing of a company in the stock exchange.


Candidates will remember that that the general rule in S33(1) on deductibility of expenditure requires evidence that it bears a relationship to the production of income from that source, during that period.

The first matter for discussion is expenditure relating to annual general meetings. There is no argument that expenses for directors' meetings are deductible but those for the annual general meetings with shareholders' has raised a contention.

This issue arose in the case of *Sharikat KM Bhd v DGIR (1972) 1 MLJ 224* which is discussed in **Table 1**.

### FACTS OF THE CASE

The Revenue disallowed the above expenditure but based on a concessionary agreement with the

**Table 1**

The appellant company had the sole business of letting out its five shop houses. They had incurred the following expenditure;

| | | |
|---|---|---|
| a) | postage for sending out notices of general meeting | $100.00 |
| b) | printing of notices of general meeting, minutes of previous meetings, directors' report and statement of accounts | $360.00 |
| c) | cost of nasi briani for shareholders attending the general meeting *(this cost was excluded upon appeal to the courts)* | $300.00 |
| | | $760.00 |

taxpayer, allowed a nominal sum of $208. The taxpayer appealed on grounds that as a company it is required by law to hold an annual general meeting at which the appointment of its various officers have to be made and many other matters have to be discussed and decisions taken thereon, without which the company cannot exist for long. They argued that in considering the expenses incidental to the holding of such a meeting, a lenient and liberal approach should be made by the Revenue authorities

## DECISION OF THE COURT

The Special Commissioners (and the High Court upon appeal) held that the above expenditure were not deductible. This conclusion was drawn based on the following premise:

- they were not wholly and exclusively incurred in the production of income
- i.e. they are incurred after the income has been produced (normally after the financial year-end, the accounts are finalised, an audit is performed, any necessary adjustments are effected, the finalised audited accounts are printed and only then an AGM is held; so it is after the production of income for that basis period)
- they cannot be regarded as an integral part of the income-earning process of the company
- the fact that it is a legal requirement to hold an annual general meeting is not relevant.

The Special Commissioners found support in Lord Davey's dictum in *Strong and Cos of Romsay Ltd v Woodifield 5 TC 215, 220)*

It is not enough that the disbursements is made in course of, or arises out of, or is connected with, the trade or is made out of the trade. It must be made for the purposes of earning the trade.


However, some other tax pundits have held the view that annual general meetings is an expense wholly, exclusively and even necessarily incurred in the production of income. They argue that it is part of the company's working expenses, albeit that by no stretch of imagination can it be regarded as an integral part of the profit earning process of the company, BUT it is also not capital in nature, and accordingly should rank for a deduction in ascertaining the adjusted income of the company.

However, it is advisable for candidates to ignore this dissenting view and adopt the general consensus that expenditure relating to annual general meetings is not deductible. This is the stand taken by the panel of Examiners of the Institute as is evident in the following examples of past year questions.

***Tax IV D13 Question 2(i)***

Powerpack Bhd had its annual general meeting which was attended by 100 shareholders. After the meeting, the company organised a lunch for the shareholders and 45 employees of the company. The lunch was also to celebrate the company's 25th anniversary. The cost of the annual general meeting was RM18,000 and the lunch cost RM26,000.

***SOLUTION***

Generally, expenses connected with the AGM are not deductible since they are not incurred in the production of gross income under S33(1). So the RM18,000 is not deductible. *Syarikat KM Bhd v DGIR.* The lunch expense could be considered an entertainment expense. Since it is not related to sales and the entertainment to the employees was merely incidental to the provision of entertainment to others, i.e. the shareholders, only 50% (RM13,000) is deductible. S39(1)(l)

***Tax V J13 Question 5(b)***

A similar stand was adopted whereby annual general meeting expenses of RM 50,000 were disallowed in arriving at the adjusted income

***Tax II J13 Question 1***

Here the figure for "refreshments for shareholders attending the Annual General Meeting" amounting to RM35,500 was added back to the profit before tax figure as an indication of non–deductibility

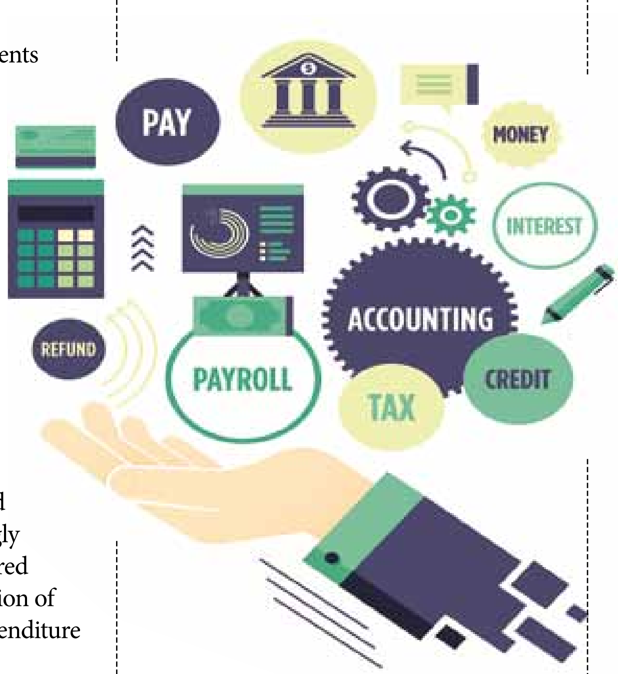
Another issue is the printing of final accounts.

## PRINTING OF FINANCIAL ACCOUNTS

As indicated earlier, the final accounts are printed after the end of the basis period and accordingly the printing expense is not incurred during the period in the production of income. In consequence, the expenditure does not rank for a deduction in arriving at the adjusted income of the company for the basis period. However a counter argument (i.e. that it should be deductible) would be that the printed accounts are also sometimes distributed to clients and business associates as a corporate document which may be said to be assist the income-earning process.

However an interesting point to note is that printing and stationery is included in the list of permitted expenses for investment holding companies, unit trust and close-end funds. That listing is not influenced by the non-deductibility of this item for business purposes. The only restriction affecting the claim for the permitted expenses is the fact that the expenditure should not rank for a deduction under S33(1) i.e. it should not be an expense which is directly attributable to the generation of any particular source of income. Therefore the printing of financial accounts should be included in computing the permitted expenses under S60F for investment holding companies, S60H for unit trust and S63B for close-end funds.

However, if the question relates to a listed investment holding company or a real estate investment trust then the treatment will be different. This is




because all income (for the former) and rental income (for the latter) constitutes business income and accordingly business deduction rules will apply i.e. printing of financial accounts will not be deductible.

Candidates can get a good example by looking at the ACCA Paper P6(MYS) December 2012 Question 1 which can be viewed at the *accaglobal* website. However, the issue in this question was not printing of financial accounts but on secretarial fees, but this is another item which is included as a permitted expense but which would not rank for a deduction against business income. (Note that although a restricted deduction for secretarial fees was announced in the 2014 Budget but the gazette order has not been issued yet and therefore for exam purposes we treat it as not deductible.)

Another expenditure for which a deduction is not allowed is expenses incurred by a company to be listed on the Bursa Malaysia. This is an expenditure which has the features of an enduring benefit, offers a long term privilege to the company and since companies don't get listed and unlisted on a recurring basis, it is obviously a capital expenditure not qualifying for a deduction in ascertaining the adjusted income of the company.

This concludes our discussion on the deductibility of annual general meeting expenses, cost of printing of financial accounts and the listing expenses of a company.

*Siva Subramanian Nair is a freelance lecturer. He can be contacted at sivasubramaniannair@gmail.com*

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# CONTINUING PROFESSIONAL DEVELOPMENT (CPD)

## CPD Events: OCTOBER – DECEMBER 2014

| Month /Event | Details | | | | Registration Fee (RM) | | | CPD Points |
|---|---|---|---|---|---|---|---|---|
| | Date | Time | Venue | Speaker | Member | Member's Firm Staff | Non - Member | |
| **OCTOBER 2014** | | | | | | | | |
| Workshop: GST Transitional Issues | 8 Oct | 9a.m. – 5p.m. | Johor Bahru | Thenesh Kannaa | 335 | 385 | 435 | 8 WS/046 |
| Workshop: GST Transitional Issues | 15 Oct | 9a.m. – 5p.m. | Penang | Thenesh Kannaa | 335 | 385 | 435 | 8 WS/047 |
| Workshop 2: Employment Income *(In collaboration with MAICSA)* | 16 Oct | 9a.m. – 5p.m. | Kuala Lumpur | Vincent Josef | 350 | 400 | 450 | JV/016 |
| Workshop 3: Allowances & Deductions *(In collaboration with MAICSA)* | 28 Oct | 9a.m. - 5p.m. | Kuala Lumpur | Vincent Josef | 350 | 400 | 450 | JV/017 |
| 2015 Budget Seminar | 29 Oct | 9a.m. – 5p.m. | Kuala Lumpur | MoF, IRBM, RMC, CTIM | 350 | 400 | 450 | 10 BS/001 |
| GST Training Course (6-days) GST Examination Day *(subject to RMC confirmation)* | Oct: 12, 13, 14, 19, 20, 21 TBC | 9a.m. – 5p.m. | Subang | Royal Malaysian Customs | 2,200 *(fee for 6 days course)* | 2,700 *(fee for 6 days course)* | 3,000 *(fee for 6 days course)* | JV/015 |
| GST Training Course (6-days) GST Examination Day *(subject to RMC confirmation)* | Oct: 17, 18, 19, 31 Nov: 1, 2 TBC | 9a.m. – 5p.m. | Johor Bahru | Royal Malaysian Customs | 2,200 *(fee for 6 days course)* | 2,700 *(fee for 6 days course)* | 3,000 *(fee for 6 days course)* | JV/012 |
| GST Training Course (6-days) GST Examination Day *(subject to RMC confirmation)* | Oct: 31 Nov: 1, 2, 7, 8, 9 TBC | 9a.m. – 5p.m. | Kota Kinabalu | Royal Malaysian Customs | 2,200 *(fee for 6 days course)* | 2,700 *(fee for 6 days course)* | 3,000 *(fee for 6 days course)* | JV/013 |
| **Public Holiday** ***(Hari Raya Aidiladha: 5 Oct, Deepavali: 22 Oct, Awal Muharram: 25 Oct)*** | | | | | | | | |
| **NOVEMBER 2014** | | | | | | | | |
| Workshop 4: Special Topics (I) *(In collaboration with MAICSA)* | 4 Nov | 9a.m. - 5p.m. | Kuala Lumpur | Vincent Josef | 350 | 400 | 450 | 8 JV/018 |
| 2015 Budget Seminar | 17 Nov | 9a.m. - 5p.m. | Melaka | IRBM, CTIM | 350 | 400 | 450 | 10 BS/002 |
| 2015 Budget Seminar | 18 Nov | 9a.m. - 5p.m. | Subang | IRBM, CTIM | 350 | 400 | 450 | 10 BS/003 |
| 2015 Budget Seminar | 18 Nov | 9a.m. - 5p.m. | Kota Kinabalu | IRBM, CTIM | 350 | 400 | 450 | 10 BS/004 |
| 2015 Budget Seminar | 19 Nov | 9a.m. - 5p.m. | Kuching | IRBM, CTIM | 350 | 400 | 450 | 10 BS/005 |
| 2015 Budget Seminar | 19 Nov | 9a.m. - 5p.m. | Kuantan | IRBM, CTIM | 350 | 400 | 450 | 10 BS/006 |
| 2015 Budget Seminar | 20 Nov | 9a.m. - 5p.m. | Penang | IRBM, CTIM | 350 | 400 | 450 | 10 BS/007 |
| 2015 Budget Seminar | 25 Nov | 9a.m. - 5p.m. | Johor Bahru | IRBM, CTIM | 350 | 400 | 450 | 10 BS/008 |
| 2015 Budget Seminar | 27 Nov | 9a.m. - 5p.m. | Ipoh | IRBM, CTIM | 350 | 400 | 450 | 10 BS/009 |
| Workshop 5: Special Topics (II) *(In collaboration with MAICSA)* | 27 Nov | 9a.m. - 5p.m. | Kuala Lumpur | Vincent Josef | 350 | 400 | 450 | JV/019 |
| **DECEMBER 2014** | | | | | | | | |
| 2015 Budget Seminar | 2 Dec | 9a.m. - 5p.m. | Kuala Lumpur | IRBM, CTIM | 350 | 400 | 450 | 10 BS/010 |
| GST Training Course (6-days) GST Examination Day *(subject to RMC confirmation)* | Dec: 5, 6, 7, 12, 13, 14 TBC | 9a.m. - 5p.m. | Kuala Lumpur | Royal Malaysian Customs | 2,200 *(fee for 6 days course)* | 2,700 *(fee for 6 days course)* | 3,000 *(fee for 6 days course)* | JV/014 |
| **Public Holiday** ***(Christmas: 25 Dec)*** | | | | | | | | |

DISCLAIMER : CTIM reserves the right to change the speaker (s)/date (s), venue and/or cancel the events if there are insufficient number of participants. A minimum of three days notice will be given.

ENQUIRIES : Please call Yus, Jason, Ally or Nur at 03-2162 8989 ext 121, 108, 123 and 106 respectively or refer to CTIM's website ***www.ctim.org.my*** for more information on the CPD events.


What makes your world better?
For some, it's the thrill of bringing dreams to life
For some, it's the wonder of discovering new things
For some, it's the warmth of a helping hand when in need
While others just want to be loved
We all seek different things
But as priorities change with time
It's nice to know that one thing remains
And that's our promise:
To always keep the light on
To keep the energy flowing
To make it all happen
For you
For the planet
For our tomorrow
To make everyone's search for better
A much brighter one
Better. Brighter.
Watch the Better. Brighter. film on youtube.com/TENAGAofficial
TENAGA NASIONAL BERHAD (200866-W)